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Dear Mr Moxey,

Creating value through governance – towards a new accountability: a consultation

Introduction

We are the Quoted Companies Alliance, the independent membership organisation that champions the interests of small to mid-size quoted companies. Their individual market capitalisations tend to be below £500m.

The Quoted Companies Alliance is a founder member of European**Issuers**, which represents over 9,000 quoted companies in fourteen European countries.

The Quoted Companies Alliance Corporate Governance Expert Group has examined your proposals and advised on this response. A list of members of the Expert Group is at Appendix A.

Response

Firstly, we would like to repeat our thanks to you for attending a meeting of our Corporate Governance Expert Group in order to discuss some aspects of this consultation in greater detail. It is clear that both ACCA and the Quoted Companies Alliance share the view that governance should enhance companies, rather than inhibit them. It was particularly useful to explain to you our thinking behind the drafting of the Quoted Companies Alliance Corporate Governance Code for Small and Mid-size Quoted Companies (QCA Code) (most recent edition May 2013).

We welcome the opportunity to respond to this consultation. We welcome ACCA's initiative to conduct an in-depth study to help promote better understanding of good corporate governance and to encourage debate on how this can be improved. We have considered ACCA's report and advised on key aspects that we believe should be taken into consideration by ACCA when producing its updated paper reflecting the responses received.

Responses to specific questions

Q1.1 Do you agree with the seven hypotheses? If not, in what way(s) do you disagree?

We have considered the seven hypotheses individually below:

1 - There is confusion as to what governance is for and what can be expected from good governance.

No, we do not believe this statement is true. Whilst we appreciate that there are often challenges in the delivery of governance, we believe that the purpose of corporate governance is clear.

2 - Regulation of governance and risk management has not helped to create a healthy corporate culture or effective boards.

We generally agree with this hypothesis. We believe good governance arises from companies rather than regulation. As we set out at the beginning of section 3 of the QCA Code, good corporate governance promotes and maintains good behaviour. Regulation will only ever be focussed on outcomes. Culture is most effectively developed from within an organisation.

3 - Governments, companies and shareholders have used unreliable measures to manage performance.

We agree with this statement and strongly believe that governments, companies and shareholders need to work to improve these over time.

4 - Boards often have less control over companies than is generally recognised.

This statement is false. Boards have full control, subject to reserved shareholder rights. Executive management will always be accountable to the board. If a board is too weak to be an effective foil to the executive, the constitution of the board needs to be examined.

5 - Many people mistakenly view governance as merely structure and process, whereas it should be seen as a complete system with purpose, inputs and outputs and one that involves people.

We agree. Viewing governance as merely structure and process is both incorrect and harmful.

6 - Boards and executives of many large listed companies have become unaccountable.

We generally disagree. We believe that shareholder voting indicates otherwise. The most significant break in the chain is probably between senior executives and junior staff.

7 - Governments and regulators have pursued a simplistic incremental approach to reform and have failed to consider the broader context of the whole system. Attempts to deal with symptoms have had unintended consequences; root causes of problems remain unaddressed.

We do not understand the hypothesis above. We believe that the focus in corporate governance analysis should be in the behaviours of companies rather than the actions of law makers and regulators – one cannot make rules as to how a company should make decisions. We do have concerns that too much of the public governance debate for all companies is directed by the failures in both governance and regulation of a small number of institutions in the financial services sector.

Q1.4 Has corporate governance become too focussed on form and compliance at the expense of the quality and integrity of decision making?

Far too often corporate governance debates, codes and reports focus on structures and processes, omitting two important factors: having clarity of objectives and the people in place with the right skills and experience to deliver those objectives.

As we set out in the QCA Code, good corporate governance is a dynamic relationship between the company, its directors and its shareholders (i.e. the entity, its managers and the providers of its risk capital). Companies need to focus decisions and how they move in the best interests of their shareholders, who in turn are influenced by a number of external factors including regulators, legal framework and social responsibility. To focus on form and compliance by creating complex but irrelevant arrangements, unsuitable for the business, will only create a false sense of security. Good corporate governance processes should enable quality decision making and reduce the risk of poor decisions.

Q3.1 Should creating sustainable value be the overarching purpose of governance? If not, can you suggest a better purpose?

As stated in the QCA Code, "the objective of corporate governance is to deliver growth in long term shareholder value by maintaining a flexible efficient and effective management framework within an entrepreneurial environment".

Indeed, we believe that the clear focus of corporate governance should be creating and preserving value for shareholders and see growth in long term shareholder value and as a guard against value destruction as well. We understand that ACCA's view is focused on creating new growth, not preservation of value; in that sense, we do not agree with ACCA's definition of the purpose of corporate governance.

Q6.1 Must boards be able to hold management to account? / Q6.2 Must shareholders be able to hold boards to account?

We generally support a focus on greater accountability. We have set out in our QCA Code our firm view that the chairman of the board has primary responsibility for corporate governance within the company. The directors have legal obligations to promote the long term interests of the members of the company as a whole. The chairman of the board is responsible for determining where responsibility lies within the company for delivery of key outputs and ensuring such arrangements are effective.

Shareholders are the people with the right to select or reject directors, and the ability to reject any directors who might be intent on objectives that the shareholders disagree with. For that reason, we believe that having the right people is a key factor to achieving the objectives of the organisation, as without the right people, even the best structures and processes will fail to deliver the desired outcomes.

Q7.1 Is the comply or explain approach working as it should? / Q7.2 Should 'apply and explain' replace 'comply or explain'?

"Comply or explain" is a concept that has taken root and matured. It is now firmly adopted in the UK and in many places around the world (importantly within the European Commission) as an appropriate description of the role Codes have to play. The work carried on by the Financial Reporting Council and others in promoting good disclosures reflects the maturity of attitudes towards "comply or explain". Furthermore, Companies Act 2006 changes to narrative reporting emphasise the importance of a clear and understandable corporate narrative. Accordingly, we do not think that there will be any benefit in seeking to redefine "comply or explain" to "apply and explain" or anything else.

Q7.7 Which of these relationships is most problematic? Between: (a) executive management and boards (b) boards and institutional shareholders(c) institutional shareholders and savers. Are there any simple fixes?

Whilst this tests the boundaries of corporate governance, it is probably the case that the greatest area where further accountability is required lies between professional intermediaries and ultimate investment holders (e.g. participants in pension schemes and investors in collective investment schemes). It is noted that the fiduciary duties of investment intermediaries is currently under the review of The Law Commission.

Q8.3 Should economic and other policies to promote growth attempt to encourage companies to create value rather than capture value that others have created? How could regulators, investors and employees do this?

We believe that it is important to emphasise both the importance of value creation and the difficulty in measuring value, which cannot be done just by measuring profit. Likewise, it is important to consider the sustainability of the time period, which may differ from company to company and the differences between sectors when considering appropriate corporate governance focus.

Governance codes can help identify structures and processes that might be suitable for an entity to apply. They do not identify a ubiquitous set of best practices. They should not be treated as a check list of things that have to be done.

Q9.1 Is lack of trust a problem? What should policy makers, businesses, and investors do to restore trust?

As stated in the QCA Code, good corporate governance inspires trust between companies and their shareholders, and “without trust, there will be no appetite from shareholders to invest further or remain shareholders”. Corporate governance reduces the risks that a company faces and by doing so, the cost of capital is also reduced. As stated above in Q6.1 and Q 6.2, the role of the chairman of the board is vital, as the chairman should be responsible and accountable for corporate governance.

We believe that one problem is ignoring the fact that process and culture need to come from the top and be instilled in a company. Investors not only look at how companies apply corporate governance principles, but also find it important to meet with the board and see answers that make them comfortable with, assessing factors such as personality and trust.

Q10.2 Is it a major problem that much regulation, particularly in financial services, has allowed people to avoid personal responsibility or to fail to apply moral judgement? What can be done?

We do not think that the regulation and governance of certain entities within the financial services industry (and the failure thereof) should be used as a benchmark for companies generally.

Q10.7 Do you agree with each of the five recommendations? If not, with which do you not agree, and why? / Q10.8 Do you have any other recommendations? / Q10.9 Have you any further suggestions for how the recommendations could be made to work?

1. *There should be general acceptance that the purpose of governance is to create value sustainably.*

As stated above in 3.1, we believe that the clear focus of corporate governance should be creating and preserving value for shareholders and see growth in long term shareholder value and as a guard against value destruction as well. We understand that ACCA's view is focused on creating new growth, not preservation of value; in that sense, we do not agree with ACCA's definition of the purpose of corporate governance.

Our views are clearly set out in the QCA Code, being a balance of growth in long term shareholder value whilst maintaining a flexible, efficient and effective management framework within an entrepreneurial environment.

2. *Governance codes and policies should be assessed against the accountability framework at each of the interfaces between management, boards, institutional shareholders and providers of funds.*

   We generally agree. As stated above in Q8.3, Governance codes can help identify structures and processes that might be suitable for an entity to apply. They do not identify a ubiquitous set of best practices. They should not be treated as a check list of things that have to be done.

3. *Companies and investors should develop and report using more suitable measures of performance and value creation.*

   A) Performance should be considered in terms of both value created by the company and the contribution of boards, management and staff.

   B) Corporate reporting should additionally include:

   i. probabilistic information on confidence and uncertainty

   ii. information on the ethical health and values of the organisation, including the assessment and assurance system

   iii. information to convey how, and by how much, companies create sustainable value and contribute to public good

   iv. governance reports should be based on the principle of 'apply and explain' rather than 'comply or explain'

   Subject to the comments above regarding preservation of value vs. creation of new value, we generally agree with 3.A.

   Regarding 3.B, we support high quality, clear disclosure reporting, based on culture rather than procedure. In order to retain trust vested in them by shareholders, directors need to explain how the company is governed in practice rather than simply reiterating sterile published guidance.

4. *Policymakers and institutional shareholders should:*

   – address the asymmetry in the risk : reward ratio between management, shareholders and other stakeholders. Ways should be found to enfranchise savers in order that they can hold institutional investors to account.

– *examine ways to give investors incentives to favour companies that create long-term value for themselves and for society against those that rely on short-term economic rent for their profits.*

We agree that ways should be found to enfranchise savers in order that they can hold institutional investors to account. This is difficult. We do not think that the Investor Forum concept promoted by Professor Kay is intended to achieve this objective, but to give all investors a more effective voice in the organisation. Furthermore, the manner in which shares are voted makes it very difficult for ultimate investors to have an effective voice. However, further consideration of this problem is welcome.

If you would like to discuss any of our responses in more detail, we would be happy to attend a meeting.

Yours sincerely,

Tim Ward
Chief Executive

APPENDIX A

Quoted Companies Alliance Corporate Governance Expert Group

Edward Craft (Chairman)	Wedlake Bell
Colin Jones (Deputy Chairman)	UHY Hacker Young
Victoria Barron	Hermes Equity Ownership Services
Edward Beale	Western Selection Plc
Rob Burdett	FIT Remuneration Consultants
Anthony Carey	Mazars LLP
Jo Chattle / Julie Keefe	Norton Rose Fulbright LLP
Richie Clark	Fox Williams LLP
Louis Cooper	Crowe Clark Whitehill LLP
Madeleine Cordes	TMF Corporate Secretarial Services Ltd
Mebs Dossa	McguireWoods
Kate Elsdon	PricewaterhouseCoopers LLP
David Firth	Penna Consulting PLC
Peter Fitzwilliam	The Mission Marketing Group PLC
David Fuller	CLS Holdings PLC
Nick Gibbon	DAC Beachcroft LLP
Nicola Green / Eleanor Kelly / Jane Mayfield	LexisNexis
Andrew Hobbs	EY
Alexandra Hockenhull	Xchanging plc
David Isherwood	BDO LLP
Nick Janmohamed	Speechly Bircham LLP
Dalia Joseph	Oriel Securities Limited
Claire Noyce	Hybridan LLP
Gabriella Olson-Welsh	McguireWoods
Anita Skipper	Aviva Investors
Julie Stanbrook	Hogan Lovells International LLP
Nicholas Stretch	CMS Cameron McKenna LLP
Peter Swabey	ICSA
Eugenia Unanyants-Jackson	F&C Investments
Melanie Wadsworth	Faegre Baker Daniels LLP
Cliff Weight	MM & K Limited