



## The ABI's Response to the FRC's Review Of The Impact Of The Combined Code

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### Introduction

1. The Association of British Insurers, on behalf of its Members who are institutional investors owning around 20% of the shares of UK-listed companies welcomes the opportunity to respond to this consultation on the impact of the Combined Code. This focus on assessing the effectiveness of the Code is the right one since it is this that should determine whether it is well-drafted. We continue to believe the Code works well and that there is no pressing need to change its provisions. Indeed the Code continues to make a strong contribution to the effectiveness of the UK's corporate sector, avoiding unnecessary and burdensome regulation but ensuring that through an appropriate measure of accountability to shareholders that governance structures are balanced and effective that helps companies pursue their business activities in a manner that creates sustained value.
2. As the consultation document itself recognises there are EU developments in a number of areas that have implications for the Code. Accounting and auditing, including the role of audit committees and the scope of their reporting to shareholders, is one broad subject area where there are a number of possible developments in respect of which where there may be a role for the Combined Code to embody evolved best practice. The FRC's own project on Audit Competition is one example of a potential agent of change in this regard but there are others.
3. There would be sense in envisaging the possibility of a need to update the Code to reflect regulatory and other developments on a number of fronts and to plan with a view to consultation at an appropriate future time on updated guidance. However, we would emphasise our central message that the Code continues to work well and that there is no obvious need for a revision of the Code in order to improve its effectiveness.
4. We continue, however, to have concerns over the provision in the Code, contained within Paragraph A.4.3, that "No individual should be appointed to a second chairmanship of a FTSE 100 company". This is prescriptive wording that appears out of keeping with the principles-based ethos of the Code. The need for individuals to have sufficient time to provide to the role and to be available in the event of crises is already made clear in the rest of this paragraph of the Code. The efficacy of the prescriptive provision is also in doubt since it focuses narrowly on the holding of other company chairmanships within one part of the listed market and ignores time commitments elsewhere both inside and outside the corporate sector which, individually or cumulatively, might be very significant. Accordingly, we suggest that consideration should be given to whether the prescriptive wording relating to dual FTSE 100 chairmanships should now be deleted.

## **Specific Comments on the Consultation Questions**

### **Q1 Does the Code support better board performance over time?**

Yes, we believe the operation of the Code has been a powerful spur to increased professionalism of Boards and to ensuring that the unitary board system works well in a practical way that is consistent with its objectives. The role of non-executive directors has developed in important ways, including through the roles played by audit and remuneration committees. The practical importance of these roles played by the NEDs which are complementary to the business and management roles played by the executive directors will have contributed to cohesiveness of boards and to improved overall decision-making. The Code's carefully crafted provisions regarding periodic assessment of board effectiveness in turn ensures that where board performance is not at the highest level this can be identified and remedied.

### **Q2 Is the “comply or explain” approach working effectively?**

Yes, we consider the 'comply or explain' approach to be of utmost value and importance and it is the embodiment of this design principle in the Code that has ensured the Code's effectiveness. This is the antithesis of a legalistic and regulatory compliance-driven approach and it ensures the flexibility exists to make departures from the Code's provisions where this is justified.

It is important, though, that the company can provide cogent and convincing explanations of departure from the Code where it has taken the decision follow that course. We do not consider concerns about 'box-ticking' by investors to be well-founded. It is as likely to be the case that companies who have doubts about their ability to make adequate explanations have themselves fallen back on a compliance with checklist approach to minimise the likelihood of criticism.

### **Q3 What impact has the Code had on smaller companies?**

We have always been sensitive to the concerns of smaller companies that the compliance burden will be proportionately greater for them than those of larger size though there is no particular reason to conclude that this concern would be greater in respect of the Code and its 'comply or explain' approach than with any approach to governance or compliance. The Code already contains derogations in certain respects and, in practice, institutional investors would expect the volume of disclosure by smaller companies to be significantly less than that of large ones.

The FRC is right to wish to maintain an open mind. For our part we intend to give further thought to this subject and have agreed with the Quoted Companies Alliance (QCA) to aim to do so through a joint event later this year.

**Q4 Do disclosures on the Combined Code in annual reports provide useful information to shareholders at proportionate cost to companies?**

Although there clearly are costs incurred in applying the provisions of the Code and reporting on this to shareholders through the Annual Report we believe these costs are dwarfed by the substantial benefits provided by the operation of the Code and in providing information to shareholders that is necessary if they are to exercise their stewardship responsibilities effectively. It should also be noted that governance-related disclosure does not relate exclusively to Combined Code obligations and that legislative requirements for disclosure such as under the Directors' Pay Regulations may be voluminous by comparison. The ability under the Code to report by exception is an important means of both saving on space and providing relevant information in an accessible and digestible form.

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