Policy Research Journal
ISSN (E): 3006-7030 ISSN (P): 3006-7022 Volume 4, Issue 3, 2026

INSTITUTIONAL INVESTORS AND CORPORATE GOVERNANCE IN THE UNITED KINGDOM: MECHANISMS OF INFLUENCE, GOVERNANCE RISKS, AND THE LIMITS OF THE STEWARDSHIP FRAMEWORK

Nadia Saleem[1], Mamoona Idrees[*2], Syed Faraz Hussain Shah[3]

[1]*LLM, Corporate Law Nottingham Trent University, Nottinghamshire, UK*
[*2]*LLM, School of Law, Ocean University of China, China*
[3]*LLM, Khyber Law College, University of Peshawar, Pakistan*

[*2]mamoonakhan596@gmail.com

DOI: https://doi.org/10.5281/zenodo.21885022

Keywords
Institutional investors; corporate governance; UK Stewardship Code 2020; comply or explain; comparative corporate law; short-termism.

Article History
Received: 30 January 2026
Accepted: 15 March 2026
Published: 31 March 2026

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Mamoona Idrees

Abstract
Institutional investors, including pension funds, mutual funds, insurance companies, and global asset managers, now hold decisive equity stakes in UK listed companies, making them central actors in corporate governance. This paper examines the legal and market mechanisms through which institutional investors influence corporate decision-making in the United Kingdom, and critically evaluates the risks created by growing reliance on them as governance monitors. The research problem is that while UK law and soft-law instruments, namely the Companies Act 2006, the UK Corporate Governance Code 2018, and the UK Stewardship Code 2020, increasingly assign institutional investors a stewardship role, it remains unclear whether their incentives and behaviour make them effective and legitimate governance actors. Adopting a doctrinal methodology, the study analyses statutes, governance codes, regulatory documents, and case examples alongside academic literature. The findings show that institutional investors exert influence through voting, engagement and escalation, monitoring of disclosure, market-based pressure, and reputational sanction, but that this influence is undermined by passivity and free-riding, short-termism, concentration of power among a few asset managers, superficial box-ticking stewardship, and inaction during crises. The paper concludes that the "comply or explain" model is only as strong as the scrutiny investors apply, and recommends stronger enforcement of stewardship reporting, reform of advisory pay votes, regulation of proxy advisers, and mechanisms to protect retail investor voice, drawing comparative lessons for jurisdictions such as Pakistan that have transplanted the model without an equivalent institutional investor base.

INTRODUCTION

In the United Kingdom, the corporate governance landscape is significantly shaped by the growing presence of institutional investors such as pension funds, mutual funds, insurance companies, and asset managers who hold substantial equity stakes in public companies. Concentrated ownership of markets that are otherwise dispersed has given them the power to act as powerful market actors who can exercise influence on corporate decisions through voting, engagement and stewardship. In recent years, the UK Stewardship Code 2020 and post-financial-

crisis regulatory interventions have further encouraged their involvement in governance.

Research problem

The UK's governance framework increasingly depends on institutional investors as the primary check on boards, yet their willingness and capacity to perform that role is contested. Passive investment models, misaligned incentives, and conflicts of interest raise doubt as to whether investors can be relied upon as effective stewards, and their concentrated, unelected power raises questions of democratic legitimacy.

Significance of the problem

Because the UK model is built on flexible, market-enforced instruments (most notably "comply or explain") rather than hard-law prescription, any failure of investor scrutiny weakens the entire accountability architecture of UK company law. The global financial crisis demonstrated the systemic cost of investor passivity.

Existing scholarship has examined investor activism, stewardship, and the transnationalisation of governance separately; fewer studies bring together the mechanisms of influence, the risks of over-reliance, and the interaction with the UK Corporate Governance Code 2018 within a single doctrinal analysis of the post-2020 stewardship regime.

Research objectives

The study aims (i) to identify the legal and market mechanisms through which institutional investors influence UK corporate governance; (ii) to critically evaluate the governance risks posed by reliance on institutional investors; and (iii) to assess how effectively the UK Corporate Governance Code and Stewardship Code channel investor influence toward accountable, long-term governance.

Research questions

RQ1: Through what legal and market mechanisms do institutional investors influence corporate governance in UK listed companies?

RQ2: What governance risks arise from the growing reliance on institutional investors as governance actors?

RQ3: How effectively does the UK regulatory framework (particularly the Corporate Governance Code 2018 and the Stewardship Code 2020) direct institutional investor influence toward accountable, long-term governance?

The study is confined to UK listed companies and the UK regulatory framework, with reference to international scholarship and a comparative treatment of Pakistan where it illuminates transnational dynamics. It does not undertake empirical measurement of engagement outcomes.

Literature Review

The role of institutional investors in corporate governance has generated a substantial body of scholarship. Moore and Petrin provide the foundational account of institutional investors as governance actors, explaining how the accumulation of capital pools and the globalisation of financial markets have made these institutions hugely influential, while also identifying the free-rider problem: investors may lack sufficient incentives to monitor management actively because they can benefit from the monitoring efforts of others without incurring the costs themselves.[1] Earlier studies of UK pension funds similarly questioned whether large institutional holdings translate into effective monitoring.

A second strand examines the changing composition of the investor base. Kastiel and Nili document the rise of passive index funds and the "governance gap" this creates, noting that passive investors may lack the resources or motivation to engage meaningfully with firms beyond minimal compliance, while also observing that large institutions are increasingly willing to publicly criticise companies and coordinate votes in response to ESG failings.[2] Katelouzou and

[1] Marc Moore and Martin Petrin, Corporate Governance (Bloomsbury Publishing 2017).

[2] Kobi Kastiel and Yaron Nili, 'The Corporate Governance Gap' (2022) 131 Yale LJ 782

Zumbansen situate these developments transnationally, arguing that regulatory arbitrage and cross-border operation have created a complex multi-jurisdictional governance environment that poses normative challenges for legitimacy and accountability.[3]

A third strand addresses the regulatory response. MacNeil and Esser analyse the emergence of "comply or explain" as a global model, finding that its flexibility often collapses into a check-the-box mentality with minimal scrutiny.[4] The Kingman Review criticised earlier versions of the Stewardship Code for encouraging boilerplate disclosures with little evidence of meaningful action.[5] Bruner connects investor influence to the sustainability imperative, suggesting market-based influence may align capital flows with long-term ESG performance.[6]

The limitation of the existing literature is its fragmentation: activism, stewardship regulation, and legitimacy critiques are rarely integrated. The present study contributes by combining these strands into a single doctrinal analysis of the mechanisms, risks, and Code interactions under the post-2020 UK stewardship regime.

Legal Framework / Legal Background

Statutory framework

The Companies Act 2006 provides the statutory foundation for shareholder rights, including voting on director appointments, remuneration policies, and significant transactions, and, through section 414C, requires strategic reports giving investors insight into a company's business model, risks, and stakeholder relationships. The Enterprise and Regulatory Reform Act 2013 introduced the "say on pay" regime, empowering shareholders in respect of directors' remuneration.[7]

Soft-law and regulatory instruments

The UK Corporate Governance Code 2018 operates on a "comply or explain" basis under the Listing Rules; Provisions 1 and 5 address investor and stakeholder engagement, Provisions 9 and 11 board independence, and Provisions 33–41 remuneration. The UK Stewardship Code 2020, administered by the Financial Reporting Council, frames stewardship as "the responsible allocation, management and oversight of capital" and, following criticism of its predecessors, prioritises reported outcomes over policy statements, with Principle 9 setting expectations for engagement and escalation.[8] Listing Rules Chapter 9 requires continuous disclosure of price-sensitive information.[9] The Takeover Panel's Practice Statement No 26 requires boards to consult investors before defensive action in takeover

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https://www.yalelawjournal.org/pdf/131.3_KastielNili_3ow2k1hi.pdf accessed 17 April 2025.

[3] Dionysia Katelouzou and Peer Zumbansen, 'The Transnationalization of Corporate Governance: Law, Institutional Arrangements, & Corporate Power' (2021) 38 Ariz J Int'l & Comp L 1.

[4] Iain MacNeil and Irene-Marie Esser, 'The Emergence of "Comply or Explain" as a Global Model for Corporate Governance Codes' (SSRN, 29 January 2021) https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3775736 accessed 17 April 2025.

[5] John Kingman, 'Independent Review of the Financial Reporting Council' (2018) https://assets.publishing.service.gov.uk/media/5c1bbe68ed915d7327b92162/frc-independent-review-final-report.pdf accessed 17 April 2025.

[6] Christopher M Bruner, 'Corporate Governance Reform and the Sustainability Imperative' (2022) 131 Yale LJ 1217 https://www.yalelawjournal.org/pdf/3.Bruner_v473572r.pdf accessed 17 April 2025.

[7] Department for Business Innovation & Skills, 'Directors' Pay: Guide to Government Reforms' (2012) https://assets.publishing.service.gov.uk/media/5a789f7740f0b62b22cbb781/12-900-directors-pay-guide-to-reforms.pdf accessed 17 April 2025.

[8] Financial Reporting Council, 'The UK Stewardship Code 2020' (FRC, 30 September 2023) https://www.frc.org.uk/library/standards-codes-policy/stewardship/uk-stewardship-code/ accessed 17 April 2025.

[9] Financial Conduct Authority, 'Listing Rules, LR 9' (FCA Handbook) https://www.handbook.fca.org.uk/handbook/LR/9.pdf accessed 17 April 2025.

situations.[10] Regulatory history is also relevant: the FSA's 2009 letter to the Institutional Shareholders' Committee, responding to the financial crisis, catalysed the first Stewardship Code in 2010, and the 2018 Kingman Review of the Financial Reporting Council drove the 2020 revision.[11]

International dimension

The UK model has been widely exported: "comply or explain" has become a global template for governance codes, and stewardship codes modelled on the UK's now operate in numerous jurisdictions.[12] At the same time, the transnational operation of asset managers means UK-listed companies are governed partly by investors whose incentives and standards are set elsewhere, complicating the comparison of national and international frameworks.[13]

Comparative perspective: the Pakistani legal framework

Pakistan's corporate governance framework offers an instructive contrast to the investor-led UK model. The Companies Act 2017 provides the statutory foundation for shareholder rights in Pakistan, broadly paralleling the Companies Act 2006 in respect of voting on directors and major transactions, while the Securities and Exchange Commission of Pakistan (SECP) regulates listed companies under the Listed Companies (Code of Corporate Governance) Regulations 2019, made under the Companies Act 2017 and the SECP Act 1997.[14] The 2019 Regulations marked a deliberate shift toward a hybrid model in which core requirements remain compulsory but a substantial set of provisions operate on a "comply or explain" basis, a direct transplant of the UK approach. Subsequent amendments in 2023 and 2024 have extended board responsibility for sustainability, ESG oversight, and diversity and inclusion, aligning the Pakistani code with international best practice at the level of board duties.

The critical difference lies not in the codes but in the ownership structures they regulate. Whereas the UK framework assumes dispersed ownership disciplined by large institutional investors, Pakistani listed companies are characterised by concentrated family, group, and state ownership, with domestic institutional investors, namely mutual funds, insurance companies, and pension funds, holding comparatively small stakes and exercising limited voice. Pakistan has no stewardship code, no equivalent of the Investor Forum, and no regulatory expectation that institutional investors monitor explanations for non-compliance. The consequence is that "comply or explain" has been transplanted without the enforcement engine the UK model presupposes: if investor scrutiny is weak even in the UK, as this paper's findings demonstrate, it is largely absent in Pakistan, leaving compliance quality dependent on SECP supervision alone. This comparison sharpens the paper's central argument, that the effectiveness of flexible governance codes is contingent on the incentives and capacity of the investors expected to police them, and signals a reform direction for Pakistan considered in the recommendations.

Pakistani courts have nonetheless begun to develop a minority-protection jurisprudence that

[10] The Takeover Panel, 'Practice Statement No 26: Shareholder Activism' (2023) https://code.thetakeoverpanel.org.uk/tp/ps/ps-26.html accessed 17 April 2025.

[11] Alasdair Steele, 'FSA Clarification on Collective Shareholder Action' (Lexology, 26 August 2009) https://www.lexology.com/library/detail.aspx?g=bec9c1bb-b677-43ea-9f49-9f7df7b54f5d accessed 17 April 2025.

[12] Iain MacNeil and Irene-Marie Esser, 'The Emergence of "Comply or Explain" as a Global Model for Corporate Governance Codes' (SSRN, 29 January 2021) https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3775736 accessed 17 April 2025.

[13] Dionysia Katelouzou and Peer Zumbansen, 'The Transnationalization of Corporate Governance: Law, Institutional Arrangements, & Corporate Power' (2021) 38 Ariz J Int'l & Comp L 1.

[14] Securities and Exchange Commission of Pakistan, 'Listed Companies (Code of Corporate Governance) Regulations, 2019 (Amended up to March 2025)' (SECP) https://www.secp.gov.pk/ accessed 21 July 2026.

parallels the UK position. In *Asif Mannaan v Suleman Lallani*, the Sindh High Court applied the rule in *Foss v Harbottle* and its exceptions, permitting minority shareholders to sue where the statutory criteria are met, though on the facts the claim failed given the claimant's minimal stake and the prior involvement of the SECP.[15] Read with the oppression and mismanagement remedy in section 286 of the Companies Act 2017, the decision shows that judicial and regulatory oversight operate in parallel rather than to the exclusion of one another; what remains absent, by contrast with the United Kingdom, is any comparable body of institutional investor stewardship to activate these protections in practice.[16]

Judicial decisions and case law

Although UK corporate governance is driven principally by statute and code, the courts define the boundaries within which investor influence operates. Three lines of authority are relevant. First, the proper-purpose rule in section 171(b) of the Companies Act 2006, authoritatively restated in *Eclairs Group Ltd v JKX Oil & Gas plc*, constrains boards from deploying their powers to frustrate shareholder decision-making.[17] Second, the rule that directors' duties are owed to the company rather than to individual shareholders, established in *Percival v Wright*, shapes the remedial routes open to investors.[18] Third, *BTI 2014 LLC v Sequana SA* confirms that the section 172 duty to promote the success of the company is not a mandate for shareholder primacy without limit, since it is qualified by the interests of creditors as insolvency approaches.[19] Together these decisions frame the legal space in which the mechanisms analysed below must operate.

[15] Asif Mannaan v Suleman Lallani PLD 2020 Sindh 660.
[16] Foss v Harbottle (1843) 2 Hare 461.
[17] Eclairs Group Ltd v JKX Oil & Gas plc [2015] UKSC 71, [2016] 3 All ER 641.
[18] Percival v Wright [1902] 2 Ch 401.
[19] BTI 2014 LLC v Sequana SA [2022] UKSC 25, [2024] AC 211.

Research Methodology

This study adopts a doctrinal (black-letter) research approach combined with critical legal analysis. The research design is qualitative and analytical rather than empirical. Primary sources comprise UK statutes (the Companies Act 2006; the Enterprise and Regulatory Reform Act 2013), regulatory codes and rules (the UK Corporate Governance Code 2018; the UK Stewardship Code 2020; the FCA Listing Rules; Takeover Panel Practice Statement No 26), and official documents (the FSA's 2009 correspondence; the Kingman Review; government guidance on directors' pay). Secondary sources comprise books, peer-reviewed journal articles, and institutional reports. Data were collected through library-based and electronic legal research and analysed thematically: mechanisms of influence, risks of reliance, and Code interaction were treated as analytical categories corresponding to the research questions. Illustrative cases, such as investor responses to executive pay at Barclays, are used to test doctrinal claims against practice. No human participants were involved, so ethical approval was not required.

Results / Findings

Findings on RQ1: Mechanisms of institutional investor influence

Voting Rights and Shareholder Resolutions

One of the most fundamental mechanisms of influence is the exercise of voting rights. Institutional investors vote on key corporate matters, including director appointments, remuneration policies, and significant transactions such as mergers or acquisitions. The Companies Act 2006 provides the statutory framework for these rights, which are complemented by best practice guidance under the UK Corporate Governance Code. As Moore and Petrin explained, institutional investors can significantly influence outcomes due to the size of their holdings, particularly when they coordinate voting agendas or pre-declare intentions.[20]

[20] Marc Moore and Martin Petrin, Corporate Governance (Bloomsbury Publishing 2017).

Notably, the evolution of "say on pay" policies has empowered institutional investors to vote on directors' remuneration reports, a development driven by reforms such as the Enterprise and Regulatory Reform Act 2013 and guided by resources like the Investment Association Principles of Remuneration.[21] Investor assertiveness is evident in growing criticism of executive pay at AGMs. The 2020 guidance emphasises linking remuneration to long-term performance and stakeholder outcomes, equipping investors with detailed criteria to assess and influence directors' decisions on pay.[22] However, most shareholder votes on remuneration are advisory rather than binding, raising questions about their actual impact on curbing excessive pay. This limits their effectiveness, especially when boards choose to ignore adverse votes.

Engagement and Stewardship

Beyond formal votes, engagement is central to how institutional investors exert influence. This is institutionalised in the UK Stewardship Code 2020, which frames stewardship as "the responsible allocation, management and oversight of capital."[23] Institutional investors are expected not only to monitor companies but to engage constructively to promote long-term value. The revised 2020 Code responded to earlier criticism by focusing on measurable engagement outcomes rather than policy declarations. As a result, the current Code includes reporting requirements that force asset owners and managers to show the real-world impact of their stewardship activities. Principle 9 of the Code sets expectations for proactive engagement. This can take the form of meetings with non-executive directors, submitting questions on strategic direction, or raising concerns about ESG practices. The role of intermediaries such as the Investor Forum also enables collective engagement on sensitive issues, often acting behind the scenes to push boards toward reform.[24] Despite this, there is ongoing debate about the depth and sincerity of engagement practices. Critics argue that some institutions engage superficially to meet compliance standards rather than drive meaningful change.[25]

Escalation of Stewardship Activities

Where engagement fails, institutional investors may escalate. This process is explicitly endorsed by the Stewardship Code and includes voting against directors, filing shareholder resolutions, or publicly criticising the board. Escalation is formally recognised in the 2020 Stewardship Code. Shareholder revolts over pay and climate inaction show increasing intolerance for weak governance. The Takeover Panel Practice Statement No 26 supports investors' influence during takeover situations by requiring boards to consult investors before taking defensive action, reinforcing their ability to shape corporate transactions.[26] Additionally, Kastiel and Nili noted that large institutional investors are increasingly willing to publicly criticise companies and coordinate their votes in response to poor

[21] The Investment Association, 'The Investment Association Principles of Remuneration' (2020) https://www.ivis.co.uk/media/13885/principles-of-remuneration-2021.pdf accessed 17 April 2025.

[22] Department for Business Innovation & Skills, 'Directors' Pay: Guide to Government Reforms' (2012) https://assets.publishing.service.gov.uk/media/5a789f7740f0b62b22cbb781/12-900-directors-pay-guide-to-reforms.pdf accessed 17 April 2025.

[23] Financial Reporting Council, 'The UK Stewardship Code 2020' (FRC, 30 September 2023) https://www.frc.org.uk/library/standards-codes-policy/stewardship/uk-stewardship-code/ accessed 17 April 2025.

[24] The Investor Forum, 'Annual Event 2022' (The Investor Forum, 27 February 2023) https://www.investorforum.org.uk/annual-event-2022/ accessed 17 April 2025.

[25] John Kingman, 'Independent Review of the Financial Reporting Council' (2018) https://assets.publishing.service.gov.uk/media/5c1bbe68ed915d7327b92162/frc-independent-review-final-report.pdf accessed 17 April 2025.

[26] The Takeover Panel, 'Practice Statement No 26: Shareholder Activism' (2023) https://code.thetakeoverpanel.org.uk/tp/ps/ps-26.html accessed 17 April 2025.

governance or ESG failings.[27] This shift suggests growing investor willingness to move beyond passive stewardship and embrace more activist postures, especially in the face of systemic risks like climate change.

Investor Oversight of Governance through Monitoring and Disclosure

Monitoring is a prerequisite for meaningful engagement. Investors use internal teams and data providers to assess disclosures and performance. The Listing Rules Chapter 9 requires continuous disclosure of price-sensitive information, giving investors real-time access to material developments.[28] Moreover, strategic reports required under the Companies Act 2006 s 414C provide institutional investors with insight into a company's business model, risks, and stakeholder relationships. Such disclosures support investors in engaging on strategic and ESG-related concerns. As Moore and Petrin argue, institutional investors' capacity to gather and interpret data enhances their legitimacy as monitors and allows them to challenge managerial discretion more effectively.[29]

Market-Based Influence

Institutional investors can also exert influence by adjusting their investment decisions. By selling or reducing holdings, investors signal disapproval, exerting indirect pressure on governance outcomes. Such influence is particularly significant for companies dependent on equity financing or concerned with market reputation. Bruner highlighted the role of investors in promoting sustainable corporate governance, suggesting that market-based influence may complement formal mechanisms by aligning capital flows with long-term ESG performance.[30] This approach has gained traction, with pension funds and asset managers increasingly making investment decisions based on sustainability ratings and ethical conduct, often disclosed in annual stewardship or engagement reports.

Reputational and Normative Pressure

In addition to formal and economic pressures, institutional investors influence directors through reputational mechanisms. Media and peer scrutiny often influence corporate behaviour even in the absence of formal investor actions. The FSA letter of 2009 to the Institutional Shareholders' Committee emphasised that investor engagement must move beyond passive observance to active stewardship, citing the failures of the financial crisis as justification for enhanced investor involvement.[31] Cases like Barclays' CEO pay scandal show how investors challenge unfair governance under public pressure.[32]

In summary, the research finds six operative mechanisms: statutory voting rights, including advisory say-on-pay votes; engagement and stewardship institutionalised by the 2020 Code; escalation through votes against directors, resolutions, and public criticism; monitoring enabled by mandatory disclosure under the Listing Rules and section 414C strategic reports; market-based influence through capital allocation; and reputational pressure. A key

[27] Kobi Kastiel and Yaron Nili, 'The Corporate Governance Gap' (2022) 131 Yale LJ 782 https://www.yalelawjournal.org/pdf/131.3_KastielNili_3ow2k1hi.pdf accessed 17 April 2025.

[28] Financial Conduct Authority, 'Listing Rules, LR 9' (FCA Handbook) https://www.handbook.fca.org.uk/handbook/LR/9.pdf accessed 17 April 2025.

[29] Marc Moore and Martin Petrin, Corporate Governance (Bloomsbury Publishing 2017) ch 6.

[30] Christopher M Bruner, 'Corporate Governance Reform and the Sustainability Imperative' (2022) 131 Yale LJ 1217 https://www.yalelawjournal.org/pdf/3.Bruner_v473572r.pdf accessed 17 April 2025.

[31] Alasdair Steele, 'FSA Clarification on Collective Shareholder Action' (Lexology, 26 August 2009) https://www.lexology.com/library/detail.aspx?g=bec9c1bb-b677-43ea-9f49-9f7df7b54f5d accessed 17 April 2025.

[32] Kavitha Sivasubramaniam, 'Barclays Doubles CEO Pay and Awards Shares to 90,000 Staff' (Personnel Today, 13 February 2025) https://www.personneltoday.com/hr/barclays-doubles-ceo-pay-and-awards-shares-to-90000-staff/ accessed 17 April 2025.

pattern is that formal legal rights are amplified by informal, market and reputational channels, but that several mechanisms, notably advisory pay votes, lack binding force.

Findings on RQ2: Governance risks of reliance on institutional investors

Passive Institutional Investment and the Free-Rider Problem

A primary risk lies in the passivity of many institutional investors. While they are well-positioned to hold directors accountable, many do not exercise this influence consistently. Moore and Petrin observe that institutional investors may lack sufficient incentives to monitor management actively because they can benefit from the monitoring efforts of others without incurring the costs themselves.[33] This "free-rider problem" is particularly acute in widely held companies where ownership is dispersed among many large investors. The issue is compounded by the dominance of index funds and passive investment vehicles, which track market indices and do not select companies based on governance quality. As Kastiel and Nili noted, passive investors may lack the resources or motivation to engage meaningfully with firms beyond minimal compliance.[34] Their business models emphasise diversification and low fees, which limit their capacity to investigate specific governance failures or escalate concerns.

Short-termism in Institutional Investment and Misaligned Governance Incentives

Institutional investors may also prioritise short-term financial returns over long-term company value or stakeholder interests. Many investors prioritise quarterly results, favouring short-term profits over sustainable growth. This short-term focus can weaken the push toward sustainable and inclusive corporate strategies.[35] Directors may face pressure to engage in share buybacks, reduce R&D spending, or avoid long-term investments in human capital and climate risk mitigation to meet investor expectations. Thus, institutional investor influence may crowd out stakeholder interests and distort managerial incentives. Furthermore, institutional investors are themselves corporations with their own governance issues. For example, asset managers may vote in favour of management at client companies to preserve business relationships or secure access to new investment opportunities. This "conflict of interest" undermines their credibility as stewards of good governance.

Concentration of Institutional Investor Power and the Democratic Deficit in Governance

Another concern is the increasing concentration of ownership in a small group of global asset managers, such as BlackRock, Vanguard, and State Street, who collectively manage trillions of assets and hold significant voting power in most large public companies. This concentration risks placing corporate governance in the hands of a few unelected financial institutions with little transparency or accountability to ordinary investors or the public. Katelouzou and Zumbansen highlight that this concentration poses significant normative challenges for the legitimacy of transnational corporate governance structures.[36] It shifts control away from boards and stakeholders toward financial intermediaries that may not share the same objectives or governance standards across jurisdictions. There is also a broader issue of democratic legitimacy. Institutional investors are not elected by stakeholders, employees, or the broader community, yet they wield substantial power over

[33] Marc Moore and Martin Petrin, Corporate Governance (Bloomsbury Publishing 2017) ch 5.

[34] Kobi Kastiel and Yaron Nili, 'The Corporate Governance Gap' (2022) 131 Yale LJ 782 https://www.yalelawjournal.org/pdf/131.3_KastielNili_3ow2k1hi.pdf accessed 17 April 2025.

[35] Christopher M Bruner, 'Corporate Governance Reform and the Sustainability Imperative' (2022) 131 Yale LJ 1217 https://www.yalelawjournal.org/pdf/3.Bruner_v473572r.pdf accessed 17 April 2025.

[36] Dionysia Katelouzou and Peer Zumbansen, 'The Transnationalization of Corporate Governance: Law, Institutional Arrangements, & Corporate Power' (2021) 38 Ariz J Int'l & Comp L 1.

strategic business decisions, including mergers, executive pay, and sustainability. This technocratic governance model can marginalise other corporate constituents, undermining inclusive decision-making and stakeholder participation.

Superficial Stewardship and Box-Ticking Governance Practices

Although the UK Stewardship Code 2020 was designed to address superficial engagement, evidence suggests that much institutional investor behaviour still relies on form rather than substance. The Kingman Review criticised earlier versions of the Stewardship Code as encouraging "boilerplate disclosures" with little evidence of meaningful action.[37] Despite reforms, stewardship often remains focused on procedural compliance, echoing earlier critiques of box-ticking governance. This superficiality weakens the monitoring function of institutional investors. Boards may satisfy investor expectations through symbolic gestures, such as gender quotas or ESG statements, without implementing deeper governance reforms. As MacNeil and Esser discuss, the "comply or explain" model has the potential to promote flexibility and innovation, but in practice it often results in a check-the-box mentality with minimal scrutiny.[38]

Institutional Investor Inaction During Governance Crises

The global financial crisis exposed the failure of institutional investors to provide an effective check on corporate excesses. As previously noted in the context of the Stewardship Code, regulatory concerns over investor passivity were raised following the 2009 financial crisis.[39] Similarly, the Takeover Panel Practice Statement No 26 reflects concerns about the lack of investor activism during critical events like mergers or hostile takeovers. Investors often acquiesce to board recommendations without critically evaluating the long-term consequences, especially when presented with complex or time-sensitive decisions.[40] These examples illustrate the danger of assuming that institutional investors will act in the best interest of the company or broader society, particularly under pressure or in fast-moving scenarios.

Institutional Disengagement on Politically Sensitive Governance Issues

Institutional investors frequently avoid engagement on politically sensitive or controversial topics such as climate change, tax strategies, supply chain ethics, or executive misconduct. The Investor Forum was created in part to enable collective, confidential engagement on difficult issues, acknowledging that individual institutions may shy away from confrontation.[41] The risk here is one of silence or complicity, where institutional investors, for reputational or financial reasons, fail to challenge boards on critical matters. Avoidance of sensitive issues raises doubts about the authenticity of investor stewardship.

[37] John Kingman, 'Independent Review of the Financial Reporting Council' (2018) https://assets.publishing.service.gov.uk/media/5c1bbe68ed915d7327b92162/frc-independent-review-final-report.pdf accessed 17 April 2025.

[38] Iain MacNeil and Irene-Marie Esser, 'The Emergence of "Comply or Explain" as a Global Model for Corporate Governance Codes' (SSRN, 29 January 2021) https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3775736 accessed 17 April 2025.

[39] Alasdair Steele, 'FSA Clarification on Collective Shareholder Action' (Lexology, 26 August 2009) https://www.lexology.com/library/detail.aspx?g=bec9c1bb-b677-43ea-9f49-9f7df7b54f5d accessed 17 April 2025.

[40] The Takeover Panel, 'Practice Statement No 26: Shareholder Activism' (2023) https://code.thetakeoverpanel.org.uk/tp/ps/ps-26.html accessed 17 April 2025.

[41] The Investor Forum, 'Annual Event 2022' (The Investor Forum, 27 February 2023) https://www.investorforum.org.uk/annual-event-2022/ accessed 17 April 2025.

Power Imbalances Among Institutional and Retail Investors

Institutional investors may crowd out smaller investors in decision-making. Their access to private meetings with boards, their ability to influence proxy advisers, and their expertise give them advantages that ordinary retail investors do not possess. This exacerbates inequality among investors and entrenches a hierarchy within corporate governance. The Barclays CEO pay case, for instance, saw institutional investors expressing concern, but the outcome still reflected board preferences, raising questions about the actual leverage of investors, even powerful ones, in shaping executive outcomes.[42]

In summary, the research identifies seven risk categories: the free-rider problem intensified by passive index investing; short-termism and conflicted incentives; concentration of power creating a democratic deficit; superficial, box-ticking stewardship; inaction during governance crises; disengagement on politically sensitive issues; and structural disadvantage of retail investors. The pattern across these findings is that the same features that make institutional investors powerful, namely scale, diversification, and intermediation, also weaken their incentives to monitor.

Findings on RQ3: Interaction with the UK Corporate Governance Code

The research finds that the 2018 Code presupposes active investor scrutiny at every pressure point, namely engagement (Provisions 1 and 5), board composition (Provisions 9 and 11), remuneration (Provisions 33–41), and stakeholder voice, and that "comply or explain" delegates enforcement to investors. Where investors are passive or conflicted, boilerplate explanations go unchallenged and the Code's accountability model is hollowed out. The detailed analysis follows in the next section.

Discussion / Legal Analysis

Stewardship and the Role of Institutional Investors

Although the Code primarily targets the responsibilities of company boards, it explicitly recognises the importance of investor engagement. Provision 1 of the UK Corporate Governance Code 2018 notes that a company's governance framework should promote effective engagement with investors and wider stakeholders. Moreover, Provision 5 highlights the need for companies to understand investor views, which implies an active and reciprocal dialogue. Institutional investors, especially asset managers and pension funds, are in a privileged position to support or challenge boards in delivering good governance. The Stewardship Code 2020, which complements the Corporate Governance Code, aims to formalise this relationship.[43] Institutional investors are expected to monitor investee companies, engage constructively, and escalate concerns when necessary. However, the success of this interaction depends heavily on the behaviour and incentives of institutional investors.

Comply or Explain: Limitations and Investor Responsibility

The UK's "comply or explain" approach offers flexibility, allowing companies to diverge from strict adherence to Code provisions provided that they explain their reasons. This structure requires institutional investors to play an oversight role by assessing whether explanations are reasonable and justified. In theory, it encourages thoughtful application rather than mechanical compliance. However, this framework is only as effective as the scrutiny investors apply. As MacNeil and Esser observe, many institutional investors either fail to analyse explanations rigorously or do not

[42] Kavitha Sivasubramaniam, 'Barclays Doubles CEO Pay and Awards Shares to 90,000 Staff' (Personnel Today, 13 February 2025) https://www.personneltoday.com/hr/barclays-doubles-ceo-pay-and-awards-shares-to-90000-staff/ accessed 17 April 2025.

[43] Financial Reporting Council, 'The UK Stewardship Code 2020' (FRC, 30 September 2023) https://www.frc.org.uk/library/standards-codes-policy/stewardship/uk-stewardship-code/ accessed 17 April 2025.

act when unsatisfied.[44] This results in a weakening of accountability mechanisms, as companies may provide boilerplate justifications without facing consequences. This issue was highlighted in the Kingman Review, which criticised weak enforcement of stewardship standards.[45] Institutional investors therefore play a critical role in interpreting and holding companies accountable for non-compliance with the Code's provisions. When they neglect this duty, whether due to resourcing constraints, conflicts of interest, or passivity, the overall legitimacy and credibility of the "comply or explain" model is undermined.

Board Composition and Institutional Investor Influence

The Code places significant emphasis on board independence, diversity, and the separation of powers (such as the roles of CEO and Chair). For example, Provision 9 requires that the chair should be independent on appointment, while Provision 11 advocates for at least half the board to be independent non-executive directors. Institutional investors influence board composition by voting on director appointments, remuneration reports, and corporate resolutions. While this can be a powerful accountability mechanism, it also raises concerns about who influences the influencers. There is growing scrutiny of proxy adviser firms like ISS and Glass Lewis that help institutional investors decide how to vote on key governance matters. While proxy advisers enhance coordination, their guidance can reduce governance flexibility.[46] Thus, the interaction between institutional investors and the Code's provisions on board structure can promote or hinder good governance, depending on how actively and independently investors exercise their rights.

The judiciary has reinforced this boundary between board and shareholder power. In *Eclairs Group Ltd v JKX Oil & Gas plc*, the Supreme Court held that directors must exercise their powers only for the purposes for which they are conferred, and that using share-restriction powers to influence the outcome of a shareholder vote fell outside those proper purposes.[47] The proper-purpose rule, as the Court observed, is the principal means by which equity polices the constitutional division between the board and the general meeting; it thus operates as a legal backstop where institutional investor voting is resisted by incumbent boards. The longstanding principle that directors owe their duties to the company rather than to individual shareholders, established in *Percival v Wright*, further explains why investor influence must be channelled through voting and engagement rather than through direct fiduciary claims.[48]

Remuneration and Institutional Investor Impact on Long-Term Governance

Executive pay remains one of the most contentious aspects of UK corporate governance. The Code (Provisions 33–41) sets out detailed expectations for remuneration policies, including alignment with company purpose and values, clarity, and a focus on long-term sustainable performance. Institutional investors are expected to scrutinise pay policies, approve remuneration reports, and ensure that performance-related pay structures are not misaligned with investor interests. This reinforces the earlier concern

[44] Iain MacNeil and Irene-Marie Esser, 'The Emergence of "Comply or Explain" as a Global Model for Corporate Governance Codes' (SSRN, 29 January 2021) https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3775736 accessed 17 April 2025.

[45] John Kingman, 'Independent Review of the Financial Reporting Council' (2018) https://assets.publishing.service.gov.uk/media/5c1bbe68ed915d7327b92162/frc-independent-review-final-report.pdf accessed 17 April 2025.

[46] Dionysia Katelouzou and Peer Zumbansen, 'The Transnationalization of Corporate Governance: Law, Institutional Arrangements, & Corporate Power' (2021) 38 Ariz J Int'l & Comp L 1.

[47] Eclairs Group Ltd v JKX Oil & Gas plc [2015] UKSC 71, [2016] 3 All ER 641.

[48] Percival v Wright [1902] 2 Ch 401.

about short-termism driving misaligned incentives in executive pay structures.[49] While the Code aims to temper these effects through enhanced transparency and guidance, its success again depends on the quality of investor oversight. Where institutional investors are passive or conflicted, excessive or misaligned pay structures may go unchallenged.

Corporate Culture, Stakeholders, and Institutional Investor Governance

The 2018 version of the Code marks a notable shift toward stakeholder-inclusive governance. Provision 5 suggests mechanisms for workforce engagement, such as appointing a worker representative or designating a non-executive director to liaise with employees. Institutional investors have a pivotal role in either advancing or resisting this broader shift toward stakeholder-inclusive governance. Institutional investors may prioritise financial outcomes over broader stakeholder concerns.[50] This creates a mismatch between the aims of the Code and the likely behaviour of institutional investors, particularly when they resist initiatives like ESG disclosure, living wage campaigns, or supply chain accountability that may affect short-term profits. Hence, while the Code attempts to embed a broader understanding of corporate purpose, its success is limited unless institutional investors internalise stakeholder values and reflect them in their engagement practices.

The limits of a purely shareholder-oriented reading of directors' duties are visible in the case law on section 172. In *BTI 2014 LLC v Sequana SA*, the Supreme Court confirmed that the duty to promote the success of the company for the benefit of its members is qualified by a duty to consider creditors' interests once the company is insolvent or bordering on insolvency, illustrating that the statutory conception of "success" already reaches beyond immediate shareholder returns.[51] This judicial recognition of interests beyond the shareholder body strengthens the Code's stakeholder-inclusive turn, but it also underscores the tension examined here: institutional investors whose mandate is financial return may resist precisely the broader conception of corporate purpose that both the Code and the courts increasingly endorse.

Investor Engagement and Collective Action

The Code and its accompanying guidance encourage constructive investor engagement. However, in practice, collective action problems, conflicts of interest, and resource limitations mean that many institutional investors struggle to engage meaningfully with multiple companies in their portfolios. As noted earlier, historic disengagement by institutional investors continues to shape collective action challenges today.[52] The Investor Forum was established to improve this dynamic by enabling confidential collective engagement among long-term investors.[53] However, its voluntary nature and limited scope mean that it cannot fully substitute for strong individual institutional accountability or replace robust public regulation.

Synthesis: Effectiveness, Legitimacy, and International Comparison

Interpreting the findings together, three conclusions emerge. First, on effectiveness: the UK framework equips institutional investors with extensive rights and expectations, but its

[49] Christopher M Bruner, 'Corporate Governance Reform and the Sustainability Imperative' (2022) 131 Yale LJ 1217 https://www.yalelawjournal.org/pdf/3.Bruner_v473572r.pdf accessed 17 April 2025.

[50] Marc Moore and Martin Petrin, Corporate Governance (Bloomsbury Publishing 2017).

[51] BTI 2014 LLC v Sequana SA [2022] UKSC 25, [2024] AC 211.

[52] Alasdair Steele, 'FSA Clarification on Collective Shareholder Action' (Lexology, 26 August 2009) https://www.lexology.com/library/detail.aspx?g=bec9c1bb-b677-43ea-9f49-9f7df7b54f5d accessed 17 April 2025.

[53] The Investor Forum, 'Annual Event 2022' (The Investor Forum, 27 February 2023) https://www.investorforum.org.uk/annual-event-2022/ accessed 17 April 2025.

enforcement logic is circular: the Code relies on investors to police companies, while the Stewardship Code relies on disclosure and reputation to police investors. Neither layer carries hard sanctions, so effectiveness depends on incentives that the findings under RQ2 show to be weak or conflicted. This confirms MacNeil and Esser's diagnosis of check-the-box compliance and extends it to the post-2020 regime: outcome-based reporting has improved transparency without demonstrably changing engagement depth.[54]

Second, on legitimacy: the concentration of voting power in a few unelected asset managers, identified by Katelouzou and Zumbansen as a normative challenge for transnational governance, sits uneasily with the 2018 Code's stakeholder-inclusive turn.[55] A technocratic monitor whose mandate is financial return is being asked to enforce provisions designed to protect employees and wider society, a mismatch the Barclays pay episode illustrates, where institutional concern did not displace board preference.[56]

Third, by comparison with international best practice: the UK remains the model exporter of stewardship regulation, yet jurisdictions adopting binding elements, such as mandatory engagement disclosure with regulatory review, suggest that soft law alone is insufficient. The Pakistani experience examined in the legal framework illustrates the risk in exportable form: a code transplanted without the investor infrastructure to enforce it.[57] The UK's experience since 2010 indicates that revising code language in 2020 without strengthening enforcement (the gap Kingman identified in the FRC) produces incremental rather than structural improvement.[58] The critical argument of this research is therefore that institutional investors should be treated as regulated governance intermediaries, not merely encouraged stewards.

Recommendations

1. For government and Parliament: legislate to make shareholder votes on annual remuneration reports binding rather than advisory for premium-listed companies, closing the gap identified in the say-on-pay findings, and give the successor regulator to the FRC statutory powers to assess and sanction the quality of stewardship reporting, as contemplated by the Kingman Review.
2. For the regulator (FRC/ARGA and FCA): move from tiering signatories of the Stewardship Code to substantive review of reported engagement outcomes, with public identification of boilerplate reporting; and require asset managers to disclose conflicts of interest affecting voting at client companies.
3. For the Takeover Panel and FCA jointly: strengthen expectations of investor participation during takeovers and crises, building on Practice Statement No 26, so that acquiescence to board recommendations is a considered rather than default position.

[54] Iain MacNeil and Irene-Marie Esser, 'The Emergence of "Comply or Explain" as a Global Model for Corporate Governance Codes' (SSRN, 29 January 2021) https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3775736 accessed 17 April 2025.

[55] Dionysia Katelouzou and Peer Zumbansen, 'The Transnationalization of Corporate Governance: Law, Institutional Arrangements, & Corporate Power' (2021) 38 Ariz J Int'l & Comp L 1.

[56] Kavitha Sivasubramaniam, 'Barclays Doubles CEO Pay and Awards Shares to 90,000 Staff' (Personnel Today, 13 February 2025) https://www.personneltoday.com/hr/barclays-doubles-ceo-pay-and-awards-shares-to-90000-staff/ accessed 17 April 2025.

[57] Securities and Exchange Commission of Pakistan, 'Listed Companies (Code of Corporate Governance) Regulations, 2019 (Amended up to March 2025)' (SECP) https://www.secp.gov.pk/ accessed 21 July 2026.

[58] John Kingman, 'Independent Review of the Financial Reporting Council' (2018) https://assets.publishing.service.gov.uk/media/5c1bbe68ed915d7327b92162/frc-independent-review-final-report.pdf accessed 17 April 2025.

4. For institutional investors: pool engagement resources through the Investor Forum for systemic issues (climate, pay, culture) to overcome collective action costs, and pre-declare voting intentions on contested resolutions to increase transparency.
5. On proxy advisers: introduce a registration and conduct regime for proxy advisory firms such as ISS and Glass Lewis, given their outsized influence on institutional voting identified in the findings.
6. For retail investor protection: require platforms and nominees to pass through voting rights to underlying beneficial owners by default, mitigating the power imbalance between institutional and retail investors.
7. For Pakistan (SECP): before deepening reliance on "comply or explain," develop the institutional preconditions the model requires: a Pakistani stewardship code for mutual funds, insurance companies, and pension funds; mandatory disclosure of institutional voting records; and SECP review of the quality of companies' non-compliance explanations, while retaining mandatory status for core protections, given concentrated ownership and the limited monitoring capacity of domestic institutional investors.

Conclusion

The answer to the research problem is qualified: institutional investors are indispensable but unreliable guardians of UK corporate governance. The findings show that they possess a uniquely powerful toolkit, comprising voting, engagement, escalation, monitoring, exit, and reputational sanction, institutionalised through the Companies Act 2006, the Corporate Governance Code 2018, and the Stewardship Code 2020. Yet the same analysis shows that passivity, short-termism, concentration of power, superficial stewardship, and crisis inaction systematically weaken the monitoring on which the UK's "comply or explain" model depends. The contribution of this research is to integrate the mechanisms, risks, and Code interactions into a single doctrinal assessment of the post-2020 regime, demonstrating that the framework's weakness is structural: it delegates enforcement to actors whose incentives are misaligned with the task. The main legal implication is that soft-law stewardship has reached the limit of what disclosure and reputation can achieve, and that targeted hard-law reform, namely binding pay votes, regulated stewardship reporting, and proxy adviser oversight, is now required. Future research could empirically test engagement outcomes under the 2020 Code and compare the UK regime with emerging stewardship frameworks in other jurisdictions, including Pakistan.

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