

COMMITTEE
ON
THE FINANCIAL ASPECTS
OF CORPORATE GOVERNANCE

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3 March 1994

To all Committee Members

Dear Sir Adrian

Committee Meeting - 23 February 1994

Please find attached a copy of the minutes of the above meeting. I should be grateful if you would make a note that, in response to a request from those present at the meeting, the time of the next meeting has been put back from 3.00 pm to 4.00 pm on 19 May.

Also enclosed with this letter are various other items which, for ease of reference, I list below:-

- (1) Minutes of the Overload Meeting of 13 December 1993. [Paragraph 4 of the Committee's minutes refers.] Sir Adrian has asked me to particularly bring to your attention the top sentence on page 3, "The Committee's recommendations were designed".
- (2) Copy of a letter from Sir Dermot de Trafford dated 23 February relating to the APB exposure drafts on "Fraud and Error" and "Law and Regulations". [Paragraph 6 of the minutes refers.]
- (3) IOD Press Release. [Paragraph 17 refers.]
- (4) Article on Corporate Governance appearing in the March edition of Company Reporting. The editor has always in the past taken a rather negative view of the Committee's recommendations, preferring to highlight where they have not been complied with, rather than pointing out the high levels of compliance in larger companies. The current survey follows this mould.

I am concerned that he refers throughout to "mandatory compliance" with the Code, when he means the requirement to make a compliance statement. I will take this up with him. I will also try and establish how he selected his sample of non-FT-SE 100 companies.

- (5) Touche Ross's Progress Report No 4 on the Financial Aspects of Corporate Governance. In contrast to Company Reporting, Touche Ross's reports have to date been very positive. There are interesting comments on compliance with the Code by small and medium-sized companies in the section on page 9. I will obtain a copy of the East Midlands survey, perhaps if you would like a copy you would let me know.
- (6) At the 23 February meeting it was agreed that the Committee should not comment formally on the draft guidance on internal control. I have, however, received copies of submissions made to the Working Group by the ABI and Coopers and Lybrand, which I am copying to you for information.

With best wishes

Gina

Gina Cole
Secretary

**COMMITTEE ON THE FINANCIAL ASPECTS
OF CORPORATE GOVERNANCE**

MINUTES OF THE MEETING HELD ON WEDNESDAY 23 FEBRUARY 1994
AT THE BANK OF ENGLAND

Present: Sir Adrian Cadbury
Jonathan Charkham
Hugh Collum
Sir Andrew Hugh Smith
Sir Sydney Lipworth
Nigel Macdonald
Arthur Russell
Martin Taylor
Sir Dermot de Trafford
Gina Cole

Agenda Item 1

1. Apologies for absence were received from Mike Sandland, Andrew Likierman, Jim Butler and Mark Sheldon.
2. The Chairman warmly welcomed Sir Sydney Lipworth on joining the Committee. Sir Ron Dearing had agreed to continue to serve the Committee as an adviser, but Sir Sydney would provide the direct link with the Financial Reporting Council.
3. Sir Sydney advised that his only reservation in accepting the invitation to join the Committee had been a potential conflict of interest between the roles of the ASB and the Committee, particularly in the area of "overload". Nigel Macdonald was of the view that the potential for conflict was more likely to arise vis a vis the APB, rather than the ASB, but the Committee should remain alert to it. The Committee's successor body would also need to consider carefully how any actions they proposed fitted into the whole jigsaw.

Agenda Item 2

4. The minutes of the previous meeting on 24 November 1993 were agreed. The Chairman reiterated the points he had made in his letter of 9 December to Bill Morrison at the APB, which was subsequently discussed at the Overload meeting on 13 December. The Secretary added that before he retired from the FRC, Sir Ron Dearing had given permission for the minutes of that meeting to be circulated to Committee members, and this would be done shortly.

5. Hugh Collum advised that the 100 Group had submitted its views on the draft Internal Control Guidance, and they were in accordance with the views expressed in the 9 December letter. In answer to a query raised by Sir Dermot de Trafford, he confirmed that no-one within the 100 Group spoke on behalf of smaller companies.

Agenda Item 3 - APB Exposure Drafts

6. Sir Dermot de Trafford tabled a letter to the Secretary (copies attached) which the Institute of Directors' view on the Exposure Drafts on "Fraud and Error" and "Law and Regulations" were expressed. He confirmed to the Chairman that the IOD would be making these points direct to the APB, but was concerned that the Committee, if making comment on its own behalf, should not greet the Drafts too enthusiastically, as some points in them were erroneous. The Chairman said that the Committee would let the debate take its course and would not make any formal comment.

Agenda Items 4 & 5- Draft Guidance on Going Concern and Internal Control

7. The Chairman requested views on whether the Committee should comment on the draft guidance, or to let the debate develop. Hugh Collum said that on the going concern issue, the argument remained on the definition of "foreseeable future". The APB suggested it should be on the anniversary of the approval of the accounts, as opposed to 12 months from the end of the financial year. The 100 Group were for the shorter period. Sir Andrew Hugh Smith added that companies should not be involved in substantial extra effort in complying with the going concern requirement, and therefore if the Committee were to make a statement it should endorse the shorter period. The view was strongly supported by Nigel Macdonald. However, he questioned the wisdom of making a public contribution to the debate at this stage. He felt it would be a pity if the debate became too focussed on the actual date, preventing directors from taking a longer term view.

8. Sir Dermot de Trafford advised that the Institute of Directors were unhappy that the APB were defining the duties of directors. They considered it was up to directors to make a judgement on the question of going concern, and for the auditors to make sure that the directors had taken all the necessary steps when coming to their decision.

9. Summing up, the Chairman confirmed that the Committee should resist pressure to be drawn into the public debate. The Committee's role was to make the recommendation and for others to make decisions on implementation. He agreed with Sir Sydney Lipworth's observation that if a formal comment were made, and the relevant body disagreed with the Committee's view, the Committee would be put in a very false position. In answer to Martin Taylor's query, he advised that the Committee might be asked to endorse the guidance once it had been finally agreed, but that it should only do so if it were in line with the Committee's recommendations.

10. On internal control, Nigel Macdonald advised that it was likely that the proposed guidance would be shortened to bring it more in line with the Canadian "principles-based" approach. He referred to two recent conferences at which the Chairman of the Internal Control Working Group, Paul Rutteman, had spoken and

his defence of the document had been well-received. This contrasted with current press reporting on the issue. The fact that management were beginning to think positively about internal control was welcomed by Jonathan Charkham, and he thought that whatever form the final guidance did take, companies should be urged to face the questions posed by internal control now. The lack of guidance did not place everything on hold. This view was supported by Nigel Macdonald.

Agenda Item 6 - Compliance query from Seagram Distillers plc

11. Sir Andrew Hugh Smith advised that it was a difficult situation, but in his view the company should put a complex report in their Report and Accounts, explain any outstanding ordinary shares and the very tight controls exercised on a formal basis. The Chairman added that a statement on the company's system of global control would also be helpful. The Secretary agreed to submit the query to the Head of Listing at the Stock Exchange for ratification of the above views.

Agenda Item 7 - Controlling Shareholders

12. The Chairman said that the question of controlling shareholders had arisen when he was visiting both Toronto and Singapore, mainly in the form of queries on the composition of the board. The situation also arose in the UK in family companies where there was a controlling shareholder. He considered that the guidance in the new Yellow Book was clear, but queried whether the Stock Exchange would be able to monitor it effectively.

13. Sir Andrew Hugh Smith advised that there were cases of a 60% or higher shareholding. However, it was a matter of judgement and the Listing Department had to look carefully at each case, usually when a company was just coming to the market. It was of particular importance when only, say, 25% of the equity was put on the market.

14. Jonathan Charkham said he felt that there was a related question of tenure of office for non-executive directors. If there were a controlling shareholder, they could feel vulnerable and lose their independence, effectively taking on the role of adviser. He suggested that the Committee's successor body should look at the issue further. However, in response to a suggestion from Martin Taylor, it was agreed that the Monitoring Sub-Committee should investigate whether it could take this on.

Agenda Item 8 - Update on distribution of the Report and Code

15. The Secretary reported that, excluding those copies distributed free to companies at the time of publication, over 8,500 copies of the Report and Code had been distributed during 1993, and over 300 in the first month of 1994.

9. Agenda Item 9 - Any Other Business

16. The Chairman advised that, together with Mike Sandland and the Secretary, he had held some informal briefings for the press on 17 February. These had been instigated on the advice of the Committee's PR consultants with a view to the press gaining a better appreciation of the Committee's current position, and to try to defuse

some of the more extreme comments being made at the time. Overall, the briefings had been well-received.

17. The Chairman drew the attention of those present to the Institute of Directors draft on "Good Practice for Boards of Directors". Sir Dermot de Trafford added that the IOD was in no way trying to "outdo" Cadbury, but that where Cadbury could be equated with integrity, the IOD could be equated with enterprise. The Chairman also advised of the training courses for directors to be run at Henley, Manchester and Ashridge, in June, September and November respectively. These three were pilot courses, and more would follow if they were successful. He agreed to contact John Harper at the IOD to see if it would be possible for some Committee members to sit in on some of the sessions, in view of the Committee's interest.

Agenda Item 10 - Date of Next Meeting

18. The next meeting will be held on Thursday 19 May at the London Stock Exchange. The meeting will now commence at **4.00 pm**, instead of 3.00 pm as previously advised.

Gina Cole
Secretary
2 March 1994