

Martin A Scicluna
Chairman



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Letter by email to codereview@frc.org.uk.

Dear Catherine

I have read with interest the FRC's proposed revisions to the UK Corporate Governance Code. While I am supportive of most of the proposed changes and the underlying objectives of the reforms, there are several I feel could have a negative impact on listed companies. I have provided my feedback on these below.

Independence criteria: remuneration

The FRC's proposed revisions to the UK Corporate Governance Code include¹ changes to the wording about the independence of individual non-executive directors so that directors who fall within the bulleted items "should not be considered independent". Unlike most of the other bulleted items which refer to "material" or "significant" or are time limited, there is currently no threshold limitation applied to the bullet relating to additional remuneration. In our experience a non-executive director with extensive experience of the applicable sector might well (much earlier in their career) have worked for the listed company (or a company that is now part of the group held by that listed company) that is now considering appointing them as a director.

My Board recently had cause to consider this provision in detail in relation to our current Senior Independent Director who, although a member of one of our group's pension schemes, we have determined to be independent. As part of our deliberations, we considered a number of factors including the relative proportion the relevant pension makes up of the SID's net wealth and retirement planning and we are completely comfortable that her membership of the scheme will not cloud her judgement. It would be extremely disappointing if the operation of the revised independence provisions precluded our SID from being adjudged independent.

In an industry such as insurance (though I think this has a wider application), where there has been much consolidation over the years, there are relatively few large players and people tend to move employment around companies, this could significantly limit the pool of industry experts available to serve as independent non-executive directors. This feels

¹ Appendix A, provision 15

particularly acute when balancing the very significant contribution a person with a career in our industry can bring to a Board. I strongly urge the FRC to review this proposal and to include a materiality qualifier a Board can utilise if comfortable that membership of such a scheme would have no impact on the director's independent judgement. Clearly, since financial affairs are so different as between individuals, the appropriate method for this ought to be a qualitative rather than quantitative assessment.

Independence criteria: cross-directorships

Until recently two of my Board had a cross – directorship, in the sense that they were both non-executive directors of RSA and of a second company. As a Board we considered the matter thoroughly and were completely comfortable that it did not impact negatively the individual directors' judgement or independence. To lose the ability to give a reasonable explanation of why independence provisions are still complied with in such instances would be a great pity and, I believe, detrimental to the composition of many listed Boards.

Independence criteria: requirement for Chairman to remain independent

We also note that the proposed wording refers to a chair not being considered independent if they have served on the board for more than nine years from the date of their first election. One potential impact of this amendment is that it will become less likely for a Board to appoint a Chair who is an existing Director because of the implicit limit on their future tenure as Chair. In my experience there can be significant benefit in appointing a prospective Chair to serve on the Board in advance of becoming Chair as it enables an individual to get to know a business and a Board to evaluate properly the strengths of that individual. As a Chairman this can materially assist prudent succession planning as well as enable an appropriate overlap with successors both at the start and at the end of a Chair's appointment.

The consequence of the proposed "hard stop" of nine years for an independent Chair would be to move to a shorter-term view of board succession planning, with any "overlap" periods at either end of the Chair's tenure further reducing the length of their appointment. Again, I strongly urge the FRC to review this proposed change and potential ramifications on succession planning.

Lastly I note the potential conflict between the need for a Chair to remain independent throughout their tenure and prescribed need to "foster relationships founded on mutual respect and open communication ...between the NEDs and the executive team" and to develop "productive working relationships with all executive directors, and the chief executive in particular, providing support and advice while respecting executive responsibility²". As a Chairman of a FTSE100 company, I endorse wholeheartedly the sentiment behind these responsibilities but am concerned that the particular nature of a Chair's role can be incompatible with the concept of independence, as understood. I urge, for the reasons set out above, the FRC not to require a Chair's independence.

I make these points conscious that there also seems to be some uncertainty as to whether this change of wording is only a change of emphasis, meaning that, with appropriate explanation, directors who fall within the bulleted items can, notwithstanding that, still be considered by a board as being independent and therefore overall the company would still

² Paragraph 50 of the proposed Revised Guidance on Board Effectiveness

be considered to be in compliance with the code. As the one of the key strengths of the UK's Corporate Governance Code is the flexibility provided by the "comply or explain" approach, a flexibility that gives the same weight to well-articulated explanations of tailored approaches as it does to compliance with standard models, I would very much welcome the FRC's confirmation that this is still the approach. Some commentators seem to have interpreted the FRC's consultation document³ differently, so it would be extremely helpful to clarify this.

My Company Secretary or I are at your disposal to discuss anything in this letter further with you or provide any additional information

Yours sincerely

Martin A Scicluna
Chairman

³ Paragraph 52