



Sir Christopher Hogg  
Chairman  
Financial Reporting Council  
5<sup>th</sup> Floor  
Aldwich House  
71-91 Aldwych  
London WC2B 4HN

June 1 2009

Re: Review of the Combined Code

I am writing in my personal capacity, but for your information I serve as senior fellow (and incoming executive director) of the Yale School of Management's Millstein Center for Corporate Governance and Performance and nonexecutive chair of Hermes EOS, as well as an advisor to several other funds.

As a member of the International Corporate Governance Network (ICGN), I fully support the statement submitted on behalf of the group in respect of this consultation. However, I wanted to expand on the ICGN's advice with a few additional suggestions for the FRC's consideration.

**A. Institutional Investors**

Commentators are right, in my view, that the Code should broaden to include guidance on investor responsibilities such as that produced by the ICGN itself, and by the Institutional Shareholders Committee. As to the content of such guidance, the FRC may wish to review recommendations that Jon Lukomnik, David Pitt-Watson and I have framed for a forthcoming journal article on reform of fund governance in different jurisdictions. In "Tomorrow's Investor: Refreshing the Paradigm for Pensions" (*Rotman International Journal of Pension Management*, Fall 2009), we suggest the following measures for pension schemes but which could be applied to institutional investors generally:

- (1) Each retirement plan should be required to disclose a statement on its governance and report annually on progress toward achieving best

practices. The statement should be subject to the scrutiny of an outside audit and submitted both to members and the appropriate regulator.

- (2) Pension funds should be required to report annually on oversight of conflicts of interest. If a plan does not address these risks, it should have to explain why. The statement should be subject to the scrutiny of an outside audit and review by regulators.
- (3) Retirement plans should be obligated to make a clear annual statement about their investment beliefs, how such beliefs are integrated into their investment practices, and how those investment practices will meet liabilities. The statement should specifically include a review of how compensation arrangements for portfolio managers and others are aligned with beneficiaries' interests. For example, if a pension fund expresses investment beliefs that include a long-term investment horizon but selects, evaluates and compensates its advisors and portfolio managers exclusively on short-term criteria, it should explain why. The statement should include a review of agent monitoring and evaluation and identify any overall investment performance benchmarks used to evaluate fund performance.
- (4) Each retirement plan should have to disclose annually how its investment approach identifies, evaluates and manages intangibles and externalities such as climate change, human capital, reputation and corporate governance, and monitors its agents and portfolio managers.
- (5) Fund scrutiny can be advanced by ultimate beneficiaries (workers and retirees) using social networking tools. The regulator, for instance, could require each plan it supervises to mount an interactive website enabling employees and retirees to review and comment on savings arrangements. Web 2.0 now enables collective user-generated ratings of services from medical practices to restaurants. It would be possible to do the same with pension plans to spur a race to the top, and help regulators police.

## **B. Board Nomination Process**

The FRC may wish to consider an additional matter in the corporate governance section of the Combined Code, namely improvements in information and processes surrounding investor votes on director candidates. Jon Lukomnik and I wrote a column in *Compliance Week* a year ago contending that votes on directors, once literally labelled "routine" by funds and their advisors, must now be understood as more akin to hiring decisions. Nomination committees and boards should clearly remain first line for decision making in this respect. But shareowners need to demonstrate responsible stewardship by making voting



choices in an informed manner. In our article, we recommended three specific measures:

- (1) Companies should produce more and better background information on candidates;
- (2) Boards should have candidates participate in outreach exercises such as pre-AGM conference calls and answering basic questions on their outlook and value to the company; and
- (3) Investors should develop a common enhanced candidate disclosure questionnaire focused on what they need to know about board nominees to arrive at informed choices. One such effort in response to our call, shaped for US conditions, was submitted to the Securities and Exchange Commission on May 19 2009. I have attached that for your information.

You can see our full article, "How to Hire a Director," at <http://blogs.law.harvard.edu/corpgov/2008/05/14/how-to-hire-a-director/>. Note that SEC chair Mary Schapiro told the US Council of Institutional Investors that "in June the Commission will consider whether to enhance disclosure around director nominee experience, qualifications and skills. The current rules only require a very brief description of a candidate's business experience over the past five years. That may not be sufficient in today's complex business environment. I want to make sure that shareholders have the information needed to make sound proxy voting decisions." I would recommend that the FRC consider taking similar steps.

Thank you for the opportunity to contribute to this consultation, which is important both to Britain and to other markets that draw from UK practice. Feel free to contact me should you have any comments or questions. I can best be reached on my Yale number, +1 203 432 9689, or via email [stephen.m.davis@yale.edu](mailto:stephen.m.davis@yale.edu).



Stephen Davis, Ph.D.  
Senior Fellow

ATTACHMENTS:

- A. Letter to Mary Schapiro on Disclosure Requirements for Director Candidates
- B. Sample Director Candidate Information Request

A

May 19, 2009

SENT BY EMAIL AND  
OVERNIGHT DELIVERY

Honorable Mary L. Schapiro, Chair  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

**Re: Disclosure Requirements for Director Candidates**

Dear Madam Chairman:

We write as global asset owners and investment managers with \$1 trillion of assets under management, representing the savings and pension assets of millions of individuals, to express our strong support for more detailed, relevant disclosures about director candidates and the candidate selection process.

In your April 6th address to the Council of Institutional Investors, you expressed concern regarding the sufficiency of current disclosure requirements for director candidates and indicated that investors should be provided with additional information to help them make informed decisions when casting their votes. We share your concern.

As major shareholders of American public companies, we believe that the election of directors is one of our most important responsibilities. It is the primary means through which we participate in a company's corporate governance and seek to safeguard both the value of our investment and future success of the corporation.

In order to determine how to best obtain needed information regarding director candidates, a group of global institutional investors consulted over the past year with corporate directors, executive search firms, proxy voting advisors, corporate legal counsel and institutional investors. Based on these inquiries, the attached Director Candidate Information Request was developed to seek additional information from both director candidates and company nominating committees.

The supplemental information requested of director candidates is intended to help investors assess the independence, competency and skills of the candidate, as well as understand the candidate's perspective on issues relevant to the company. The information requested of



Honorable Mary L. Schapiro, Chair  
May 19, 2009  
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nominating committees is intended to provide a clear picture of the process and criteria that were used to identify the candidate. The Director Candidate Information Request also inquires about whether the candidate will be made available to respond to shareholder questions.

As the Commission develops reforms to address the concerns you mentioned regarding the process for election of directors, we hope you will consider using the attached Information Request as a template and incorporate additional disclosure requirements similar to those contained in it.

As an example of how companies outside the United States are moving toward more meaningful disclosure about director candidates, we have attached an annual meeting notice from the Japanese company Eisai Co, Ltd., which contains much of what is covered in the Director Candidate Information Request.

We believe that requiring better disclosure would provide investors with the type of information they need to make fully-informed voting decisions on director candidates.

Please contact any of us if we can be of further assistance.

Very truly yours,



Paul Frentrop  
Head of Corporate Governance  
APG Investments



Anne Sheehan  
Director of Corporate Governance  
California State Teachers' Retirement System

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Elizabeth E. McGeveran  
Senior Vice President  
Governance & Sustainable Investment  
F&C Management Ltd. - Boston, MA



Ian Greenwood  
Chairman  
Local Authority Pension Fund Forum - UK  
(On Behalf of 48 Local Funds)



Thomas P. DiNapoli  
New York State Comptroller  
New York State Common Retirement Fund

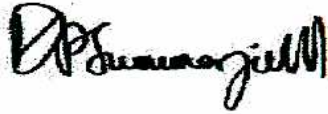


Marcel Jeucken  
PGGM Investments  
Head of Responsible Investment



Frank Curtiss  
Head of Corporate Governance  
Railpen Investments - UK

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A handwritten signature in black ink, appearing to read "DPSummerfield".

Dr. Daniel Summerfield  
Co-Head of Responsible Investment  
Universities Superannuation Scheme – UK

Attachment: Director Candidate Information Request  
Eisai Co, Ltd, Proxy

cc: SEC Commissioners  
Kayla Gillan, Senior Advisor

B

**SAMPLE DIRECTOR CANDIDATE INFORMATION REQUEST**  
[May be adapted on a company by company basis.]

[DATE]

[ADDRESSEE]  
[TITLE]  
[COMPANY]  
[ADDRESS LINE 1]  
[ADDRESS LINE 2]

Re: Director Candidate Information Request

Dear [NAME]:

The undersigned investors collectively manage approximately \$\_\_ billion in global assets and are long-term beneficial shareholders of [COMPANY].

As shareholders, the election of directors is one of our most important responsibilities. Directors play an important role and hold a position of enormous trust. Independent directors, in particular, serve a central function in corporate governance by overseeing management on behalf of the owners.

Recent changes have increased the influence that shareholders have in the election of directors. The trend toward adoption of a majority vote requirement for election of directors has made shareholder voting decisions on directors more meaningful. Director candidates now face the real possibility of not being elected.

In addition, the Chairman of the Securities and Exchange Commission announced in an April 6, 2009 speech to the Council of Institutional Investors that the SEC will likely propose new rules to grant shareholders the right to place director candidates on the company's proxy and may also mandate additional disclosures regarding qualifications of all director candidates. These developments highlight the increasing significance of shareholders' votes on directors and how important it is that shareholders be able to exercise their votes in an informed manner.

In this context, we are writing to request more information regarding the nomination and selection of director candidates. To simplify the process, we have attached an information request for the nominating committee regarding the selection of director



candidates, and one for director candidates themselves, regarding their qualifications as shareholder fiduciaries.

Most of the information requested has not been included in the company's proxy statement. However, shareholders welcome comments from both the company and the director candidates on these issues. We encourage the company to make the candidate available at least three weeks before the shareholder meeting to respond to any shareholder questions. We also encourage the company to make the responses available to all of its shareholders.

Thank you for taking the time to provide this information to your shareholders! Should you have any questions, please contact [CONTACT] at [NUMBER]

Sincerely,

**[SIGNATORIES]**

Enclosure: Director Candidate Information Request

**Nominating Committee Information Request:**  
**Selection of Director Candidates** -

**Introduction and Instructions**

We are requesting information about the process of selecting director candidates. Shareholders can exercise their voting rights in a more informed manner if they understand the dynamics of the board of directors and the process for nominating director candidates. Please respond to the below listed questions. Attention to quality, rather than quantity, of information in responses is appreciated.

**Information Request**

1. **Nominating Process.** Please describe the process the nominating committee adopted in order to develop selection criteria and identify the director candidate.
2. **Independence.** Please describe the role (if any) that the Chief Executive Officer played in determining non-management director candidates.
3. **Criteria for Selection.** Describe the criteria developed for use by the Nominating Committee in selecting the director candidate and briefly explain how those criteria apply to the candidate. For example, what knowledge, skills and experiences would the candidate bring to the company in regard to:
  - Achieving company strategic objectives;
  - Representing shareholder interests;
  - Supplementing competencies and skills of other board members;
  - Providing expertise required on specific committees;
  - Evaluating the company's long-term business plans, capital structure, risk exposures and organizational design; and
  - Recruiting, developing, compensating, evaluating and coaching executive talent.<sup>a</sup>
4. **Shareholder Questions.** If applicable, how and when will the candidate be available to respond to shareholder questions, and how can shareholders participate, submit questions and receive all responses?

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<sup>a</sup> These criteria are listed only as an example and should not be substituted for what was actually used by the Nominating Committee.

## **Director Candidate Information Request**

### **Introduction and Instructions.**

We are requesting information about new director candidates. As shareholders, the election of directors is one of our most important responsibilities. In order for shareholders to cast votes in an informed manner, please respond to the questions listed below. They ask for current, personal views and are not intended to preclude a candidate from exercising future discretion. Attention to quality, rather than quantity, of information in responses is appreciated.

### **Information Request.**

1. **Effectiveness.** Why do you think you would be an effective director at the company?
2. **Independence.** Please tell us about any financial, business, family or personal relationships with members of the company's senior management or board that are not disclosed in the proxy (if any) and, if you are a non-management candidate, explain how they might/might not affect your independence.
3. **Company Issues.** If there are particular issues you would like the company to address or goals you would like to achieve as a director, please comment on them.<sup>b</sup> You may include longer-term concerns, such as environmental risks and other extra-financial issues, as you deem appropriate.
4. **Corporate Governance.**
  - (a) To help shareholders understand your views on key corporate governance and investor responsibility issues, if not previously described, please comment on any changes or improvements in governance practices you would like to see made at the company, if any.
  - (b) Please briefly summarize your general views on key corporate governance issues, regardless of whether they are applicable to the company. Some of the areas you might want to comment on are set out below. Feel free to add explanatory comments on additional issues.
    - The appointment of an Independent Board Chair
    - Requiring that director candidates receive a majority of shareholder votes to be elected
    - Shareholder access to the proxy for nomination of director candidates
    - Communication between shareholders and independent directors on governance matters
    - Company use of, and shareholder approval of, anti-takeover devices
    - Shareholder advisory votes on selection of company auditors

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<sup>b</sup> These questions are not intended to imply that candidates should have a particular agenda or platform. They only seek information about any personal views or priorities a candidate would bring to the board.



- Board consideration of shareholder resolutions which have been approved by a majority shareholder vote
- Company reporting and disclosure of environmental and other major risk exposures
- The disclosure and use of company-related political/campaign contributions
- Advisory shareholder votes on executive compensation
- Independence of the Board's executive compensation consultant

Any Additional Governance-Related Comments:

5. Other Matters. If there are other things you would like shareholders to know when voting their proxies, please address them.