UK Ownership and Control: A Transformational Analysis

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ABSTRACT
This study presents a transformational analysis of corporate ownership and control in the UK. Using a sample of 643, UK listed non-financial companies and relying on data from the Office for National Statistics, this analysis revealed a declining ownership by major institutional domestic ownership coupled with an increase in foreign ownership. The study further found 42% of UK companies having multiple large shareholders and that about 40% of the sampled firms separated cash flow-rights from control-rights, confirming the presence of controlling block holders. This is contrary to the traditional understanding that UK ownership structure is dispersed. These findings are significant given the little attention in literature examining corporate ownership and control structures of corporations in the UK.

Key words: Ownership structure, Institutional ownership, cash flow rights, control rights

INTRODUCTION

The 20th century has witnessed a decline in individual ownership and significant growth of institutional ownership. In his book Cheffins (2008), reveals that in post-World War II period, UK institutional investors faced some difficulties when investing stocks and were discouraged due to lack of sufficient investor protection. In spite of these difficulties, a the promise of superior returns relative to other options made shareholding in UK companies an attractive option. In this article, we analyse the trends of corporate ownership and control among UK companies. This article focuses on the UK for several reasons: First, the UK is a developed market and has relatively better investor protection measures than most European countries. Secondly, according to Laeven and Levine (2008), about 40% of the Western European firms have their roots in the UK. Thirdly, the level of disclosure for UK companies is relatively higher compared to most European countries and thus data is more readily available. Indeed accessibility of data is a pertinent issue and can at times be frustrating. Faccio and Lang (2002) when tracing the ultimate ownership of unlisted companies of the companies in Western Europe, also single out UK as benign choice; "Where the ultimate owner of a corporation is an unlisted firm, we tried to trace its owners using all available data sources. We had incomplete success because most of our sample countries do not require

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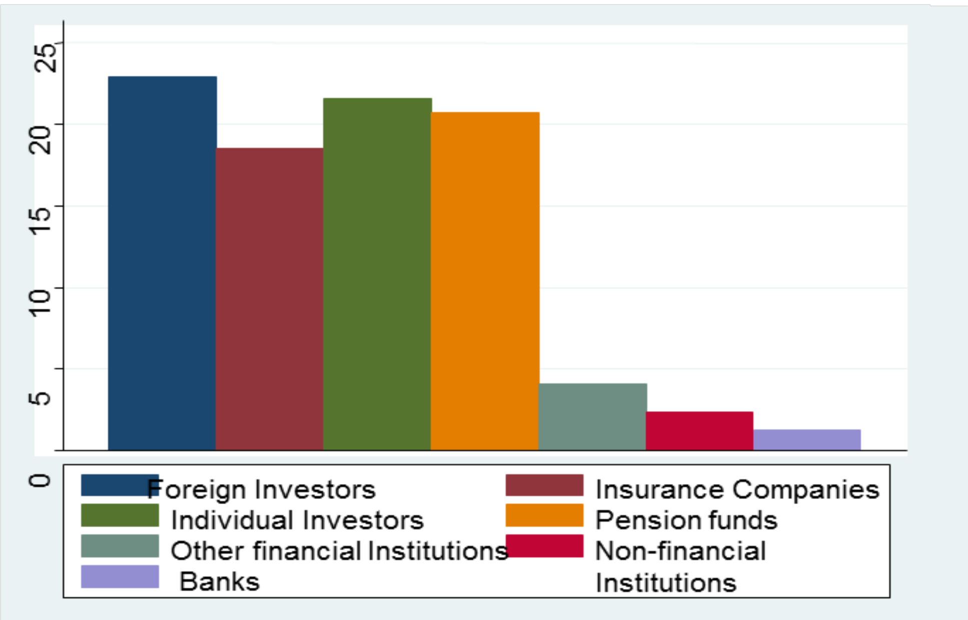
unlisted firms to disclose their owners. One exception is the UK, where the 3% disclosure rule also applies to unlisted firms" (p.373)

The UK equity market has recently witnessed a decline in equity ownership by local institutional investors and a rapid increase in foreign ownership (Office for National Statistics, 2012). According to statistics, ownership by UK pension funds fell from 17.2% in 2004 to 13.4% at the end of 2010 while ownership by UK insurance companies declined from 15.7% in 2004 to 8.6 % in 2010. Within the same period, foreign ownership increased from 36.3% in 2004 to 41.2% in 2010, (see figure 1 below). On average since 1963 to 2010, the percentage of ownership by foreign investors has been on the increase. Furthermore, contrary to the traditional belief that listed firms in the UK have dispersed ownership structures, Leaven and Levine (2008) reported a surprise finding where in a sample of 689 listed companies in UK about 75% of them had either multiple large shareholders or one large shareholder. Leaven and Levine (2008) specifically report that 26.7% of firms have no controlling owner, and 42.8% have one controlling owner while 30.5% of the sample represents companies with multiple large shareholders.

Ownership structure, which was previously characterised as dispersed, has now become more concentrated. Previously, most large public companies operating in London Stock Exchange had ownership of shares widely dispersed but it appears this changed. According to Cheffins (2008), transfer of ownership from individual shareowners to institutional investors has occasioned the shift.

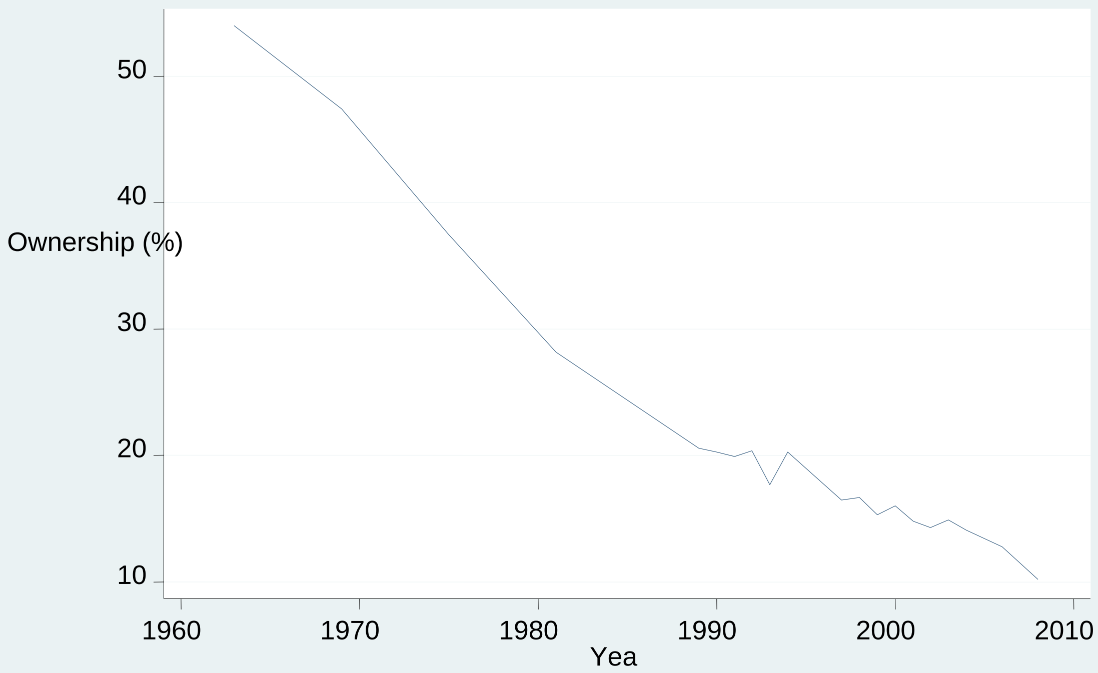
FIGURE 1:
UK Average Ownership Distribution among Different Owners' Identities 1963-2010



Source: Data sourced from office for National Statistics; Ownership Statistics Bulletin (2010)

The trend of share ownership as described in National Office for Statistics bulletin (2010) reveal that since 1963, individual shareholding has been falling. Several factors have been associated with this trend and two seem to be more relevant. The first factor is the wave of privatization that evolved in the early 1990s. Secondly, the demutualization of most building societies in the UK appears to have catalysed the exit of individual shareholders'. These factors among others are suspected to have significantly contributed to the sustained downward trend of individual stakes from 54% in 1963 to around 11% in 2010, which reflected in figure 2.

FIGURE 2
Individual Ownership Distribution (1963-2010)

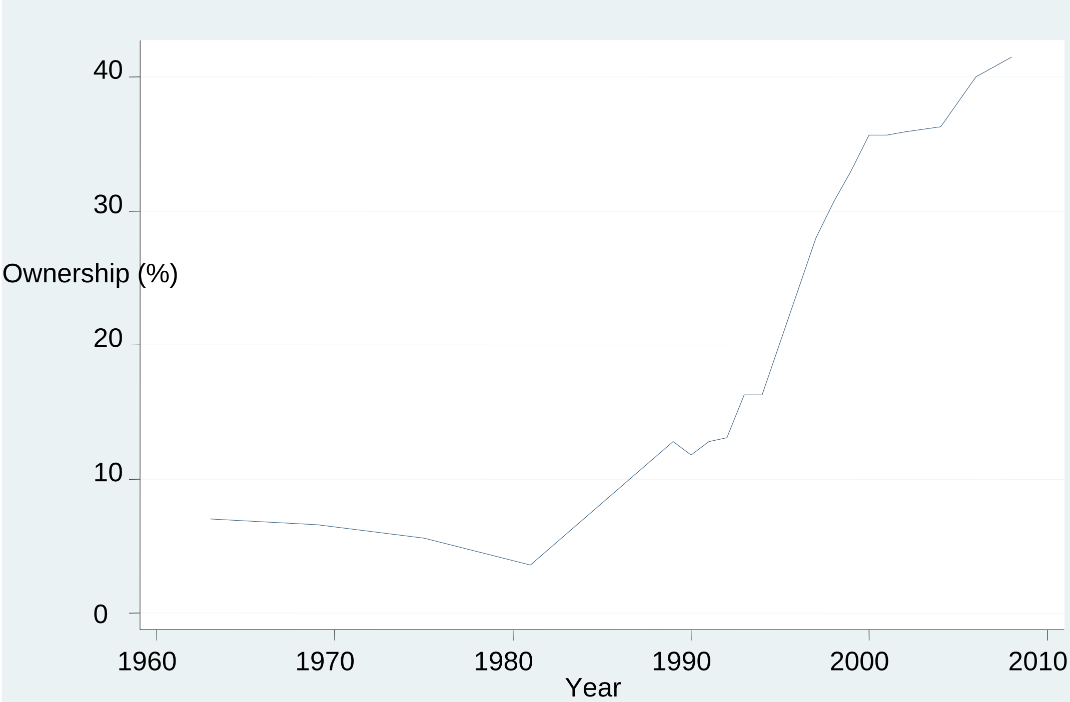


SOURCE: **Data sourced from Office for National Statistics, Ownership Statistics Bulletin (2010)**

In the last two decades, European capital markets have witnessed a loosening of restrictions in the operational environments, for example restriction on capital exports. According to Hurtsi (2006), in earlier periods foreign ownership of share was either strictly prohibited or restricted to shares without voting rights. Since then, major changes have taken place and investors can now invest across borders. In figure 3 below, we note that over the last 20 years, the proportion of UK shares owned by foreigners increased substantially from 4 per cent in 1981 to about 16 per cent in 1994, a four-fold increase.

It will be noted that as individual shareholdings continued to decrease, institutional ownership was on the rise. A more interesting observation is the increase in foreign ownership. In an ownership survey, the Office for National Statistics reported that by 2000 foreign share ownership shot up significantly to 35.7 per cent, which had risen to around 41 per cent in 2010.

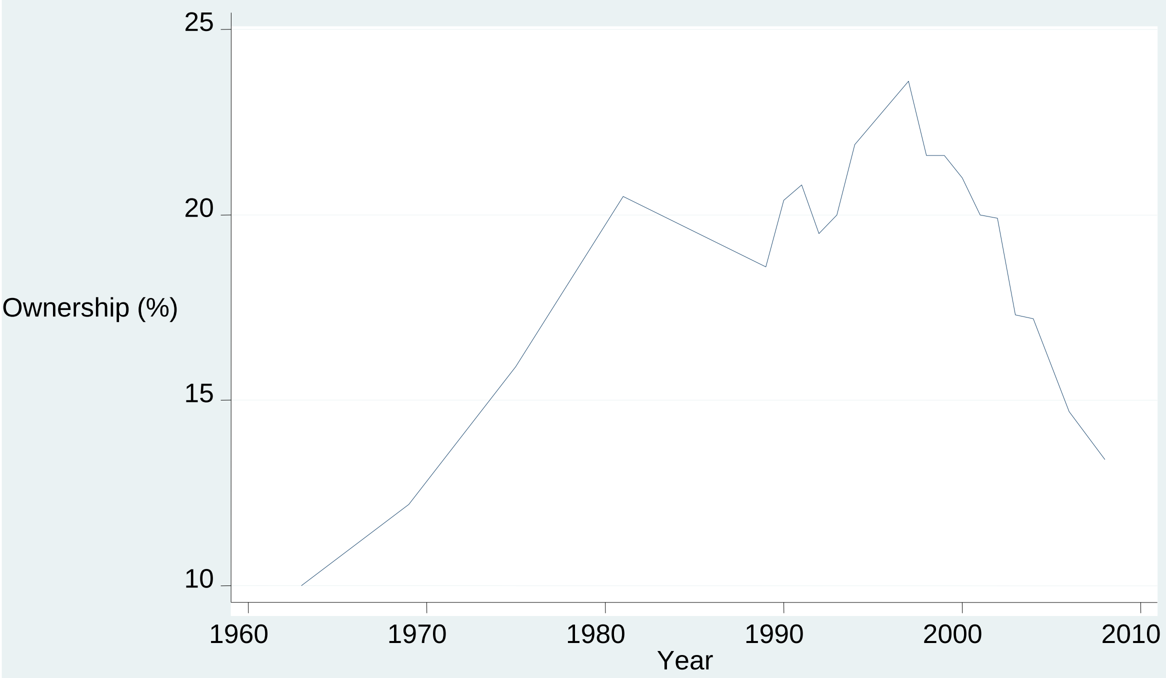
FIGURE 3
Foreign Ownership Distribution (1963-2010)



SOURCE: **Data sourced from Office for National Statistics, Ownership Statistics Bulletin (2010)**

According to the Office of National Statistics report, investors from North America dominated foreign investors investing in UK companies contributing about 56% per cent of foreign investment. Within the same period European holdings of UK shares dropped from 38% in 2001 to 28% at the end of 2010. According to Mallin (2007), most foreign investors are US-based and the rapid increase in foreign investment has begun to influence the behaviour of UK investors by enhancing the investor activism because US investors have more concerns on corporate governance issues. While this is happening for foreign investors, UK institutional shareholding is on the downward side. The proportion of share held by insurance companies shot up by 7% from 1963 to 2004.The figure started dropping by 1% since 2000 up to 2002, the drop became more significant in 2003, and from 2004 to 2010, the drop was by about 4%. This is ilusrated in figure 4 below.

FIGURE 4
Insurance Ownership Distribution (1963-2010)

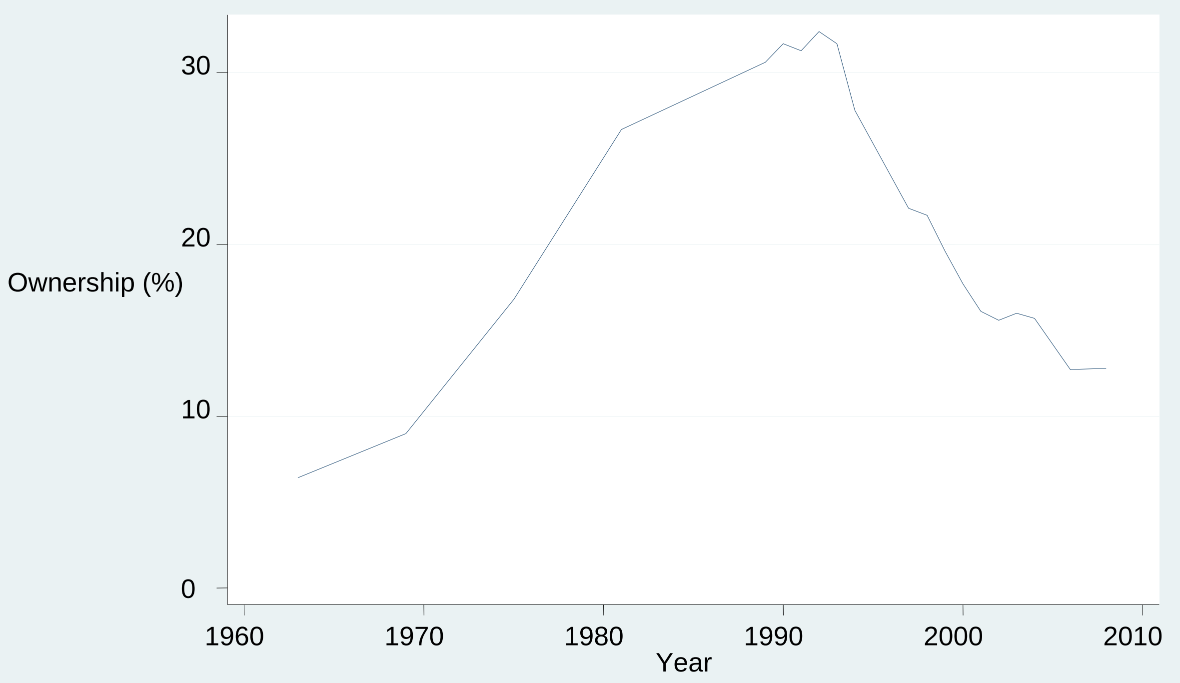


SOURCE: **Data sourced from Office for National Statistics, Ownership Statistics Bulletin (2010)**

This decrease in ownership by insurance companies is associated to several factors. According to Cheffins, (2008), some regulations and market factors are responsible for this down turn. The regulatory changes in 2004 by UK Financial Securities Authority on the treatment of life insurer's assets and liabilities was one of the key factor which accelerated the noted drop of equity ownership by insurance companies. Different from traditional accounting treatment where investment assets were valued in such a manner that they fluctuate with market value while liabilities do not, current accounting treatments require also liabilities to vary with market value to benefit the insured. The new form of accounting treatment is less attractive for insurers' because they have to provide for implied future obligation to pay more obligations in a potential market downturn. Speculatively, this could be the major reason why insurance companies became equity net sellers in the 2000-2003 stock market downturn noted by Cheffins (2008).

A similar situation was replicated by pension funds where the decrease from 2004 hit the same level of around 4%. As for pension funds, the change in treatment of dividends received by pension funds in regards to tax and the drift to liability-driven investments in 2005 where assets and liabilities associated with the pension schemes ought to be matched by investment managers. As Cheffins,(2008) notes, this is contrary to the practice of the 1990s where dividends received by pension funds were tax exempt. The abolishment of this tax free dividends incentive in 1997 amounted to a shift of pension funds from equities investments, which is reflected in figure 5.

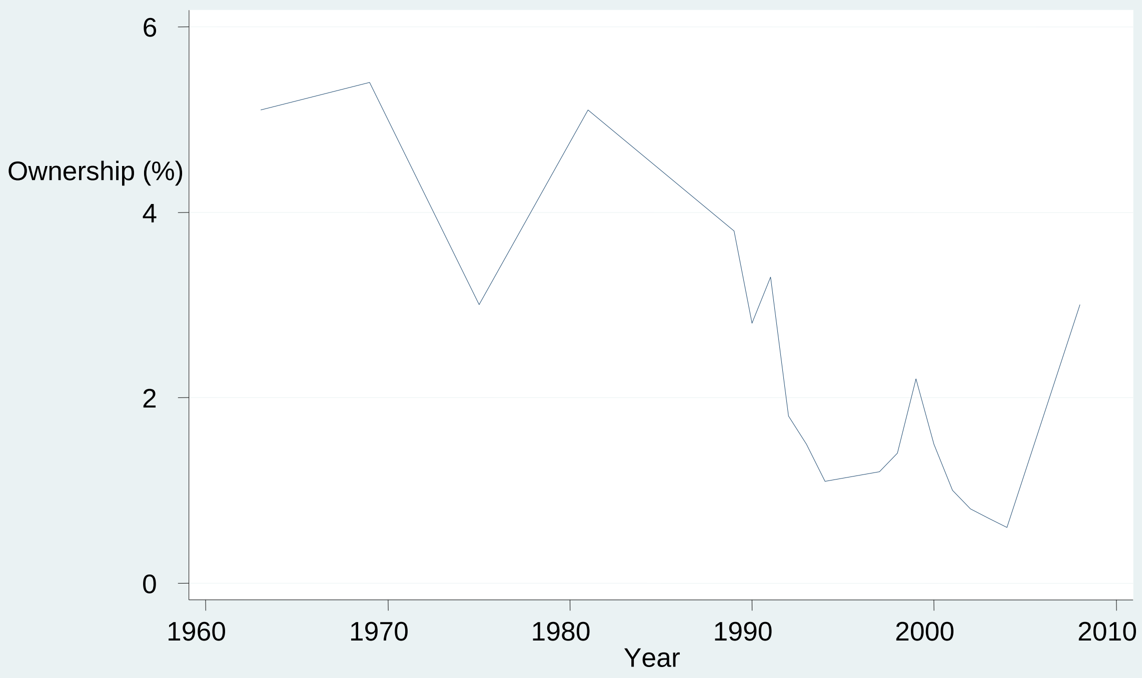
FIGURE 5
Pension Fund Ownership Distribution (1963-2010)



SOURCE: **Data sourced from Office for National Statistics, Ownership Statistics Bulletin (2010)**

Uniquely non-financial institutions have experienced no specific trend up to 2004 where the level of their ownership have been linearly increasing until 2010 .Overall, the foreign investors shareholdings and other financial institutional ownership have been increasing while UK institutional share ownership has been decreasing. This trend is shown in figure 6 below. On the other hand, ownership by banks has also been increasing and in 2008, the level of ownership of banks has shot to 3.5% and dropped down in 2010 to 2.5%, details of which are shown in figure 7.

FIGURE 6
Non-Financial Institutions Ownership Distribution (1963-2010)

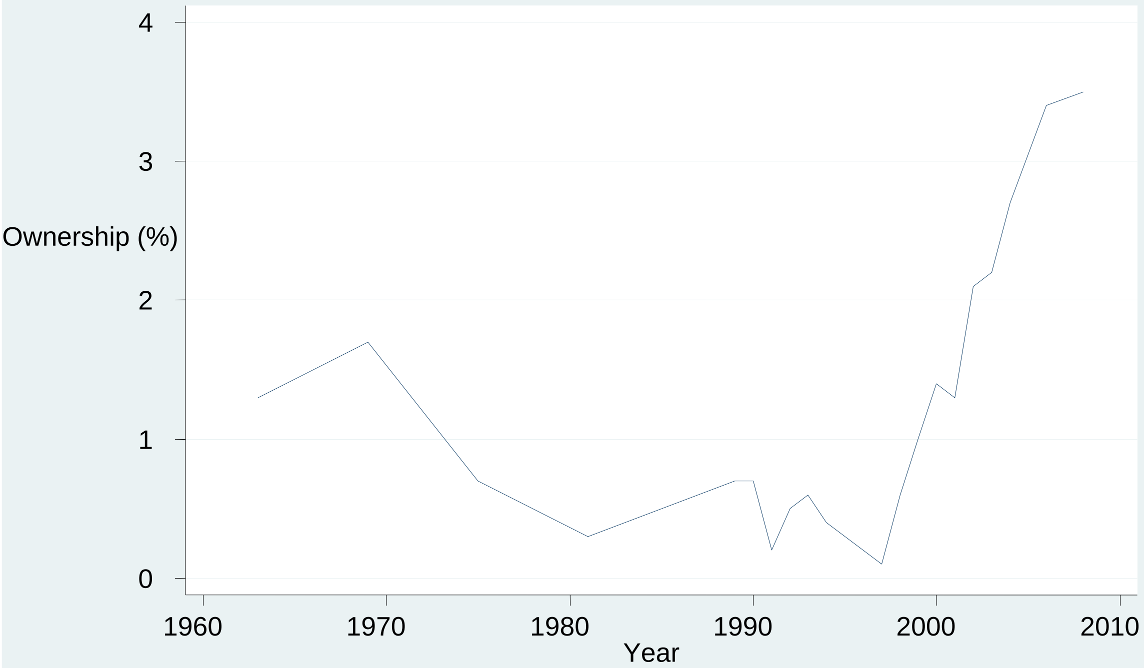


SOURCE: **Data sourced from Office for National Statistics, Ownership Statistics Bulletin (2010)**

TRANSFORMATION OF UK OWNERSHIP AND CONTROL

Previous studies have consistently shown that the UK ownership structure is more dispersed relative to other European countries. Recent literature, however, indicates a change of UK ownership structure from dispersed to concentrate. According to Marchica and Mura (2005), more than 10% of firms in UK are controlled through complex structures and the degree of departure of control-rights from cash-flow rights is reported to be around 11% at a 10% threshold. It is, therefore, hard to doubt that the presence of complex control structures may be being used by controlling shareholders to expropriate the interests of minority shareholders in the UK. Using a sample of 643 UK listed non-financial companies; this study reveals that ownership in the UK is more complex than considered by most previous ownership studies. The study reveals that, 42% of UK companies have multiple large shareholders and about 40% of the sample firms separate cash flow-rights from control-rights, confirming the presence of controlling block holders. This is contrary to the orthodox and extant belief that UK ownership structure is dispersed.

FIGURE 7
Banks Ownership Distribution (1963-2010)



SOURCE: **Data sourced from Office for National Statistics, Ownership Statistics Bulletin (2010)**

Ownership Characteristics

Table 1 shows the distinguished ownership structure based on shareholders' voting rights. An owner was said to be ultimate if he/she owned over 20 per cent of company's direct or indirect voting rights. The alternative cut-off of 10 per cent has also been conventionally used in literature and both criteria provide significant thresholds of votes (Faccio & Lang, 2002; La Porta *et al*, 1999). If a company had no shareholder holding more than 20% of equity ownership, it was classified as a widely held company. In their recent study on complex ownership and valuation, Laeven and Levine (2008) have used a similar approach to classify ownership holding. The types of ownership applied in this study and defined by Faccio and Lang (2002) include;

a) Family, which comprises of a firm owned by individual and not listed on any stock exchange.
b) Widely held financial institutions: A financial firm, which is widely held at the 20%, 10% or 5% control threshold.
c) Widely held firms: Firms that do not have a shareholder controlling at least 20% of votes

TABLE 1
Companies Ownership characteristics

	Widely Held owners at 5% threshold	Ultimate owners at 5% threshold	Total
Number of Companies	343	300	643
Percentage	53.3%	46.7%	100%

In this study, the ultimate ownership was analysed and the results in table 1.1 show that, about 46.7% of sample firms used are those controlled by ultimately held companies at 10% threshold while 53.3% of all firms are firms owned by widely held companies at 10% threshold. This shows that UK ownership structure is not as dispersed as previously claimed

Ownership Distribution Based on Block holders' Types

The literature realizes that the diverse group of share owners have different levels of monitoring competence, different levels of wealth, different preferences about the way they like to receive the return on their investments, different cultures and so many cross-border differences, Thomsen and Pedersen (2000). According to the authors, the identity of firm's owners may determine their goals and this might have a great impact on the firm's behaviour which ultimately affects the firm's financial decisions and firm value in particular. For instance, the interest of financial institutional investors may be to realize short term return on their investments and they would just sell their shares when a firm suffers a down turn while corporations or non-financial institutions may be more focused on the long term- relationship hence make effort to participate in a restructuring process, Douma et al (2006). Table 2 presents the distribution of shareholders' types at 10% threshold. The table shows that, widely held financial institutions and 64.7 % by family firms control 24.7% of companies with ultimate ownership at 10% threshold. The table also reports that 10.6% represents other shareholders apart from family companies and financial institutions.

TABLE 2
Sample Distribution Based on Shareholders' Types

	Number and Percentage in bracket of Companies with Ultimate Ownership		
Type of shareholder	Financial Institutions	Family Companies	Others
At 10% threshold	74 (24.7%)	194 (64.7%)	32 (10.6%)

Distribution of Control Structures

Furthermore, table 3 shows that, 47.3% of the sample firms (643) have multiple large shareholders with the largest shareholder holding at least 20% of equity share and the second largest owning the minimum of 10% of the equity share as defined by Laeven and Levine

(2008) and Faccio and Lang (2002) as in La Porta *et al.* (1999). Following Faccio and Lang, (2002), in this study a controlling shareholder is said to be "alone" if no other owner controls at least 10% (or 20%) of the voting rights. Table 3 reports that, 54.7% of the sample firms are firms with single controlling shareholder at 10% threshold while about 50% of the sample firms are companies controlled by single class closely held firms. Likewise, as in Faccio and Lang (2002), this study defines a pyramid firm as a firm with an ultimate owner who controls it indirectly through another corporation which it does not wholly control. Further examination of control structures reveals that some companies have both pyramidal structure and dual-class equity structure. Table 3 shows that, while about 26% of the sample firms are considered to have dual-class equity structure about 31% have pyramidal structure. The table reports further that only 7% of the sample firms comprise of both pyramidal and dual share structure.

TABLE 3
Distribution of Companies Control Structure

Multiple Large Shareholders	Stand-alone controlling Shareholder	Controlled by pyramiding	Controlled by dual-class equity closely held firms	Controlled by single class closely held firms
304 (47.3%)	352(54.7%)	198(30.8%)	170(26.4%)	321(49.9%)

Composition of Multiple Large Shareholders

Concerning the composition of multiple large shareholders, the study considers two major types of shareholders, which form about 90% of the sample firms with multiple large shareholders namely family companies and widely held financial institutions. Table 4 shows that, only 5.6 % of all companies having multiple large shareholders have both the largest shareholder and the second largest, financial institutions while 39.1% of all companies with multiple large shareholders have both the largest and second largest, family companies. On the other hand, while 19.1 % of companies with multiple large shareholders have the largest shareholder a financial institution and the second largest a family company, 36.2 % of companies with multiple large shareholders have the largest shareholder a family company and the second largest a financial institution.

TABLE 4
Compositions of Multiple Large Shareholders

	Companies with Multiple Large Shareholders				
	The largest is Financial institution & the second largest is also Financial institution	The largest is Financial institution & the second largest is a family Company	The largest is Family company &the second largest is also family company	The largest is a family company & the second largest is a financial institutions	Total
Number of Companies	17	58	119	110	304
Percentage	5.6%	19.1%	39.1%	36.2%	100%

Coalition and Control Sharing

In an attempt to measure a control dilution, the study identifies firms whose largest owners control less than 50% of shares, hence, their control being diluted and no single shareholder possesses absolute control. Table 5 shows that, among companies with multiple large shareholders, 24% have the largest shareholder holding less than 50% of shares of the company such that there is no single shareholder with full control of the company. The table further shows that, about 75% of the companies have shareholders with full control. While about 53% of the sample firms with their control shared between two larger shareholders, 46.5% of the companies have their control shared by more than two larger shareholders.

TABLE 5
Coalition Formation and Control Sharing

	Largest owner has ownership greater than 50%	The largest owner has ownership less than 50%	Control is shared by more than two larger shareholders	Control is shared between first two larger shareholders
No. of Companies (Percentage)	48 (24%)	150 (75%)	106 (53%)	93 (46.5%)

Table 6 reports the number of firms in which the controlling shareholder use votes in excess of and equal to their cash-flow rights. In about 40% of firms the total sample the control-rights of the largest shareholder deviate from her cash-flow rights in which cases high voting shares are used to increase control. It can be observed that, there is a significantly larger separation of ownership and control for the largest and the second largest shareholder. When the mean difference of the cash flow-control rights ratio between the largest and second largest is tested, it was realized that the difference are statistically significant at 1% significant level as depicted in table 6, panel B.

Table 6 also shows that, about 60% of the sample firms do not separate the ownership and control and therefore their cash flow-control ratio is unit. When considering the second largest shareholders, the table in panel A, reports that, about 25% of the companies with second largest owners do not separate their ownership and control while only 18.5% have their control-rights greater than their corresponding cash-flow rights. Table 6 reports the number (and percent) of firms where the 1st and the 2nd largest owner has cash-flow rights to-control-rights (CF/CR) ratios equal to one and less than one in Panel A. Tests of mean difference in the use of dual-class equity to enhance control by the largest and second largest shareholders are reported in Panel B.

TABLE 6
Separations of Ownership and Control

Panel A: Largest shareholders' use of dual-class equity	Largest owner	2nd owner
Number (%) of CF/CR=1 firms	388(60.3%)	163(25.3%)
Number (%) of CF/CR <1 firms	255(39.7%)	37(18.5%)
Difference between largest owner vs. Second largest owner , t-value = -2.37***		

*, **, *** *Significant at the 10, 5, and 1 per cent levels, respectively.*

CONCLUSION

In general, it can be concluded that UK equity ownership has witnessed a rapid decline by major domestic institutional investors and increase in foreign ownership since 2004.

It is also concluded that UK ownership structure is not dispersed as reported in previously literature .The fact that about 47% of sampled firms are controlled by ultimately held companies at 10% threshold while 53% are firms owned by widely-held companies preliminarily support that corporate ownership is concentrated among UK Companies .

It is further reported that only 25% of ultimately owned companies are controlled by widely-held financial institutions, while 65% of the control of ultimately owned companies rests in the hands of families. This provides direct preliminary evidence that the agency problem between majority and minority shareholders in UK listed companies is becoming severe, when compared to in the 1980's where most companies were widely held and the core agency problem was between managers and shareholders.

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