

COMMITTEE
ON
THE FINANCIAL ASPECTS
OF CORPORATE GOVERNANCE

CAD-02503

December 1992

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Moorgate Place
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Mr R Gavin Burnett
7 Ralston Road
Bearsden
Glasgow G61 3SS

Thank you for your letter of 8th December.

I reply without having consulted the Committee, but I am sure it is not the Committee's intention that audit committees should involve themselves (unless they want to) in the nuts and bolts of internal audit investigations. In saying that the internal audit programme should be reviewed by the audit committee, our expectation is simply that the audit committee should generally understand and endorse the objectives of the internal auditors, their annual audit plan, and their areas of emphasis.

You may be interested to see the enclosed document entitled 'Audit committees for the 1990s' which Arthur Andersen published following the issue of our draft report. The Committee has not specifically endorsed it but you may find it a helpful discussion of how audit committees can operate in practice. Our specimen terms of reference for audit committees are intended only as a guide and we note that companies will wish to adapt and build on them to suit their own circumstances.

Sir Adrian

Nigel Peace
Secretary

I have sent the reply to Mr Lewis but have held back the reply to Mr Gavin Burnett in case you want to suggest any changes.

Nigel
11/12

R. Gavin Burnett, B.Com., C.A., F.C.M.A.

7 Ralston Road,
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December 8, 1992

Telephone
041-942 5513

The Secretary,
Committee on the Financial Aspects of Corporate Governance,
P. O. Box 433,
Moorgate Place,
London EC2P 2BJ.

Dear Sir,

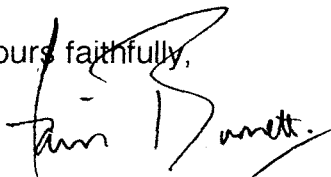
I wrote in response to the draft report and welcome the publication on December 1 of the final report. This report indicates that any queries on the report should be addressed to you. When I responded in July I did so in my capacity as chairman of an audit committee concerned as to our remit and wishing to keep it in line with best practice. The point I make below and its inclusion (or omission) from our revised terms of reference is giving me concern and I should welcome any further guidance you may be able to give.

I reproduce below my earlier comment. Unless I have missed it, the final report (pages 29f and 73g) does not clarify the extent to which "The internal audit programme should be reviewed by the audit committee." If that means what it says, it will require a level of time commitment and both a detailed knowledge of the company and of auditing techniques that rarely are available to non-executive directors.

I feel sure that your committee could not have envisaged audit committees becoming involved to that depth in the workings of internal audit. However, to exclude that part of your suggested remit as being unrealistic, from what I am sure your committee would like to be regarded as "best practice", could cause problems in the future for audit committees who so restrict their remit.

If you are able to give guidance on this point I should be most grateful.

Yours faithfully,



Note referred to:

One of the duties of the audit committee you identify is "to review the internal audit programme." Membership of the audit committee, you suggest, is confined to non-executive directors (with which I agree) who, you state, "lack the inside knowledge of the company." This appears contradictory. How can they review the internal audit programme while lacking inside knowledge of the company? Some clarification would be welcome on this point particularly as few if any members of audit committees will have any detailed knowledge of auditing or internal audit techniques.

R. Gavin Burnett, B.Com., C.A., F.C.M.A.

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July 28, 1992

Telephone
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Nigel Peace, Esq.,
Secretary,
Committee on the Financial Aspects of Corporate Governance,
P. O. Box 433,
Moorgate Place,
London EC2P 2BJ.

Dear Mr. Peace,

I write in response to your Committee's Draft Report on which you seek comment. I was for 5 years till 1991 a member of APC and was, till I retired on the merger with Ernst & Whinney, a senior partner in the Glasgow office of Arthur Young. I am a member of council of ICAS and am an honorary professor at Stirling University. I write, however, in a personal capacity and as chairman of an audit committee.

The report is to be welcomed as are all steps to improve corporate governance. The two specific comments I wish to make are:

Audit Committees

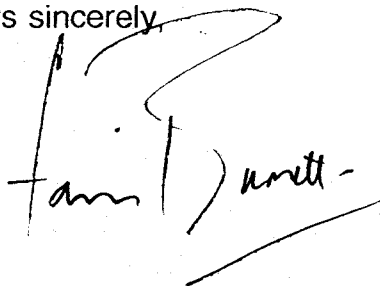
One of the duties of the audit committee you identify is "to review the internal audit programme." Membership of the audit committee, you suggest, is confined to non-executive directors (with which I agree) who, you state, "lack the inside knowledge of the company." This appears contradictory. How can they review the internal audit programme while lacking inside knowledge of the company? Some clarification would be welcome on this point particularly as few if any members of audit committees will have any detailed knowledge of auditing or internal audit techniques.

Nomination Committees

I am unconvinced as to the merits of the form of Nomination Committee you suggest for the making of Board appointments and whether this will achieve any purpose other than the creation of a facade of democracy. A common complaint, and certainly one north of the border, is that the same few non-executive directors are on many boards and once on the circuit, seem to select from that circuit and introduce only kindred spirits to the circuit and that, sparingly. I cannot see how anything will change with a nomination committee comprised of non-executive directors possibly already part of the cabal.

I wish you and your committee well in its final deliberations and commend, again, your objectives.

Yours sincerely,



R. Gavin Burnett

cc Sir Adrian

COMMITTEE
ON
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OF CORPORATE GOVERNANCE

11th December 1992

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Mr David Lewis
Molyneux Estates plc
Catherine House
76 Gloucester Place
London W1H 4DQ

Dear Mr Lewis,

Sir Adrian Cadbury has asked me to thank you for your letter of 2nd December and to reply to the points raised.

The Committee's report recognises at paragraph 3.15 that smaller companies may initially have difficulty in complying with some aspects of the Code, and it notes that boards who cannot, for the time being, comply with parts of the Code may instead give their reasons for non-compliance. The compulsory feature of the system will not be compliance with the Code, but a statement by companies in their annual report which explains whether they are complying and gives reasons for any areas of non-compliance. The Stock Exchange intend this rule to apply to USM companies as well as to companies with a full listing.

Although, as I have said, the Committee recognises the difficulties, it nevertheless believes that full compliance with the Code will bring benefits to the boards of smaller companies and that boards should seek to make sure that the benefits are achieved. In particular, the Committee believes that the appointment of non-executive directors will make a positive contribution to the development of their businesses.

I hope this clarifies the position.

Yours sincerely,

Nigel Peace

Nigel Peace
Secretary

MOLYNEUX ESTATES PLC

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2 December 1992

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

Dear Sir Adrian,

Thank you for your letter of 1st December with enclosure which I will consider with very great care. I would, however, comment that some of the recommendations may be considered onerous for small companies in relation to the size of the Board and the number of non-executive Directors, and the establishment of an Audit Committee and related matters.

I assume that whilst the USM continues a number of your recommendations would not necessarily apply.

I am, however, grateful to you for letting me have a copy of your report which has been passed to our Company Secretary.

Yours sincerely,



DAVID LEWIS

cc K. Gardner Esq

jh/me