

Thursday 8<sup>th</sup> October 2009

Chris Hodge



Corporate Governance Unit  
Financial Reporting Council  
Fifth Floor

rlam

Aldwych House

55 Gracechurch Street

71-91 Aldwych

London EC3V 0UF

telephone

London WC2B 4HN

020 7506 6500

fax

020 7506 6501

website

www.rlam.co.uk

Dear Chris,

Please find below Royal London Asset Management's contribution to the FRC's review of the effectiveness of the combined code.

#### FRC – Review of the Effectiveness of the Combined Code

Royal London Asset Management welcomes the opportunity to contribute to the FRC Review of the effectiveness of the Combined Code. We would add our support to continued adoption of the principle of comply or explain which underpins the Combined Code. We do not believe that recent experience within the banking sector should be taken as evidence against continual adoption of this fundamental approach. We would also add our support to the continual adoption of a unitary board where the whole board has to take responsibility for decisions. This does not prevent the board making use of certain sub-committees in order to help its ultimate functioning but this must not be allowed to develop into the delegation of ultimate responsibility for decision making from the whole board or to the development of two-tier boards.

We are very aware of our responsibilities as an institutional shareholder and that there are lessons to be learnt following on from this most recent period. In this context we are supportive of initiatives which are currently underway through the ISC to improve ways in which the governance process can be undertaken. Ultimately we believe that having the endorsement of the FRC to the results of the ISC's work would be very helpful.

We set out below comments relating to the specific topics raised by the FRC:

#### **Role of the Chairman & Senior Independent Director**

We feel that there needs to be a clear restatement and clarification of the SID's role in times of particular stress. At such times it is essential that the SID take on the role of properly understanding the shareholder perspective and to bring that clearly to the attention of the whole board. We do not believe that this role has been fully understood

rlam is a marketing brand including the following companies: Royal London Asset Management Limited registered in England & Wales number 2244297; Financial Services Authority (FSA) register number 141665. Royal London Pooled Pensions Company Limited registered in Scotland number SC048729; FSA register number 110456. Royal London Unit Trust Managers Limited registered in England & Wales number 2372439; FSA register number 144037. Royal London Cash Management Limited registered in England & Wales number 1963229; FSA register number 121844. All of the above are authorised and regulated by the Financial Services Authority. It also includes Royal London Asset Management Bond Funds Plc registered in Ireland number 364259 and regulated by the Irish Financial Services Regulatory Authority (IFSRA).

All these companies are subsidiaries of The Royal London Mutual Insurance Society Limited registered in England and Wales number 0099064. Head office: 55 Gracechurch Street, London EC3V 0RL.

by SID's as witnessed over the last couple of years and therefore greater clarity of the importance of the role and how it is expected to work would be very useful. In addition this clarification of the role of the SID should also encompass their ability to act as the sounding board for the executives if they have concerns over the role or performance of the Chairman.

It is highly likely that the Chairmanship of a large BOFI will require a substantial time commitment but we would not want to see a one-size-fits-all numerical target on this. We believe that individuals holding Chairmanships of the largest financial institutions would, and should, be expected to make this their priority. However, we do not believe that holding such a role should, necessarily, preclude such an individual from holding a significant position in another entity.

### **Board Balance**

We believe that creating the appropriate environment within boards, where active debate and potential dissent can be openly and constructively considered, is far more important than issues relating to definitions of independence or the time commitments that should be expected. Recent experience has clearly shown again that in many instances where there is a serious loss of shareholder value this can be due to a significant lack of checks and balances in the board rather than a question of the number of days that NED's gave. Ultimately it is the responsibility of the chairman to manage this, and they should be held directly to account for the successful management of this process.

We believe this can best be achieved through the Chairman creating the appropriate board environment where constructive challenge is both encouraged and is the norm. We believe that many corporate casualties have their roots in a board which has little constructive challenge and therefore where the Executive are not sufficiently held to account.

We believe that NED's should be prepared to give whatever time commitment is necessary in order to effectively discharge their duties. However, we do not believe that it would be appropriate to impose a one-size-fits-all numerical target against which an individual's contribution can be assessed. It would, we feel, be better to have less frequent yet high quality input than the reverse. We recognise however, that it is likely that the time commitments placed upon NED's will increase in future given the additional level of understanding that they will be asked to demonstrate.

### **Frequency of Re-Election**

As an institutional investor, we believe that annual re-election of board members, including the Chairman, may have its merits in that it could improve boardroom

accountability although application of any requirement must be on a proportional basis in relation to the size of the institution. In any event, we agree with the Institutional Shareholders Committee view that the chairs of all board committees should stand for re-election each year, again with due consideration being given to the size of the company concerned. We also have some sympathy with the growing view that all directors should stand for annual re-election. In this way we believe that shareholders would have the ability to express their dissatisfaction with the performance of any one or group of directors rather than using the chairman as a potential 'lightening rod' for such views. In addition we are supportive of the principle that whenever a certain threshold is not met then further action should occur has merit to it. This may involve the board having to formally respond to shareholders on the issue and what future actions are to be taken in order that a greater degree of support should be forthcoming in future. In addition we see merit in the idea that where the report of a specific committee does not reach a specific critical point (say 75%) then the chair of that committee should stand for re-election the following year.

#### **Board Information & Development**

We are opposed to the possible fragmentation of the board through the inappropriate use of committees and believe that issues such as risk appetite and strategic transactions have to remain the responsibility of the whole board and not rely upon the view of a sub-committee. For example, we believe that a board risk committee could be a useful tool in managing the due diligence process during a strategic transaction. However, we also believe that any decision on how to proceed with a strategic transaction should be the responsibility of the whole board. As a further example we believe that oversight of the overall remuneration policy is the responsibility of the Remuneration Committee. However the Board should ensure that it is consistent with the Company's attitude to risk and overall corporate strategy. We believe that responsibility for the implementation of the overall remuneration policy belongs with the board which should ensure that this is consistent with the company's attitude to risk and overall corporate strategy. Further, we acknowledge that a board risk committee may have a role to play in assisting the full Board to assess and manage strategic risks. However, we believe that the full Board should continue to understand, manage and ultimately have responsibility for such risks. In any event, we believe that the establishment of a board risk committee should be a decision for the company, having due regard for its circumstances, rather than a prescriptive requirement.

An area where we believe insufficient attention has been focused concerns that of boardroom succession planning. Over recent years we have seen a number of examples where it appears that issues relating to succession are not routinely considered which has led to poor planning and outcomes. We would therefore recommend that the FRC include in any revised Combined Code specific mention of the need for good quality and

regular consideration of issues relating to succession. This commentary could be included in the report of the nominations committee.

### **Board Evaluation**

We believe that regular and externally facilitated board evaluation would be a healthy development and over time should act to improve confidence in the running of the board. Any such facilitation cannot be undertaken by those where there might be a conflict of interest, for instance with remuneration consultants or recently used or retained search firms.

### **Engagement Between boards and shareholders**

We are supportive of the ongoing initiative from the ISC to explore ways in which institutional shareholders could discuss issues relating to the company's in which they are invested. This should result in ways in which representation can be made to management where substantive concerns exist in order that the company are aware that these concerns are held by a range of investors.

We believe it would be useful if a wide range of investors with a longer term perspective could be include in such initiatives of a common cause. In addition we believe that any such action should not simply be made up of the largest institutions but instead should involve all of those that can meaningfully demonstrate a commitment to governance issues and hence will bring good ideas to the table.

However we do not believe that these actions can be advance with a very formal arrangement which could be seen to bind institutions into a set process for discussing such issues with company management. A formal arrangement also risks having significant publicity attached to it on whether it had been initiated or not in a particular situation when in many occasions a lack of publicity can aid a successful resolution. An informal arrangement also fits far better with the reality that institutions can have a range of views on the appropriate outcome and therefore a formal arrangement risks discouraging some from involvement if their own views risk being completely subsumed. It will also be essential to the success of any arrangement that post any discussions among institutions that they all remain completely free to exercise their votes as they see fit. Similarly individual institutions would of course remain able to engage with management on a bilateral basis.

We agree that the sponsorship of any resulting document by the FRC would give it greater credibility. We also believe that it is important that any such document should be separate from any revised Combined Code. We subscribe to the view that any such code

should operate on a voluntary basis in order that managers can make the case to their clients relative to their respective investment process.

We are comfortable with the FSA authorisation process necessitating asset managers to clearly state their attitude towards the code and their reasoning. However we do not believe that it is the regulators role to explicitly encourage adoption of the code or that they should be monitoring shareholders compliance with the code. We do not understand why shareholders should be treated differently to corporates who do not have the FSA performing such a role. The way in which an institutional shareholder applies the code and its effectiveness should be a matter for the asset manager and their clients.



Robert Talbut  
Chief Investment Officer  
Royal London Asset Management