Shareholders' duties must be clarified to enable enlightened capitalism

As we enter AGM season, all eyes will be on the investor community, as politicians from across the spectrum focus on shareholder oversight as the answer to so-called 'crony capitalism'. If the hopes being pinned on investors are to be fulfilled, attention must turn to an aspect of the law which is pushing in precisely the wrong direction.

Legal duties which exist to protect savers have been distorted and misunderstood to the point where they risk doing the opposite. Company directors have duties designed to encourage the pursuit of 'enlightened shareholder value'. But this is undermined by a widespread perception that fiduciary shareholders are legally obliged to be unenlightened. Their duty to act in the best interests of savers is widely seen as a duty to focus solely on the maximisation of short-term returns, ignoring anything that cannot immediately be monetised. The folly of such an approach has been amply demonstrated by the banking crisis.

This interpretation is at best simplistic and at worst a myth with scant basis in law. Yet it remains deeply entrenched in the advice received by pension fund trustees and other major investors. We welcome Professor John Kay's recognition of this as an issue in his interim report on the state of UK equity markets. If politicians are serious about encouraging a more far-sighted and responsible capitalism, they must remove this perceived legal barrier. Legal clarification is needed to confirm that fiduciary investors may act as responsible and enlightened market participants in the pursuit of sustainable value creation – thus enabling them to better serve their beneficiaries' true best interests.

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