



### SOME THOUGHTS ON CORPORATE GOVERNANCE (PART 3)

Last month I mentioned that the Grant Thornton report on Corporate Governance covered all companies with a main listing on the Irish stock exchange. I also mentioned that I had started looking at corporate governance issues at companies not covered by that report and I also said that I was coming across some interesting information that might be worth writing about.

In fact what I have decided to do this month is write about one specific company. I have done this because I think that this company is a particularly interesting corporate governance case study.

Before I start talking about the company in question I have to point out that the companies not covered in the Grant Thornton report, i.e., companies listed on the IEX (Irish Enterprise Exchange) do NOT have to follow the Combined Code. I have therefore worked on a completely “what if” basis. In other words if the company in question had to follow the Code, how would they stack up? Any observations I make have to be looked at in the context that no rules have been broken and because I have no specific knowledge of the people in question I am not suggesting that there is anything wrong. All I am trying to do is make people aware that a neutral observer reading the annual report might have some doubts or concerns.

The company in question is the house builder and plant hire company Abbey Plc.



In their Annual Report they state the following:

*The Board is committed to maintaining high standards of Corporate Governance to ensure that the Company is headed by an effective Board which can lead and control the business.*

They do not state their definition of “high standards” so I cannot tell how the board determine whether they meet their commitment to maintain them. All I can say is that everything in the annual report suggests that they believe that they are “maintaining high standards”.

#### **First concern: Combined Chairman and Chief Executive**

The Combined Code provision A.2.1 states the following:

*The roles of chairman and chief executive should not be exercised by the same individual. The division of responsibilities between the chairman and chief executive should be clearly established, set out in writing and agreed by the board.*

The Abbey annual report states the following:

*The roles of the Executive Chairman and Chief Executive are combined in one individual. The directors believe that the Company benefits from consolidating the experience and knowledge of the present*

*Executive Chairman whilst ensuring that there are experienced non-executive, and executive directors for each operating division, to whom concerns may also be conveyed.*

I have to say that I struggle to understand how “the company benefits” from having a combined chairman and chief executive. Surely if there was a separate chairman and chief executive there would be the benefit of having two minds rather than one. Surely Abbey should give a practical example of how the company benefits? Surely it is not enough just to say something without attempting to support that point of view?

### **Second Concern: Independent Directors:**

#### **Part 1**

The Combined Code provisions A.3.1 and A.3.2 state the following:

*The board should state its reasons if it determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination.*

*A smaller company should have at least two independent non-executive directors.*

The Abbey annual report states the following:

*The Board considers all non-executive directors capable of exercising independent judgement.*

There are three non executive directors. One is David Gallagher a brother of the Chairman / Chief Executive. Another is John Hogan a former Managing partner of Ernst Young Ireland and Ernst and Young are auditors to Abbey.

There is nothing to say whether Abbey define David Gallagher or John Hogan as independent. By saying that they are capable of independent judgement appears to suggest that they are defined as independent but then there is nothing to explain the potential conflicts.

#### **Part 2**

The Combined Code provision A3.3 states the following:

*The board should appoint one of the independent non-executive directors to be the senior independent director.*

I can find no mention of a senior independent director.

### **Third Concern: Nomination Committee**

The Combined Code provision A4.1 states the following:

*There should be a nomination committee which should lead the process for board appointments and make recommendations to the board.*

The Abbey annual report states the following:

The Board does not have a formal Nominations Committee. All Board nominations are tabled under “Formal Matters to be Referred to the Board” and consideration of appointments are made by the Board as a whole.

Of the three concerns listed above I would guess that having a combined chairman and chief executive gives me the greatest concern. In saying that I should also point out that the Combined Code also states the following:

*Institutional shareholders should consider carefully explanations given for departure from this Code and make reasoned judgements in each case. They should give an explanation to the company, in writing where appropriate, and be prepared to enter a dialogue if they do not accept the company's position. They should avoid a box-ticking approach to assessing a company's corporate governance. They should bear in mind in particular the size and complexity of the company and the nature of the risks and challenges it faces.*

In other words if I was still working in my old job as a fund manager the Code implies that I should be prepared to enter into a dialogue with Abbey. I should meet them and state my concerns in relation to them having a combined Chairman and Chief Executive and allow them to make their case.

Given that I am no longer an institutional investor I will have to rely on others to do this work and all I can do is attempt to point out where I believe there are issues.

One of the conclusions reached in the Grant Thornton report was the following:

In a period of unprecedented economic turmoil marked by company failures and financial scandals, it is clear that companies are doing enough to comply with the provisions of the Code whilst paying lip-service to the spirit and values exemplified by good corporate governance.

I wonder what conclusions they would reach if they got round to looking at Abbey?

Would they conclude that they are only paying lip-service to good corporate governance standards?

In conclusion I think that Abbey makes an interesting case study of how Corporate Governance is being implemented in one Irish company and so if you ever get to meet Charles Gallagher please ask him about his reasons for being Chairman and Chief Executive.



Charles Gallagher