

Lord Clement-Jones CBE



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Department of Trade and Industry
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A handwritten signature in black ink, appearing to read "Derek Higgs".

Prior to entering the House of Lords I was the company secretary of Kingfisher plc - between 1986 and 1995- and before that in various legal roles in major plc's.

I believe that, following the events of this year, we have reached a watershed in corporate governance. We have had crises of confidence in corporate governance in the past after which there have been attempts to deal with corporate governance in a voluntary way. As a result we have had reports from Cadbury, Greenbury, Hampel, Turnbull and the combined code. These have attempted to fashion a succession of governance and risk management tools to give investors assurance about the governance and risk management of their companies.

Those attempts were worthy, and it is only with some reluctance that I have concluded that the current role and responsibilities of the non-executive director are no longer viable for major PLCs.

In the past, we have relied on the non-executive director—sometimes a retired professional or executive, often a busy current full-time executive—to fulfil the role of watchdog on behalf of the shareholders. In reality, however, despite attempts to boost their role through the various codes, that is a quite impossible task, except, perhaps, for a limited after a crisis has already happened.

Many companies now have audit committees and remuneration committees, the membership of which is often entirely made up of non-executives, yet abuses have nevertheless occurred nonetheless.

The other frequently cited role of non-executive directors is that of safeguarding the position of shareholders and investors and engaging in regular communication with them. Chief Executives, however, regard that-or at least the communications role- as a major part of their role, as the share price is key to the perception of a company, to the measurement of performance and, indeed, to their own bonus.

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Non-executives can and do have a major impact on the corporate social responsibility aspects of a company. But the question that needs to be asked is whether in many cases the commitment to CSR is more than skin deep.

Finally I believe that it is possible for some experienced non-executives to play a valuable strategic advisory role for executive directors. But that is as far as it goes.

The fact is that executive directors are far better informed than non-executives will ever be on matters relating to the company on whose board they both sit. It is no longer tenable that non-executives should have the same legal duties as executive directors. Someone being paid to do, say, one day a month for a major company is hardly in a position to argue with the full-time executives of that company. Often they are appointed precisely because they will not do so.

Though I am happy to discuss future governance of the accounting profession and Patricia Hewitt's recent statement following the interim report of the co-ordinating group on accounting and auditing issues is of interest-I do not believe that that is at the root of this problem.

Companies get the auditors they deserve. Unless the governance of a company is strong, the professional advisers will inevitably see their main route to retaining influence as serving the interests of the executive management team of the company. That is professional and human nature.

How many auditors will actually spill any beans at all to the non-executive audit committee when the executive directors are asked to leave the boardroom, or express doubts about any aspect of the company's financial controls? I do welcome your own review of the role of the non-executive director therefore. I am pleased also that the Secretary of State wants to see more active institutional shareholders following the Myners review.

We already have two types of director. They should have different legal duties. I believe we should rapidly move towards a fully effective two-tier board system for our major (ie FTSE 100) companies. A supervisory board should be charged with the duty of ethical and financial quality control and governance. That board should be accountable to shareholders for that aspect of the company. The members of the board should be properly remunerated; they should be serviced by its own staff; and they should be fully supported by the necessary legal and financial expertise.

There is a good case to have the internal audit function reporting to that supervisory board.

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On the other hand, the management or executive board should be responsible for commercial strategy, trading and financial performance.

I am a reluctant convert to changing governance structures for major companies but the new Companies Bill will provide the opportunity for doing so. I do not believe that we can carry on tinkering about with a bit more corporate governance here and a bit more corporate governance there. If we are genuine about ensuring proper governance, protecting shareholders' interests, managing risks and so on, we need to think more radically. A two-tier governance system deriving inspiration from continental models, but being far more proactive and with responsibilities far more carefully defined, is the best way forward.

With Best Wishes

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