FRC PROGRESS REPORT AND SECOND CONSULTATION ON THE COMBINED CODE

RESPONSE TO CONSULTATION FROM SCOTTISH AND SOUTHERN ENERGY PLC

1.	**The responsibilities of the chairman and the non-executive directors**:	**Walker Review Recommendations**	**SSE POSITION**
	• Whether it would be helpful to give further clarification of the role, key responsibilities and expected behaviours of the chairman, the senior independent director and /or the non-executive directors, either in the Code or in non-binding guidance. • Whether it would be helpful to provide further guidance on the time commitment expected of the chairman, senior independent director and / or non executive directors.	• **Recommendation 3**: The minimum expected time commitment for NEDs should be 30 to 36 days per year. • **Recommendation 6**: NEDs should be ready, able and encouraged to challenge and test proposals on strategy put forward by the executive. • **Recommendation 7**: The chairman should be expected to commit a substantial proportion of his or her time, probably not less than two-thirds, to the business of the entity. • **Recommendation 8**: The chairman should bring a combination of relevant financial industry experience and a track record of successful leadership capability in a significant board position. • **Recommendation 9**: The chairman should encourage and expect the informed and critical contribution of the directors and promote effective communication between executive NEDs. • **Recommendation 11**: The role of the senior independent director (SID) should be to provide a sounding board for the chairman, for the evaluation of the chairman and to serve as a trusted intermediary for the NEDs as and when necessary. The SID should be accessible to shareholders in the event that communication with the chairman becomes difficult or inappropriate.	On the FRC review, we feel it would be difficult to set out any measurable clarification of the roles. Similarly, the expected time commitment would vary from company to company. The Walker proposal for 2/3 of Chairman's time may be appropriate in the financial sector, but is too prescriptive for general listed companies. Walker recommendations 9 and 11 would be appropriate for all listed companies.
2.	**Board balance and composition**	**Walker Review Recommendations**	**SSE POSITION**
	• Whether section A.3 of the Combined Code gives sufficient emphasis to the need for relevant experience among the NEDs	• **Recommendation 4**: The FSA's supervisory process should give closer attention to the overall balance of the board and take into account the relevant experience and	The nine year rule can be restrictive and is arbitrary. Genuine independence depends on

	collectively • Whether the independence criteria and the way they have been applied by boards of companies and investors have unnecessarily restricted the pool of potential non-executive directors and in particular whether the so called 'nine year rule' has resulted in a loss of continuity and valuable experience. • Whether the recommendation that the boards of FTSE 350 companies should comprise at least 50% independent NEDs has resulted in fewer executives directors sitting on boards and/or boards becoming larger. • Whether more guidance is needed in the Code or elsewhere, on succession planning and the need to ensure that board composition is aligned with the present and future needs of the business.	other qualities of individual directors • **Recommendation 5**: The FSA's interview process for NEDs should involve questioning and assessment by one or more senior advisers with relevant industry experience at or close to board level of a large or complex entity.	circumstances, and is a state of mind. It is not determined by a fixed time period. This rule could therefore be relaxed and more flexible. The recommendation for the balance of FTSE 350 Boards is unnecessary. Succession planning is the role of the Nomination Committee, and further guidance is probably unnecessary as it would need to be general in nature.
3.	**Frequency of director re-elections**	**Walker Review Recommendations**	**SSE POSITION**
	The Combined Code recommends that all directors are subject to re-election every three years, with non-executive directors who have served more than nine years being subject to annual re-election. • Whether the chairman, chairs of the main board committees or all directors should be subject to re-election annually. • Whether binding or advisory votes on specific issues, or on the corporate governance statement as a whole should be introduced	• **Recommendation 10**: The chairman of the board should be proposed for election on an annual basis. • **Recommendation 36**: If the non-binding resolution on a remuneration committee report attracts less than 75 percent of the total votes cast, the chairman of the committee should stand for re-election in the following year irrespective of his or her normal appointment term.	The current re-election frequency for listed companies is satisfactory. The proposal for separate votes on the Governance Report is not supported. This is a whole Board issue and forms part of the full Annual Report which is voted on.

4.	**Board information, development and support**	**Walker Review Recommendations**	**SSE POSITION**
	The FRC invites views on various proposals concerning section A.5 of the Combined Code, including a review of the provision of business information to Non Executives.	• **Recommendation 1**: The board should provide thematic business awareness sessions for NEDs on a regular basis. The induction, training and development programme for each NED should be reviewed annually with the chairman • **Recommendation 2**: The board should provide dedicated support for NEDs on any matter on which they require advice separate from that available in the normal board process. • **Recommendation 9**: The chairman should be responsible for ensuring that the directors receive accurate and timely information.	SSE currently provides sessions and programmes of visits which the recommendation 1. addresses. Dedicated support for NEDs is available. Walker recommendation 9 is agreed.
5.	**Board evaluation**	**Walker Review Recommendations**	**SSE POSITION**
	• Whether the Code should be amended to recommend that board evaluations should be externally facilitated at least every two or three years form some or all companies. • Whether the recommendation that the effectiveness of all the main board committees should be evaluated every year should be relaxed in some way, for example to recommend a rolling cycle of committee reviews. • How disclosures in the annual report might be made more informative, either in relation to the process that was followed and / or the outcomes of the effectiveness review.	• **Recommendation 12**: The board should undertake a formal and rigorous evaluation of its performance with external facilitation of the process every second or third year. The statement on this evaluation should be a separate section of the annual report. Where an external facilitator is used, this should be indicated in the statement, together with an indication whether there is any other business relationship with the company. • **Recommendation 13**: The evaluation statement should include such meaningful, high-level information as the board considers necessary to assist shareholders understanding of the main features of the evaluation process. The statement should also provide an indication of the nature and extent of communication by the chairman with major shareholders.	An externally facilitated evaluation every 3 years or so is desirable. Annual external facilitation would be too onerous for most companies. Board Committee evaluation should continue to be on an annual basis, otherwise issues may not be addressed timeously.

6.	Risk management and internal control	Walker Review Recommendations	SSE POSITION
	• Whether the board's responsibility for strategic risks and setting risk appetite – as set out in the Turnbull Guidance – should be made more explicit in the Code, and whether the current balance between the Code and the Guidance is the right one. • Whether there is a need for all or parts of the Turnbull Guidance to be reviewed. • To what extent the particular mechanisms recommended for banks and financial institutions would also be appropriate for other listed companies. For example, there were mixed views among commentators about whether separate risk committees were necessary for companies with less complex business models. • How reporting on risk might be improved, for example by rationalising existing disclosure requirements or providing guidance on good communications tools.	• **Recommendation 23**: The board should establish a risk committee separately from the audit committee with responsibility for oversight and advice to the board on the current risk exposures of the entity and future risk strategy. • **Recommendation 24**: The board should be served by a CRO who should participate in the risk management and oversight process at the highest level on an enterprise-wide basis and have a status of total independence from individual business units. • **Recommendation 25**: The board risk committee should have access to and, in the normal course, expect to draw on external input to its work as a means of taking full account of relevant experience elsewhere and in challenging its analysis and assessment. • **Recommendation 26**: The board risk committee should oversee a due diligence appraisal of proposed acquisitions or disposals. • **Recommendation 27**: The board risk committee (or board) risk report should be included as a separate report within the annual report and accounts. An indication should be given of the membership of the committee, of the frequency of its meetings, whether external advice was taken and, if so, its source.	Our general comment on risk is that this is a fundamental responsibility of the whole Board. The requirement for a Risk Committee is for the Board to determine, and may not be appropriate for smaller, less complex companies.
7.	**Remuneration**	**Walker Review Recommendations**	**SSE POSITION**
	The Combined Code contains recommendations on remuneration levels and the procedures that should be adhered to when setting remuneration for executive directors. • Whether to revise the Code to ensure consistency with the European Commission's Recommendations and,	• **Recommendation 28**: The remit of the remuneration committee should be extended where necessary to cover all aspects of remuneration policy on a firm-wide basis with particular emphasis on risk. • **Recommendations 29 and 30**: The remuneration committee should oversee remuneration of all executives for whom total remuneration exceeds or might exceed	We agree that risk should be a key consideration in remuneration policy. The setting of remuneration should, however, remain the responsibility of the Board rather than shareholders.

	where appropriate, the FSA's proposed code of remuneration practice for financial institutions and the recommendations of the Walker Review. • Whether any other changes to the Code, or additional guidance are required to reflect developments in best practice • Whether shareholders should be given a more direct role in setting remuneration and, if so, how this might be achieved.	the median compensation of executive board members. The remuneration committee report should confirm that the committee is satisfied with the way in which performance objectives are linked to the related compensation structures for this group, and disclose total remuneration, in bands, indicating numbers of executives in each band. • **Recommendation 31**: The remuneration committee report should state whether any executive board member or senior executive has the right or opportunity to receive enhanced pension benefits beyond those already disclosed. • **Recommendation 33**: At least half the variable remuneration offered should be in the form of a long-term incentive scheme with half of the award vesting after not less than three years and of the remainder after five years. Short-term bonus awards should be paid over a three year period with not more than one-third in the first year. Clawback should be used. • **Recommendation 34**: Executive board members and executives whose total remuneration exceeds that of the median of executive board members should be expected to maintain a shareholding or retain a portion of vested awards. Vesting of stock for this group should not normally be accelerated on cessation of employment. • **Recommendation 35**: The remuneration committee should seek advice from the board risk committee on specific risk adjustments to be applied to performance objectives set in the context of incentive packages. • **Recommendation 37**: The remuneration committee report should state whether any executive board member has the right to receive enhanced pension benefits beyond those already disclosed and whether the committee has exercised its discretion during the year to enhance benefits.	
