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Ms C Woods
Financial Reporting Council
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3 February 2016

Virgin Money's response to the UK Board Succession Planning Consultation paper – October 2015

Dear Ms Woods,

Virgin Money welcomes the opportunity to respond to the Financial Reporting Council ('FRC') consultation paper on UK Board Succession Planning and is supportive of the overarching principles set out in the consultation paper. Succession planning is a strategic imperative and the link between strategic planning, corporate culture and succession planning is a key part of good governance.

We believe that the promotion of 'good practice' in this area will be helpful to many companies and investors.

We agree with the FRC's view that good succession planning contributes to the long-term success of a company and will help to ensure a supply of suitable people to take over when individuals leave a business. This also supports the delivery of the strategic plan by aligning human resource requirements with business planning and also demonstrates a commitment to career development for employees which aids recruitment and retention.

Please find attached our detailed feedback on the discussion paper. Our key points are:

Investor Engagement

- We support the use of pro-active communication with Institutional Investors, and believe it is key to good stewardship and a market that functions well. The succession planning framework is a good foundation for discussion which should facilitate constructive conversation. We also agree that Institutional Investors should not be involved in the management of the appointment process (or nominating directors).

Diversity

- We agree that a good succession plan should include an objective to address diversity. We find that many executive search firms and recruitment specialists are actively seeking greater diversity in their respective applicant pools in answer to their clients' requirements.

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- There are initiatives underway that are beginning to encourage greater diversity such as those stemming from the Davies Report. In addition, the government review on the representation of women in senior managerial roles in the financial services industry is expected to publish its report in March 2016. This review is led by Jayne-Anne Gadhia, our CEO.

- However, there is more to do across the spectrum, to remove unconscious bias and to reposition Financial Services, in particular, to dispel current negative images and assumptions and attract more diverse talent at all levels. We believe that reporting on diversity might be expanded to provide greater opportunity to benchmark and compare organisations.

Nomination Committee

- We agree that a nomination committee with a clear remit which meets at a frequency commensurate to delivering the company's succession plan is helpful in supporting the Board to deliver succession planning for the company.

- Whilst we personally have not experienced the observation of the Parliamentary Commission on Banking Standards that there is a 'widespread perception that some "natural challengers" are sifted out by the nomination process,' we strongly support the statement made by other contributors to the working group that 'challenge is integral to the role of non-executive directors' and would highlight its place in the running of an effective Board.

- In the interests of transparency and support of the requirement for 'fair, balanced and understandable' disclosure in the annual report and accounts, we would encourage disclosure of the objective criteria used in the search of Board candidates and for this to be set out in the nomination committee report.

Pipeline

- We agree that a robust talent review process is a key element of good succession planning and brings wider colleague engagement benefits across a company. However, we consider that the current structure of the recruitment market (which is quite short term in view) may need to shift before a wide spread use of external pipelines might be implemented.

We would be happy to discuss our views on this topic in greater detail if this would be helpful.

Yours sincerely

KJ Foshall

pp **Glen Moreno**
Chairman
Virgin Money

Virgin Money's response to the UK Board Succession Planning Consultation paper – October 2015

Dated: 3 February 2016

Our response addresses the key themes raised in the Consultation paper.

Business Strategy and Culture

Consultation observations:

"Central to the Code is Main Principle A.1 which states that 'Every company should be headed by an effective board which is collectively responsible for the long term success of the company.'

The consultation states that the Code makes clear that long-term business success and good governance go hand-in hand. Therefore, an effective board must take the lead in shaping and embedding a sustainable corporate culture and this is central to its purpose. It is clear from our research that the absence of strategic, thoughtful and practical succession planning can be a substantial risk to long-term success. In terms of delivering the business strategy and maintaining or enhancing investor confidence, the board carries most responsibility, and without effective succession planning the risks to the company are increased. The absence of a succession plan is also rightly seen as an indicator of poor governance."

Virgin Money response:

We concur that the link between strategic planning, corporate culture and succession planning is a key part of good governance, with the organisation's design and its people supporting the strategic intent. In our view the most pragmatic and practical way of ensuring a cohesive approach is to consider succession planning as part of the regular strategic review process. Aligning the human resource requirements with business planning ensures early identification of skills gaps and the ability to plan for orderly succession.

In terms of reporting, best practice in narrative reporting already highlights the need to link strategy and governance. Reporting could be covered at a high level in a company's annual report and accounts, via the nomination committee Report. Whilst in principle we are supportive of transparent and balanced disclosure on the rationale for appointments and more 'forward looking' succession planning disclosure, this may not always be possible. For example, detailed reporting on occasions might be restricted by the level of confidential or price-sensitive information inherent in the nomination / recruitment processes.

Nomination Committee

Consultation observations:

"The Code recommends that 'the search for board candidates should be conducted, and appointments made, on merit, against objective criteria and with due regard for the benefits of diversity on the board, including gender.' It also says that boards should satisfy themselves 'that plans are in place for orderly succession for appointments to the board and to senior management, so as to maintain an appropriate balance of skills and experience within the company and on the board and to ensure progressive refreshing of the board.'

The consultation states that from the FRC's discussions with stakeholders; clarifying the role and responsibilities of the nomination committee, and raising its profile, are key factors in *promoting the importance of succession planning. A properly functioning nomination committee with clearly defined roles for the Chairman, Senior Independent Director and the Chief Executive Officer should be evident from disclosure and reality.*

Grant Thornton's Corporate Governance Review 2014 found that the nomination committee met fewer times annually (3.3 on average) compared to other committees; fewer committee Chairmen introduced the nomination committee report (35%); and the quality of disclosure did not match that of other committees. In 12 companies, the committee did not meet during the year. Some see the nomination committee as the 'poor cousin'.

Further, some suggest that alongside board appointments, a properly functioning nomination committee should also consider the senior management team as well as having a broader oversight of talent management.

As part of the FRC discussions undertaken for the paper: the observation made by the Parliamentary Commission on Banking Standards 'that there was a 'widespread perception that some "natural challengers" are sifted out by the nomination process' was broached. The consultation states that it found virtually no assent to this."

Virgin Money response:

Nomination committee reporting could be improved by enhancing the requirements under Code Provision B.2.4 relating to 'describing the work of the nomination committee' to explicitly require a description of a company's approach to succession planning and talent management and the progress made in year. This will ensure sufficient focus by the committee on both Board appointments and senior management succession whilst giving companies the flexibility to 'comply or explain.'

Whilst we have not personally experienced the observation of the Parliamentary Commission on Banking Standards that there is 'widespread perception that some "natural challengers" are sifted out of the nomination process,' we strongly support the statement made by other contributors to the working group that 'challenge is integral to the role of non-executive directors'. We would highlight the importance of challenge in the running of an effective Board.

In the interests of transparency and support of the requirement for 'fair, balanced and understandable' disclosure in the annual report and accounts, we would encourage disclosure of the objective criteria used in the search of Board candidates and for this to be set out in the nomination committee report.

We agree that a nomination committee with a clear remit which meets at a frequency commensurate to delivering the company's succession plan is helpful in supporting the Board to deliver succession planning for the company. Subject to the comment above regarding succession planning and talent management, we agree that the responsibilities of the nomination committee are well articulated in the Code principles and provisions.

We note that the consultation asks for information about the experience of publicly advertising for non-executive positions in that doing so could offer access to a wider range of candidates who might otherwise have been overlooked. The consultation acknowledges that public advertising can bring with it associated time and resource costs which may outweigh the risk of self-selection from a narrow pool. Whilst we accept that publicly advertising may lead to access to a greater range of candidates, we feel there to be a well developed professional search industry for non-executive positions which we will continue to utilise. From our experience these executive search firms and recruitment specialists are actively seeking greater diversity in their respective applicant pools in answer to their clients' requirements.

We believe that the method of applicant search is often individual to a company and even to an individual role. As such companies should be free to choose the most appropriate method to identify the best range of candidates for any role.

A properly functioning nomination committee is and should be of importance to investors and a key governance item of discussion between investors and principally the Chairman of the Board. We would fully endorse that the absence of a succession plan can undermine a company's effectiveness and its sustainability; both key considerations for investors.

Board Evaluation

Consultation observations:

"The Code recommends that the board should undertake 'a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors' (Main Principle B.6). FTSE 350 companies are subject to an additional provision to carry out an externally facilitated evaluation at least every three years.

The consultation proposes that integrating board succession planning with a comprehensive annual board assessment improves board and committee performance and also provides a basis for altering the composition of the board and making sure that the right people are chairing the principal committees. An effective evaluation should not simply determine how well individual board members are performing; it should also address the important issues of teamwork and board dynamics, which directly affect how well the board performs its functions.

The paper highlights that some companies use matrices to provide analysis of boards in terms of a number of factors linked to meeting strategic objectives. Such matrices are often further developed to take into account non-executive directors' terms of appointment, governance issues and any company policy on board refreshment. In terms of executive board positions, these plans can also be applied to and linked with personnel just below board level in respect of performance and leadership potential, and annotated in terms of the key considerations for their future development. The results of such an analysis can then be used to inform the search or identification of potential candidates well before an appointment is needed. However there was debate as to the level of effectiveness of the matrices.

Virgin Money response:

We fully support the practice of undertaking an annual board evaluation process which considers composition as well as performance. However, we would highlight the difficulty which may arise in the timing of the respective matters considered by Boards. The consultation suggested that succession planning should link to strategic development. Whilst we agree with the rationale for such an approach, for some companies, the ability to schedule a full strategic review at the same time as a board evaluation process may be constrained by resource. Given the importance of both processes, this may impact the quality of output. We believe companies should have flexibility to schedule their annual board evaluation process at a time which fits well with other Board commitments when sufficient time commitment and focus can be given by all Directors.

More detailed reporting on changes to a company's succession planning process resulting from a Board evaluation would perhaps be beneficial, particularly for investors. The annual evaluation would act as a useful checkpoint on succession plans in particular regarding non-executive directors and their preferred tenure. On occasions there may be barriers to full disclosure on the basis that the information may be confidential or potentially price sensitive.

In terms of the use of succession planning matrices, whilst this is clearly one methodology it should be for the nomination committee to determine the approach to Board refreshment and succession planning. Clearly companies may find matrices useful to identify key skills and strengths relating to an individual role or to support a capability gap analysis, they are less precise and therefore may not be as helpful when applying them to the assessment of overall board effectiveness and succession planning on a wider basis.

Pipeline

Consultation observations:

"The consultation highlights that a key part of long-term succession planning involves the ongoing assessment and professional development of internal candidates in order to consider their suitability for senior roles. Boards therefore need to become more familiar with individuals in the pipeline, but it appears that many struggle over how best to do this. The extent to which external candidates should be tracked and assessed for executive and non-executive board appointments when they arise (and the need for external recruitment overall) are also important aspects of long-term succession planning. Ensuring a pipeline of diverse candidates ready for consideration for board or other senior appointments requires continuous identification, evaluation, development and preparation.

The consultation suggests that good practice in terms of the balance of responsibilities for the pipeline occurred in those companies where information was openly shared between HR, CEO, Chairman, Board and nomination committee, debated and acted upon; with effective collaboration between all parties.

The paper states that visibly good internal succession planning in a company demonstrates a commitment to developing talent which brings wider benefits such as better morale and improved competition for internal roles. In addition, remuneration packages tend to be lower when internal candidates are promoted and may help counter the ratcheting up of pay that has gained media attention."

Virgin Money response:

We agree that a robust talent review process is a key element of good succession planning and brings wider colleague engagement benefits across a company. The establishment of an external pipeline in which the candidates are tracked and nurtured is a more difficult task. It can be labour intensive and costly. The current structure of the recruitment market (which is quite short term in view) may need to shift before a wide spread use of external; pipelines might be implemented.

Our Annual Capability Review takes the corporate strategic goals, and provides a capability gap analysis looking out over an eighteen month to two year period. This is considered in conjunction with a judgement of retention risk and talent identification and development.

Diversity

Consultation observation:

"The 2010 Code update introduced the need to consider gender when evaluating a board's effectiveness (supporting principle to Main Principle B.2), while the 2012 version required

greater reporting about a board's policy on diversity generally (Provision B.2.4). The preface to the 2014 version of the Code expands this further:

... One of the ways in which constructive debate can be encouraged is through having sufficient diversity on the board. This includes, but is not limited to, gender and race. Diverse board composition in these respects is not on its own a guarantee. Diversity is as much about differences of approach and experience...'

In terms of succession planning, the major benefit of diversity is avoiding 'groupthink' – when conformity in the group can result in poor decision-making outcomes.

The consultation finds that the need or perceived need to be 'board ready' has come under the spotlight as more women are appointed to boards. Some have claimed that less experienced individuals are being appointed as non-executive directors as a result. Previous board experience is only one aspect of an individual's qualities and experience, however, and boards need to have regard to the risks of unconscious bias, and the natural tendency to prefer the familiar and the status quo.

There has been some debate about the Code's reference to a nine years' tenure period for independent non-executives. It is said that this has hindered the increase of women on boards, either because the period is too long, or because companies are not observing the Code and too many directors are serving greater than nine years."

Virgin Money response:

We agree that a good succession plan should include an objective to address diversity. We find that many executive search firms and recruitment specialists are actively seeking greater diversity in their respective applicant pools in answer to their clients' requirements.

There are already initiatives underway that are beginning to encourage greater diversity such as those stemming from the Davies Report, through the setting of targets and an ethos regarding representation at Board level. In addition, the government review on the representation of women in senior managerial roles in the financial services industry is expected to publish its report in March 2016. This review is led by Jayne-Anne Gadhia, our CEO.

However, there is more to do across the spectrum, to remove unconscious bias and to reposition Financial Services, at both a tactical and strategic level to dispel current negative images and assumptions and attract more diverse talent at all levels of the organisation. We believe that reporting on diversity might be expanded to provide greater opportunity to benchmark and compare organisations.

We do not consider the 9 year term a restricting factor, as it is a maximum term and does not preclude shorter tenure on a board. In terms of 'board readiness' it is incumbent on all directors to undertake continued development whilst in role and good induction and ongoing training supports board members, whether that be in terms of the company's developing business, emerging regulation or personal development. In addition companies have the flexibility to 'comply or explain' if they can justify the independence of a non executive director who has served more than a 9 year term.

We support the view of the FRC that the refreshment of the board is considered in the full context of the requirements of the company's business strategy; its current board's set of competencies and how best changes in membership would serve the company in the future.

Institutional Investors

Consultation observation:

Major investors clearly have an important role to play in succession planning. It is in their interests to ensure that there is continuity in the governance of the companies in which they invest and that the development of the business can be sustained effectively through the appropriate development and refreshment of the board. The majority of investors we spoke to said that the subject of succession planning should be on the agenda when they meet board members. In their view the conversation should include a wide range of succession issues – the board evaluation and current functioning; the need to refresh both executive and non-executive positions in pursuit of board effectiveness; board diversity; consideration of potential candidates just below board level; and the plans for 'emergency' succession. For the most senior roles, investors would prefer to be in a position to suggest the particular attributes they believe candidates should have.

Some large investors survey the market themselves for likely candidates, making recommendations to the Chairman, and keep abreast of the development of internal candidates for succession. However, for other investors there is a reluctance to become too involved and no-one we spoke to thought that it was a good idea for investors to be party to the management of the appointment process.

As with board evaluations there are inevitably sensitive issues of confidentiality and there are necessarily limits to what a company can disclose publicly. Many investors told us that the underlying principle was that they should at least have confidence that the company had an effective overall plan reviewed, updated and acted upon. This was seen by many as a good indicator of how the board is working. Investors are also interested in the structure and responsibilities within the board for succession planning.

Virgin Money response:

We support the use of pro-active communication with Institutional Investors, and believe it is key to good stewardship and a market that functions well.

We also agree that Institutional Investors should not be involved in the management of the appointment process (or nominating directors). We endorse the view expressed in the consultation that the level of disclosure and discussion around succession is inevitably constrained by issues of sensitivity and confidentiality. However, the succession planning framework is a good foundation for discussion and should allow constructive conversation.

Kgrashall

pp **Glen Moreno**
Chairman
3 February 2016