

Chris Hodge
 Corporate Governance Unit
 Financial Reporting Council
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29 May, 2007

Dear Mr Hodge,

Consultation on the Combined Code

I have pleasure in submitting a response to the above consultation on behalf of UK Shareholders Association ("UKSA"). UKSA is the leading independent organisation representing private shareholders in the UK. Our response has been prepared by a group of such shareholders all of whom have many years' practical experience of the operation of stock markets both in a business and a private capacity.

Directors' pay

The provisions of the Code are well meaning, but have been unable to prevent the ratchet effect against which the supplementary principle of Section B.1 specifically warns "...[*The Remuneration Committee*] should use such comparisons with caution, in view of the risk of an upward ratchet of remuneration levels with no corresponding improvement in performance". In view of public concern about levels of top remuneration, it could be of value if the wording were strengthened. E.g. after the words quoted above one could add "*The committee should recognise that not every company can pay above the upper quartile, nor even above the mean. Any claim to target above the average must be justified.*"

We also believe that the Code should recognise the influence of remuneration consultants and impose on them certain responsibilities:

- 1) Where consultants have been appointed to advise the committee they should be named (Section B),
- 2) Where consultants have not been appointed an explanation should be given in the Remuneration Report (Section B),
- 3) A representative of the consultants should attend the AGM to answer shareholders' questions. (Add to Section D.2)

UKSA further believes that share options are counter to shareholders' interests, rewarding volatility and not performance. This is particularly true of regular option awards, which guarantee a benefit provided oscillations about the trend are wide enough. The only case when an option grant is unambiguously appropriate is on the appointment of a new executive from outside the company:

- 1) The Code should state that, if the company consider options to be performance-related, that treatment should be justified,
- 2) The encouragement in the Code given to regular performance rewards should specifically exclude options (Schedule A:5). An additional clause should be added

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to Schedule A to state that regular option awards are not performance-related and should be discouraged.

AGM

Shareholders appoint the auditors and rely on their oversight of the company's accounting principles. A representative of the auditors should attend the AGM to answer questions on those principles (but need not answer other questions on the accounts). (Add to Section D.2).

Responses to specific questions

Is the “comply or explain” approach working effectively?

We cannot comment from a corporate viewpoint. However ‘comply or explain’, as a form of exception reporting, is an effective model of communication for the private shareholder.

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


UKSA believes that the transparency engendered by companies having to explain their governance principles in the annual report has been important for improving standards. However it must be admitted that, because the Code has promoted a standard model of governance to which all companies increasingly adhere, many such reports have become boilerplate. So they are rarely read, because they are not expected to say anything unusual.

We suggest that communication would be improved if the Code promoted a Standard Governance Report analogous to the function of Table A in company Articles. Companies could then report in terms of ‘differences from standard’. This would shorten the printed report, draw attention to items that matter and align with the principle of “comply or explain”.

General

We would be very happy to discuss any issues arising from this letter. Should you wish to take this up I suggest that you contact my colleague John Hunter in the first place as he has worked closely on this response. (01689 855774 or johnheather60@aol.com)

Yours sincerely



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