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Dear Chris,

Consultation on the Revised Corporate Governance Code

ACCA (the Association of Chartered Certified Accountants) is pleased to respond to the Financial Reporting Council (FRC) consultation on The Revised Corporate Governance Code. ACCA has provided detailed submissions to the FRC in response to the two consultations on the Combined Code last year.

ACCA is the largest and fastest-growing global professional accountancy body with 131,500 members and 362,000 students in 170 countries. We aim to offer the first choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management. ACCA works to achieve and promote the highest professional, ethical and governance standards and advance the public interest.

Overall

We congratulate the FRC on presenting this revised Code. We believe it has the potential, not just to raise standards of corporate governance, but to bring about a more enlightened approach to governance in a business environment where people are increasingly more concerned with good practice than with simple compliance.

It is generally agreed that corporate governance has been lacking in some of our financial institutions. Nevertheless, these institutions could reasonably claim to have complied with the Combined Code. Compliance may have been satisfactory but practice was not. It is important that the revised Code will bring about changes in attitudes and behaviour among executives, boards and shareholders.

It has been argued that corporate governance requires stronger regulation and enforcement. We sympathise with this view but, recognising the new focus of the Code, are optimistic that voluntary changes are possible with the right mindset and encouragement. There is evidence to suggest that many of the financial sector's problems were a result, not of too little regulation, but of inappropriate regulation and a mindset of getting around the rules rather than following their intention. More regulation could well cause more problems than solutions.

We consider that the revised Code is a very big step in the right direction but it will not, in itself, be sufficient. We are concerned that little will change without active leadership and encouragement from the FRC, enlightened and active shareholders and other stakeholders, company chairman and probably the media. ACCA offers its full support to help bring about the right changes in attitude and practice. We believe that the price of failing to encourage such change would be high: it would most probably mean the imposition, perhaps from Europe, of heavy handed regulation and enforcement.

It is primarily peoples' values which determine how they behave and whether they comply with the spirit, or just the letter, of rules, procedures and codes. We therefore strongly suggest that the revised Code should make reference to values in its main principles. We propose that the words *'The board should set the company's values and standards'* be elevated from a supporting principle to A1 to become a new main principle. We would also add *'and ensure that they are in place'*. The new principle would therefore say *'The board should set the company's values and standards and ensure that they are in place.'*

The supporting principles to A1 are probably the most important in the Code. Given this importance, and as an alternative to elevating part of these supporting principles, the Code could ask that companies pay particular attention to stating how 'in practice' they apply these particular supporting principles.

We have the following more detailed comments about the wording of the revised Code:

Governance and the Code - Definition of corporate governance

We are pleased to see the inclusion of this definition of corporate governance. We highlighted above the importance of having the right values. We therefore suggest that the definition be expanded to include boards' responsibility for setting, and ensuring adherence to, company values.

Chairman's Preface

It might be appropriate to re-title this '*Preface by the Chairman of the FRC*' to avoid any confusion among those who do not closely study the Code that it may refer to another chairman.

Comply or Explain

We support this section. We are pleased that paragraph 2 implies that companies should apply both the main and the supporting principles and report how they have done so. In 2008, however, the Listing Rules were amended and the word '*main*' was inserted in front of principles so that companies no longer need to say how they apply the supporting principles. We think this change was unfortunate; it could help to bring about the required changes in behaviour if companies were asked to state how they apply both the main and the supporting principles.

The supporting principles to the first principle A1 are particularly important and encapsulate the essence of corporate governance as far as the board is concerned. As suggested above, asking companies to say how they apply these particular principles should help ensure that good governance is seen as being fundamental to strategy and business success.

Principles

A Leadership

We support the addition of the words '*long term*'. We are also pleased to see the new supporting principle about fiduciary and statutory duties. The problems in the banking sector highlighted an apparent lack of attention by the directors of some banks to their fiduciary duties as set out in the Companies Act 2006. It may therefore be helpful to include these duties in an appendix or footnote to the Code.

We have also set out above our rationale for disclosure of how boards apply these supporting principles, particularly how boards set company values and ensure they are in place.

A3 Chairman and A4 Non-executive directors (Neds)

Lack of challenge by Neds seems to continue to be a major issue in spite of the work done in this area by the late Sir Derek Higgs and others. We support the new principle that Neds should constructively challenge and develop proposals on strategy. The support of the chairman in encouraging and developing this approach from all directors is vital. We therefore also support the new requirement in the supporting principle to A3 that the chairman should promote a culture of openness and debate.

More may need to be done to bring about the required change in behaviour and temperament. To help to encourage a culture where constructive challenge becomes common, Board Development (B4) could include facilitated meetings where board members can role play dealing with testing situations, such as involving difficult moral dilemmas, where such challenge may be required. This is something which the Institute of Chartered Secretaries and Administrators (ICSA) could consider in its update of the good practice guidance in the Higgs Report on the roles of the chairman and Neds.

B7 Re-election

We acknowledge the arguments for introducing annual re-election of directors and the chairman but are concerned that this could further contribute to what is already a short term focus by many boards and shareholders.

C2 Risk Management and Internal Control - Risk Appetite and Tolerance

We support the intention to extend the main principle to state boards' responsibility for defining risk appetite and tolerance. It is important they take greater responsibility for managing risk, including being clear about the sort and level of risk they want to take.

Unfortunately, as was and arguably still is the case with assessing the effectiveness of internal control, it is much easier written than done. Few companies outside the financial sector have taken any meaningful steps to be clear what they mean by risk appetite and tolerance and even fewer have made any sensible use of the words. The terms mean different things to different people, even within the same organisation.

In the financial services sector there is more clarity about the terms, but risk appetite and tolerance are set according to numerical indicators and treated like a budgetary control process. With hindsight, it is now clear that such an

approach blindsided some banks into misunderstanding and mismanaging risks that were critical to them.

We are currently conducting a survey about risk appetite and tolerance and will pass the results to you later in March. We think, therefore that the wording in the principle will need to change and would be pleased to discuss this with you once we have completed our study.

D1 Remuneration

In view of the furore about bankers' pay, it could be time to review the wording in the main principle. It says '*Levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully*'. The vast majority of people do not require high levels of pay to attract, retain and motivate them. Providing they have what they regard as a sufficient level of pay, other factors play a greater role in motivating them.

This should be another topic for consideration by the ICASA as it updates the good practice guidance.

Enforcement and Shareholder Engagement

After nearly two decades of a voluntary enforcement system for governance predicated on the notion that shareholders as a group provide the necessary oversight of boards, we have to conclude that it has not worked well enough. We regret that it may be necessary to introduce stronger enforcement mechanisms.

The proposed Stewardship Code should be a step in the right direction but we remain doubtful whether it is possible for concerned shareholders to exercise the necessary oversight given the diversity of shareholders. Consideration should be given to giving shareholders a vote on a company's corporate governance report. Such a vote could be in two parts, on how companies apply the Code principles and on companies' compliance and explanations for non-compliance with Code provisions.

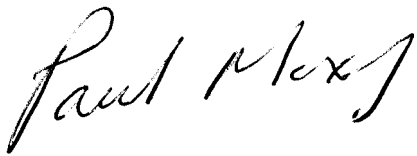
The FRC may wish to consider, and consult on, whether governance standards could be improved further by more active monitoring by them of the quality of corporate governance reports. There is, perhaps, a public interest case for this given that many other stakeholders, besides shareholders, have an interest in companies being well governed.

Concluding Remarks

We hope that the new focus in the revised Code will bring about the necessary changes, such that boards and shareholders develop a greater understanding of what good corporate governance is and how to recognise it. In our view, the principles (main and supporting) set out the essence of good corporate governance so far as is known at present. What is now needed is focus by boards, shareholders and other interested stakeholders on these principles. For this reason, clear and non-boiler plate statements by companies of how they apply the principles should give shareholders a better basis on which to engage with boards and hold them to account for good governance. We would be pleased to help in facilitating these changes.

As set out above, I will forward the results of our work on risk appetite and tolerance to you later this month. In the mean time please let me know if there is anything in the above you would like to discuss.

Yours sincerely

**Paul Moxey**

Head of Corporate Governance and Risk Management