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7 October 2009

Date Sir

Review of the effectiveness of the Combined Code – Progress report and second consultation

We write in response to the invitation to provide any additional comments or other evidence on the issues identified in the above document. Our views are set out below. They should be read in conjunction with the comments set out in our letter of 29 May 2009.

FRC guiding principles on amendments to the Code

1. We agree with the three proposed guiding principles for addressing the case for changes to the Code and in particular with the principle of the FRC seeking to avoid an increase in the overall level of prescription in the Code and to preserve its principles-based style. However, we recommend that there should be a fourth principle – adherence to the concept of proportionality – to ensure that the generality of listed companies are not burdened inappropriately with provisions considered necessary only for a few. The FRC will no doubt consider the recent reform of the Listing regime recently announced by the FSA and its potential impact on application of the Code.

The application of the recommendations arising from the Walker Review

2. On the basis of the above suggested additional principle, we consider that the recommendations arising from the Walker Review are best dealt with in FSA rules and guidance specifically for BOFIs rather than in the Code.

Responsibilities of Chairmen, Senior Independent Directors and Non-Executive Directors

3. We do not support further clarification of the individual roles, key responsibilities and behaviours of chairmen, senior independent directors or non-executive directors. This might undermine the concept of the unitary board.

4. We agree that NED time may need to increase. But, rather than specifying prescriptive time expectations, we believe that there may be scope to emphasise that the time required needs to be proportionate to the size and complexity of the business and the issues facing the board. Any relatively heavy prescriptive time expectations would appear to be contrary to the proposed guiding principles and could deter capable executive directors taking on non-executive roles in other companies, thereby reducing the pool of talent able to take on non-executive directorships.

Board balance and composition

5. There is a need to balance experience against independence. We therefore support more flexibility based on disclosure rather than retaining the current nine year independence rule or maintaining the provision for boards to include 50% independent NEDs. We consider that there is a need to tilt expectation towards having the right directors sitting on the board. This would help reverse the drift towards fewer executive directors, which may reduce the possibility of fully informed board debate.

6. We are not convinced of the need for more detailed guidance on succession planning or on ensuring that the board composition is aligned with the present and future needs of the business. However we support the need for these matters to be given further emphasis in say the preamble to the Code.

Frequency of director re-election

7. We are against annual re-election of the chairman or board committee chairs. This would undermine the unitary board concept and lead to tensions among board members. An annual re-election would also deter some people from taking on these roles because of the risks to personal reputations. It may also create pressure for increased remuneration.

Board information, development and support

8. We agree that NEDs should have an excellent knowledge of the business but would be against changing the Code in this area. We are also strongly against the creation of independent secretariats to support NEDs which would engender greater board divisiveness.

Board evaluation

9. Externally facilitated evaluation is no substitute for a robust challenge between NEDs and executives or for proper engagement with shareholders. However, we see merit in the proposal for an externally facilitated review every two or three years for listed companies.

Risk management and internal control

10. We continue to support a review of the Turnbull guidance. In addition to the suggestions we have made previously, we consider that the review could usefully focus on keeping fresh the identified significant risks and challenging whether there is unnecessary bureaucracy particularly over non-significant risks.

11. We are against mandatory risk committees or client risk officers for all listed companies. Risk management is a responsibility for the board as a whole and should be embedded throughout the business. Transaction risk is a matter for boards as a whole to take responsibility for rather than audit committees.

12. Reporting on risks should be left to a wider review of what should be done to rationalise the front half of annual reports.

Remuneration

13. We do not agree with an extension of any new remuneration requirements for BOFIs to the generality of listed companies. Also, any remuneration disclosure changes arising from sources such as the EU are best dealt with through amending statutory regulations. We support the existing non-binding vote system for shareholder oversight of director remuneration.

Quality of disclosure by companies

14. We do not support a formal role for the FRC or the FSA in monitoring and enforcement of comply or explain statements. This should be left to shareholders as part of a governance rather than regulatory process. Otherwise there is a danger that the boundary between governance and regulation would shift unnecessarily towards regulation and would actually undermine the position of UK governance which is rightly perceived as a world leader.

Engagement between boards and shareholders

15. We are unclear about the effectiveness of that part of the Code that deals with investors. Perhaps it can be subsumed into the public consultation on the proposed Principles for Stewardship. We believe that the Principles for Stewardship should put sufficient emphasis on the longer term perspective rather than merely short term trading.

Apply or explain

16. We acknowledge that there is merit in using the terminology 'apply or explain' rather than 'comply or explain'. The latter phrase is being perceived unfavourably and as contrary to the spirit of the Code.

Martyn Jones and Isobel Sharp would be pleased to discuss with the FRC our comments and other matters related to the review of the Combined Code.

Yours faithfully

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