



THE INSTITUTE
OF CHARTERED
ACCOUNTANTS
IN ENGLAND AND WALES

14 March 2008

Our ref: ICAEW Rep 25/08

Chris Hodge
Financial Reporting Council
5th Floor, Aldwych House
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Dear Chris

**2007 Review of the Combined Code:
Consultation on Proposed Changes to the Code on Corporate Governance**

The Institute of Chartered Accountants in England and Wales (ICAEW) welcomes the opportunity to comment on the Financial Reporting Council's (FRC) consultation paper on proposed changes to the Combined Code on Corporate Governance.

The FRC consultation paper seeks comments on proposed changes to two of the Code's provisions. In summary, we:

- support the removal of the restriction in Code provision A.4.3 on an individual chairing more than one FTSE 100 company; but
- do not support amendments to Code provision C.3.1 to allow the company chairman to be a member of the audit committee of a company listed below the FTSE 350.

In the attached document we provide our comments on these two specific proposals along with our initial views on the two other matters raised in your consultation paper, being a revised Preamble to the Code and the overlap with FSA corporate governance rules.

Please contact Jonathan Hunt or myself should you wish to discuss any of the points raised in this response.

Yours sincerely

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ICAEW Representation

ICAEW REP 25/08

2007 REVIEW OF THE COMBINED CODE: CONSULTATION ON PROPOSED CHANGES TO THE CODE

Memorandum of comment submitted in March 2008 by The Institute of Chartered Accountants in England and Wales, in response to the Financial Reporting Council's consultation paper *2007 Review of the Combined Code: Consultation on Proposed Changes to the Code* published in December 2007.

INTRODUCTION

The Institute of Chartered Accountants in England and Wales (ICAEW) welcomes the opportunity to comment on the Financial Reporting Council's (FRC) consultation paper on proposed changes to the Combined Code on Corporate Governance.

WHO WE ARE

The ICAEW operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the FRC. As a world leading professional accountancy body, the ICAEW provides leadership and practical support to over 130,000 members in more than 140 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The ICAEW is a founding member of the Global Accounting Alliance with over 700,000 members worldwide.

Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The ICAEW ensures these skills are constantly developed, recognised and valued.

DETAILED COMMENTS

Chairing more than one FTSE 100 company

We support the removal of the restriction in Code provision A.4.3 which limits the number of chairmanships of FTSE 100 companies any one individual can have.

We agree with the FRC that such a restriction is unnecessarily prescriptive and may adversely impact on the supply of skilled and experienced candidates to fulfil the role of chairmanship.

Time availability is the key matter here. We believe that, rather than playing a numbers game, it is more important to emphasise:

- the potentially extensive time commitment required; and
- the contingency that may be required for potential periods of crisis.

The restriction in the wording of the current Code provision A.4.3 does not take into account the, perhaps extensive, time commitments that a Chairman may have when he/she is a chairman or director of an organisation that is not a FTSE 100 company, such as a FTSE 250 or small cap or limited company as well as organisations in the public or not-for-profit sectors. Some individuals may have a number of such roles.

The current wording of provision A.4.3, without the final sentence referring to restrictions on chairmanship of more than one FTSE 100 company, adequately addresses the importance of sufficient time allocation. To strengthen the wording, consideration might be given in a future consultation to adding a reference that the Nomination Committee, in addition to preparing a job specification, should consider the time availability issue before making its recommendation to the board.

Company chairman sitting on the audit committee of smaller companies

We do not support amendments to Code provision C.3.1 to allow the Company Chairman to be a member of the audit committee of a company listed below the FTSE 350.

A key requirement of the Code is that an audit committee is composed of independent non-executive directors. Provision C.3.1 states that “*The board should establish an audit committee of at least three, or in the case of smaller companies two, members, who should all be independent non-executive directors.*” We believe that throughout their period of service on an audit committee, each member of the committee should be independent.

Members of audit committees have considerable responsibilities. They may have to take difficult decisions which could bring them into disagreement with the company’s board. This situation is recognised in the Smith guidance for audit committees. Paragraph 3.5, states that “Where there is disagreement between the audit committee and the board, adequate time should be made available for discussion of the issue with a view to resolving the disagreement. Where any such disagreements cannot be resolved, the audit committee should have the right to report the issue to the shareholders as part of the report on its activities in the annual report.” Whilst this is an option of last resort, it is nevertheless important to ensure that it remains an effective option for the members of an audit committee.

In smaller companies, to which the Code applies, there is potentially a greater chance that the Chairman of the company may have a substantial shareholding and/or be a previous chief executive. In these circumstances, upon appointment the Chairman would not have been perceived to be independent under Code provision A.3.1 and the board would have had to explain this at the time of his or her appointment. We have concerns that such a chairman might not be the most appropriate person to be a voting member of the audit committee especially where the company takes up the option of only two independent non-executive directors on the board.

It is accepted practice for the Company Chairman to be invited to attend committee meetings. Thus the committee is able to benefit from the Company Chairman’s counsel without giving him/her a formal vote as part of the audit committee’s decision taking processes.

Under the ‘comply or explain’ principle the board of any listed company to which the Code applies has the option of providing a considered explanation for non-compliance with a Code provision. Boards of smaller companies should not fear non-compliance and engagement with their investors. Institutional investors are increasingly likely to recognise the constraints under which smaller companies may operate.

Thus, if the boards of companies below the FTSE 350 wish to appoint the Chairman of the Company to be a member of the audit committee and they feel that, as a board, they can justify their reasons to investors they should do so in their corporate governance disclosures and then engage with investors as necessary.

Revised preamble

We support the idea of a proposed revision of the preamble. This would provide an opportunity to emphasise the importance of good corporate governance in encouraging entrepreneurialism while at the same time protecting shareholder value. It would also emphasise the role of the Combined Code itself in facilitating dialogue between the business and investment communities through relevant disclosures.

Overlap with FSA Corporate Governance Rules

We support the inclusion of footnotes to Code provisions where there are appropriate overlaps with FSA Listing Rules. This would eliminate ambiguity regarding which of the Code's disclosures are mandatory requirements under FSA Listing Rules and which are not. We also support the updating of Schedule C so that it lists all corporate governance disclosure requirements in one place.

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