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COMPANY DIRECTOR MAGAZINE

1) Australia took the lead in the matter of corporate governance with the publication of **Corporate Practices and Conduct**. It is an excellent document and it covers the governance field clearly and briefly. We drew on it in our Committee, but we had a narrower remit. We were asked to concentrate on financial reporting and accountability, rather than on corporate governance itself.

We have set out a Code of Best Practice to apply to all listed companies registered in the UK and two of the principles on which the Code is based are the need for adequate disclosure and for appropriate checks and balances within the governance structure of companies. I believe those principles are universally valid and I consider disclosure to be the key to governance. It ensures that all those with a legitimate interest in a company have the information which they need in order to exercise their rights and responsibilities towards it .

2) What I look for on a board is balance. Balance between executive and outside directors and balance in terms of personality and experience. An essential aspect of balance is that there should be a strong enough independent element in the board team. A good test is whether there is someone on the board who can tell chairmen when it is time they stepped down!

Another point about balance is that as the needs of a company change, so the make-up of its board should change in line with new challenges. Balance is not, therefore, a static concept but a dynamic one.

3) We welcomed in our Report the statement published by the Institutional Shareholders Committee. One of their conclusions was that, "Institutional investors should encourage regular, systematic contact at senior executive

level to exchange views and information on strategy, performance, board membership and quality of management."

This envisages a structured rather than an informal relationship and that is necessary to avoid giving an unfair advantage to institutional over individual shareholders. The one word in the ISC statement which could cause concern is "performance". In my view the dialogue should be about structure and strategy and not about current activities.

4) My answer here follows on from that to the previous question. Institutions make no claim to management expertise, but they have both a right and a responsibility to satisfy themselves as to the framework within which the company is operating. What I believe our Code of Best Practice provides is a check list for boards and an agenda for shareholders of all classes in their dialogues with boards.

5) The takeover approach to governance in the US - that a free market in the control of assets would solve the problems of governance - had two unfortunate consequences. It cast shareholders and managers as adversaries - perform or we will sell out to someone who claims they can - and it resulted in managers protecting their positions with an imaginative range of undesirable devices.

When, in addition, takeovers failed in general to deliver the promised results, the American debate took a more constructive turn. The accent now is on "relationship investing", which involves building long-term links between shareholders and directors. I am sure, however, that the more active stance of shareholders in the US will work its way to the UK, as a result of the increasingly international nature of the market for equities and for raising capital.

6) We say in our Report that boards, "...must be free to drive their companies forward, but exercise that freedom within a framework of effective accountability." Once again it is a question of balance and also of disclosure. Provided

shareholders know what risks they are running, it is up to them to decide whether to invest or not. What the law and Codes such as **Corporate Practices and Conduct** are there to prevent is investors being exposed to risks about which they are uninformed. In general I believe that control and efficiency go together and our Code aims to ensure that publicly listed companies are efficiently run.

7) There are a number of advantages to non-statutory regulation. It can adapt more quickly to deal with new issues. It has more moral force than a law, which can be seen as an obstacle to be got round and as legitimising anything which is not clearly illegal. The law also looks to the past and sets a floor to conduct, whereas Codes can set high standards and require their aims to be observed in substance, not just in form.

We are looking to shareholders to help in bringing about compliance with our Code, hence the importance of the London Stock Exchange requiring companies to state how far they comply with the Code as a condition of listing. The listing obligation requires companies to make a statement about compliance, not to comply. Compliance is a matter for boards and their shareholders.

Failure to make sufficient progress along the lines of our Committee's recommendations will. in my view, lead to pressure for statutory measures.

8) I have been impressed and encouraged by the interest which boards have shown in the work of our Committee. I believe the majority of listed companies will use the Code as a guide against which to measure where they stand. Boards were looking for a lead as to what was expected of them and to that extent our recommendations were going with the tide of business opinion.

Where old ways die hard is in the manner in which board members are selected. Word of mouth and the old boy network still predominate. The appointment of a director should be carried out as purposefully and as professionally as that of any other senior manager. Until that is generally accepted, I will not be satisfied that effective corporate governance is in place!

9) I am coming to the May Conference to take part and to listen and learn. I look on our Report as an important step

in the right direction, but not as the end of the matter. What I will hope for from the Conference will be thoughts about what direction the next steps in corporate governance should take. I will be looking for a lead as to the governance issues we should now be putting on the agenda.

Adrian Cadbury

12/4/93.