



Sir Adrian

I will give you some comments to make on the attached in the speaking notes I am doing for 14/7.

Njd
8/7. Bring card.

Sir Adrian Cadbury
Chairman of the C
Financial Aspects
PO Box 433
Moorgate Place
London EC2P 2BJ

6 July 1992

Dear Sir Adrian,

The Role of the Company Secretary in Corporate Governance

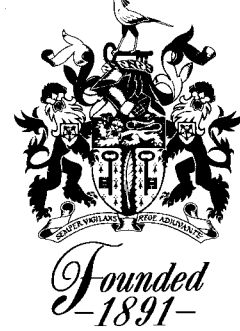
Please find enclosed our submission on the role of the company secretary in corporate governance. We will be making a separate submission on the detailed recommendations contained in the report of your Committee at a later date. We generally welcome the recommendations contained in the report and, although we have one or two minor reservations, believe that they would help to improve standards of corporate governance.

I have also enclosed a copy of the Institute's *Code on Good Boardroom Practice* which was issued in February 1991. We still stand by the principles contained in this Code and were pleased to see that many of those principles have been adopted by your Committee. Although our Code contains guidance on some of the matters which we believe should be included in the board's written procedures, we are currently preparing a more comprehensive guide for directors and company secretaries on these matters.

We welcome the statement in paragraph 4.21 of the Committee's report in so far as it recognises that the company secretary has a key role in corporate governance but would urge that specific reference be made to the company secretary in the Code of Best Practice which the Committee proposes to issue.

The role of the company secretary is of great *practical* importance within corporate governance and therefore falls naturally within the ambit of your Committee. The detailed proposals which we have made are not in themselves innovative. Rather, they represent a statement of existing best practice as carried out in many companies and also reflect the contents of the *Duties of the Company Secretary* document recently published by this Institute.

It is our contention that certain areas relating to the role of the company secretary need better definition and codification in order to encourage consistent application by company boards. This would ultimately be to the benefit of good corporate governance but, more specifically, to the benefit of directors themselves in the creation of credible systems of governance.



Sir Adrian Cadbury,
Chairman of the Committee on the
Financial Aspects of Corporate Governance
PO Box 433
Moorgate Place
London EC2P 2BJ

6 July 1992

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The Role of the Company Secretary in Corporate Governance

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It is our contention that certain areas relating to the role of the company secretary need better definition and codification in order to encourage consistent application by company boards. This would ultimately be to the benefit of good corporate governance but, more specifically, to the benefit of directors themselves in the creation of credible systems of governance.

We do not seek to change in any way the relationship between the directors and the company secretary. The secretary is legally an officer of the company and, as such, has a number of statutory and fiduciary duties. The secretary's status is not, however, directly comparable with that of the directors who are answerable to the shareholders for the management of the company. The secretary's primary responsibility is to the board of directors. However, the company secretary, as recognised by the Companies Act, is charged with the practical administration of board procedures and shares responsibility with the directors for ensuring that the company complies with many of its legal obligations.

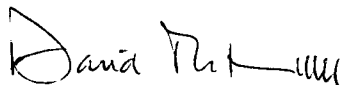
The company secretary is often charged by the directors with other executive responsibilities within the company and our proposals seek to establish a distinction between the two roles of the secretary, thus reinforcing the implicit position found in company legislation.

The roles are:

- a. As an officer of the company charged with the administration of board and the company's governance procedures. Here the secretary is responsible to the board, normally through the chairman. In this capacity, the services of the secretary are available to the whole board including the non-executive directors, for whom the secretary can act as a point of contact and advice within the company itself. In this role, it is important to maintain the integrity and, to the maximum practical degree, the independence of the company secretary. Our proposals are geared towards this aspect of the company secretary's role.
- b. As a company manager with executive responsibilities within the company. There is no reason why the secretary should not report or be made responsible to individual directors in this regard.

We believe that the inclusion of guidance on these matters in the Code of Best Practice to be issued by the Committee would help further what is already good practice in terms of the relationship between the board and the secretary. Again we would emphasise that the role of the secretary is not directly analogous to that of the directors in matters of corporate governance. The company secretary occupies a privileged position and is uniquely well-placed to act as a catalyst for good corporate governance.

Yours sincerely,



D S Mitchell
Chairman
Company Secretaries Group

Submission to the Cadbury Committee on the role of the company secretary in corporate governance

Introduction

We have made a number of detailed recommendations in this paper which we believe should be included in the Code of Best Practice which the Cadbury Committee proposes to issue. These proposals are based on a number of basic principles and philosophies:

- a. as an officer of the company, the company secretary already has a formal legal role in corporate governance (see Appendix);
- b. in any matter relating to the governance of the company, board procedures or his duties as an officer of the company, the secretary is responsible to the board collectively (normally through the chairman);
- c. all the members of the board, including the non-executive directors, should be able to rely on the impartial and independent advice and services of the company secretary;
- d. in matters of corporate governance, the company secretary is the natural ally of the non-executive directors and it is in their own interests to seek to protect the integrity and independence of the company secretary; and
- e. as a matter of best practice, the company secretary should be independent and free from the pressures that can lead to 'misjudgments and possible illegal practices'.

Detailed recommendations

1. *The company secretary should be responsible to the board of directors (through the chairman) for the proper administration of the procedures and arrangements established by the board for the conduct of its own business and the company's compliance with internal and external regulations and codes relating to corporate governance. In carrying out this responsibility the company secretary should administer, attend and prepare (or arrange for the preparation of) minutes of the proceedings of the board.*

We agree wholeheartedly with paragraphs 4.19 and 4.20 of the report. It is clearly sensible for boards to have a formal schedule of matters reserved for collective decision. We strongly believe that, as a matter of best practice, the board of directors should establish written procedures for the conduct of its business. The formal schedule of matters reserved for collective decision should merely form part of these written procedures. By establishing these procedures, the board is merely stating how it wishes to conduct its business. If the procedures prove to be unworkable, the board should identify the problems and amend them accordingly. Boards should, however, make these decisions collectively. All the directors, whether executive or non-executive, should seek to ensure that the procedures that are established enable them to fulfil their duties as directors.

If written board procedures are not established, there is a danger that the formal schedule which the Cadbury Committee has proposed listed companies should adopt will become ineffectual. In practice, important commercial decisions will occasionally be required to be made between board meetings, although this is, of course, less likely if frequent and regular meetings are held. If procedures are not established to allow decisions to be made quickly in exceptional circumstances, the existence of a formal schedule of matters may be seen as a barrier to effective decision-making. Article 4 of ICSA's *Code of Good Boardroom Practice* states:

"The board should identify matters which require the prior approval of the board and lay down procedures to be followed when, exceptionally, a decision is required before its next meeting on any matter not required by law to be considered at board level.

If it is practicable, the approval of all the directors should be obtained by means of a written resolution. In all cases, however, the procedures should balance the need for urgency with the overriding principle that each director should be given as much information as possible and have the opportunity to requisition an emergency meeting of the board to discuss the matter prior to the commitment of the company."

Without proper procedures, boards will frequently find themselves being asked to ratify decisions taken by individuals prior to the board meeting.

It may seem unnecessary to state that the company secretary should administer, attend and minute meetings of the board when, arguably that is what companies employ the secretary to do. Indeed, paragraph 4.21 of the report of the Cadbury Committee appears to take it for granted that this is what all company secretaries do. Most directors would probably be surprised to discover that, under UK law, the company secretary can be excluded from meetings of the board, and that the law does not require the secretary to attend, administer or take minutes of board meetings. We have no doubt that most directors would agree that as a matter of good practice, the company secretary should perform each of these functions and we believe that alarm bells should ring in the minds of the directors if the company secretary does not do so. We believe therefore that companies that do not follow this established practice should be required to justify why they do not do so.

The company secretary should be responsible to the board of directors through the chairman for the administration of the board. All the directors have a right to the strong and positive support of both the chairman and the secretary in ensuring that the board is run fairly in accordance with the law, the company's articles of association and the procedures laid down by the board itself. The reason why the secretary will work closely with and is responsible to the board through the chairman is because the chairman is the person that the board has nominated to manage and control its proceedings. If the chairman seeks to operate outside these criteria, the secretary has a duty to advise him of the correct procedures which should be followed. However, the power to control the actions of any director, including the chairman, lies in the hands of the board and not the secretary. The secretary is a *catalyst* for good corporate governance but it is for the board to decide what remedial action should be taken. The secretary should remain impartial and should advise all of the directors as to their duties and responsibilities under internal and external regulations.

2. *The company secretary should be appointed as the secretary to the audit committee, the remuneration committee and the nomination committee.*

It is particularly appropriate for the company secretary to be appointed as secretary to the audit, remuneration and nomination committees. The non-executive directors, who will normally form a majority on these committees, have as much right to the services of the company secretary as the board collectively and the appointment of the secretary to these committees of non-executives is a most effective method of enabling the secretary and the non-executives to build a working relationship.

Although it should be stated explicitly in the terms of reference of each committee of the board, committees have an implicit right of access to company information that is relevant to the performance of their delegated duties. The secretary can act as the first point of contact and as a channel of communication for the non-executive directors when they are fulfilling their independent monitoring or advisory role. In terms of corporate governance the non-executive directors and the company secretary can be natural allies and it is in the interests of the non-executive directors to seek to protect the independence and integrity of the company secretary.

3. *The company secretary should be appointed as the secretary of any committee of the board which has power to make decisions on behalf of the company.*

Board committees are an essential part of the decision-making process in public companies and enable the full board to concentrate on the strategic management of the company. However, the normal checks and balances of the board's collective decision-making process do not exist to the same extent in committees. Consequently, (to use a phrase from the Committee's report) the potential for 'misjudgments and possible illegal practices' are that much greater. It is particularly important therefore to establish a degree of monitoring and control of these committees. The most obvious methods of doing so are to establish clear terms of reference which should state the limits of the committee's delegated authority, to require each committee to report to the board on its actions and for the secretary to administer these committees.

The role of the company secretary in relation to committees should be similar to that which the secretary has with the board itself. The secretary should, for example be responsible to the committee (through the committee chairman) for the proper administration of the committee. Procedural formalities should not be dispensed with simply because power to bind the company has been delegated to a committee of the board, although they may be modified. It is important to ensure that committees follow agreed procedures and do not exceed their delegated authority.

4. *The removal of the secretary from office should be included as one of the matters reserved for the collective decision of the board.*

Section 286 of the Companies Act 1985 places a duty on the directors of public companies to appoint a person as secretary who is capable of performing the functions of secretary. The board is therefore responsible for the appointment of the secretary and the whole board should satisfy itself that the person appointed is capable and remains so. The board can be assumed to have a continuing responsibility to ensure that the secretary is capable, and if it proposed that secretary should be removed from office, it

is appropriate that the board should make the final decision. In practice, the articles of association of most public companies follow Regulation 99 of Table A (which can be considered to embody the government's recommended practice in these matters) by providing that the secretary can be removed 'by the directors'. Table A implies, by using the word 'directors' in the plural, that the removal of the secretary should be reserved for the collective decision of the board. We believe that the full board has a right to participate in the decision and that it is singularly inappropriate for the power to remove the secretary to be delegated to a single director or a small group of directors or to be the subject of subsequent ratification by the board.

Accordingly, the procedures for the removal of the secretary should ensure that **all** the directors participate in the decision by requiring the decision to be made at a scheduled board meeting for which proper notice has been given of the intention to propose that the secretary be removed from office.

The company secretary should be entitled to receive notice of and make representations at any meeting of directors at which a proposal that he be removed from office is to be considered. In terms of corporate governance, the directors should consider it their duty to establish why it is proposed that the secretary should be removed. The non-executives in particular should be concerned to ensure that it is not because the secretary refused to be a party to a 'misjudgment or possible illegal practice'. All the directors should seek to ensure that the secretary is able to contribute to the good governance of the company and the non-executive directors in particular should seek to ensure that the secretary's independence and integrity is not compromised. Directors cannot reasonably expect the secretary to be able to operate with independence and integrity if they leave him in an exposed position. Well-managed companies encourage the company secretary to act as a catalyst for corporate governance. Only those companies who do not comply with the law and best practice have anything to fear from this proposal.

5. Before combining the office of secretary with that of a director, careful consideration should be given to the effect that this may have on the company's internal governance procedures. If a director is appointed as the secretary (or vice versa), the company's procedures may need to be modified to ensure that conflicts of interest are avoided.

Conflicts of interest may sometimes arise when a person holds dual office as a director and company secretary of a public company. There can be no doubt that it is inappropriate for the chief executive of a public company to act as the secretary. Neither can there be any doubt that it would be inappropriate for the finance director who also holds office as the company secretary to act as the secretary to the audit committee. In our view, this is evidence that it is inappropriate for the finance director of a public company to act as the secretary rather than evidence that it is inappropriate for the company secretary to act as the secretary to the audit committee.

Whilst we have reservations regarding the desirability of combining the office of director and the office of secretary in public companies, we recognise that the law allows one person to perform this dual role and, indeed, that it is common practice in many smaller public companies. However, we believe that the independence of the company secretary is a legitimate matter of concern to those who wish to assess the company's systems of governance and we would advise that where companies combine the two offices, internal governance procedures should be reviewed and adapted to ensure that conflicts of interest are avoided.

Appendix

The company secretary as an officer of the company

The Companies Act 1985 states that the *directors and the company secretary* are officers of the company. The nature of the office of company secretary is, however, different from that of the directors. The directors and the company secretary share responsibility under the law for compliance with many of the provisions of the Companies Acts and other associated legislation. However, the directors have a number of additional legal duties and are answerable to the shareholders for the management of the company. The company secretary, on the other hand is answerable primarily (but not wholly) to the directors; not wholly, because the secretary can be held legally accountable for the company's failure to comply with its legal obligations and because, as an officer of the company, the secretary has a fiduciary relationship with the shareholders. However, this fiduciary relationship is overshadowed by the fiduciary relationship that exists between the directors and the shareholders.

Where the secretary shares legal duties and responsibilities with the directors he will, in practice, ensure compliance by a combination of his own personal actions and by advising the board of directors collectively and individually of their own duties and responsibilities. Advising the directors as to their duties and responsibilities does not by itself guarantee compliance. Consequently, the secretary can be assumed to have fulfilled his legal obligations if he has done everything in his power to ensure compliance. If the directors decide not to follow the company secretary's advice, it is they who will be accountable in law for their actions or failure to act. However, if the company secretary fails to carry out his personal responsibilities or to advise the directors of their duties and responsibilities, he cannot claim to have done everything in his power to ensure compliance and can be held accountable in law.

The company secretary is therefore established in law as an officer of the company who shares responsibility with the directors for ensuring that the company complies with its legal duties and responsibilities. He has a duty to advise the directors as to their duties and responsibilities and, thus, already has a formal and legally defined role in corporate governance.



Mr J Charkham
Adviser to the Governors
Bank of England
London
EC2R 8AH

Copy for info.

6th July 1992

Dear Mr Charkham,

Directors' access to information and the role of the company secretary

Thankyou for your letter dated 24 June 1992 regarding our guide to the duties of the company secretary. In your letter you asked: can the company secretary give the non-executive directors any information they want without reference to the chairman or CEO or the board?

The short answer to the question is that the secretary is ultimately answerable to the board acting collectively and not to any individual members of it. The board may however delegate certain areas of authority (which may cover matters such as release of information) to committees or to individual directors such as the chairman or managing director.

For instance, the specimen terms of reference for audit committees in the report of the Cadbury Committee on Corporate Governance states:

The Committee is authorised by the Board to investigate any activity within its terms of reference. It is authorised to seek any information it requires from any employee and all employees are directed to co-operate with any request made by the Committee.

Many of the requests from non-executive directors may be quite routine such as questions concerning board procedures and other internal procedures. Requests may also be made for general information on how a particular area of the company's business (which may be outside the director's own experience) operates. Perhaps the secretary may arrange for the director to visit the operation concerned.

Where substantive information on the company's affairs is supplied to a non-executive director, I would expect the secretary to keep the chairman informed of this in general terms as a routine part of their close working relationship. A chairman has a legitimate interest in such matters to assist him in monitoring and promoting the induction and development of non-executive

directors and to help him avoid being embarrassed by unexpected areas of questioning at board meetings. It would not however be usual for the secretary to have to obtain advance permission from the chairman or chief executive before providing such information or assistance.

If the information requested were of a more sensitive nature, the secretary would be expected to clear the request with the chairman or chief executive, or if the work of a committee were involved, the chairman of that committee. If the request were to be denied, one would expect the officer concerned to discuss the matter direct with the non-executive director to explain the difficulty. If the non-executive director was not satisfied with this explanation, the secretary could do little more than advise the director of his right to raise the matter at a board meeting or perhaps even to require a board meeting to be convened.

The ICSA Code on Good Boardroom Practice states:

2. The board should ensure that each director is given on appointment sufficient information to enable him to perform his duties. In particular, guidance for non-executive directors should cover the procedures:

- i) for obtaining information concerning the company; and*
- ii) for requisitioning a meeting of the board.*

3. In the conduct of board business, two fundamental concepts should be observed:

- i) each director should receive the same information at the same time; and*
- ii) each director should be given sufficient time in which to consider any such information."*

This clearly has a bearing on the question of provision of general information to directors and the equality of treatment of directors. There will however be circumstances in which, say, a committee might legitimately wish to keep certain information confidential to itself or to delay its release to other directors. It also underlines the desirability of laying down clear procedures.

Directors have some specific rights to information under company law. A director is entitled to inspect the accounting records (s. 222 of the 1985 Act) and to inspect the board minute book. Requests for such information would no doubt be complied with by the secretary as a matter of course.

In conclusion, the secretary has few powers in his own right to provide information to individual directors but will provide information in accordance with company law requirements and agreed company procedures, under the overall authority of the board or subject to other authority delegated by the board.

Discussions of the legal position apart, the independent role of the secretary plays an important part in board and committee structures. The secretary will commonly be called on to preserve confidentiality between the deliberations of the different committees which he administers and perhaps between those committees and the board (where this is required by procedures approved by the board). Clearly this is a role requiring sensitive handling in which the personal qualities of the secretary will have more importance than will strictly legal issues. Much will depend on the secretary establishing a relationship of trust and confidence with the chairman and the other members of the board.

Although our response is not quite as succinct as your question, i hope that it goes some way towards providing an explanation of our understanding of the situation. If I can be of any further assistance, do not hesitate to contact me.

Yours sincerely,

Andy Hamer
Secretary
Company Secretaries Group

BANK OF ENGLAND
LONDON EC2R 8AH

J P Charkham
Adviser to the Governors
071-601 4497

24 June 1992

Andy Hamer Esq
The Institute of Chartered
Secretaries and Administrators
16 Park Crescent
London W1N 4AH

Dear Mr Hamer

Thank you very much for your letter of 15 June and for the interesting and useful booklet it covered. I wonder if you could give me one piece of guidance about it. The last item on page 10 says "Non-Executive Directors: Acting as a channel of communication and information for non-executive directors". I just wondered whether you could enlarge on this. I can understand non-executive directors being at one end of the channel of communication: who is at the other end? Can the company secretary give the non-executive directors any information they want without reference to the chairman or CEO or board?

These are real issues and I would very much value your guidance.

Yours sincerely

J P Charkham