



Mr Chris Hodge
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Dear Chris

GENDER DIVERSITY ON BOARDS: CONSULTATION DOCUMENT

Railpen Investments welcomes the opportunity to respond to the Financial Reporting Council's (FRC) consultation on "Gender Diversity on Boards". The consultation is timely, given the recent review by Lord Davies of Abersoch, entitled 'Women on boards', and the emergence of considerations on diversity as a key theme in the debate about the quality and performance of boards, and as a way to improve board effectiveness, in many markets around the world.

We agree with the FRC that 'diversity, in all its aspects, serves an important purpose in connection with board effectiveness'. The concerns identified with respect to the impact on board effectiveness from the low percentages of women directors, namely (i) the encouragement of group think; (ii) a failure to make full use of the talent pool and (iii) weaknesses in terms of connectivity with, or understanding of, customers and workforce and offer little encouragement to aspiration among female employees, cover the myriad of reasons why the issue must be addressed. However, diversity considerations should come from the perspective of board effectiveness, which provides an appropriate segue into considerations for changes to the UK Corporate Governance Code ('the Code').

We consider that companies should be required to have a diversity policy, which applies across the organisation and they should be required to disclose their processes on how diversity on the Board and a diverse workforce across the organisation will be achieved. Any consideration on diversity should not be at the expense of appointing the best qualified candidate, and equally, should not be limited to gender as we consider diversity includes all forms of differentiation related to gender, race, skills, background, ethnicity and professional experiences. These considerations are not mutually exclusive and one does not need to be

compromised for the other. Companies should be required to disclose their processes on how diversity on the Board and a diverse workforce across the organisation will be achieved.

The most compelling outcome of Lord Davies' review was the economic and business case for addressing the gender imbalance in the current structures of the boards of UK Plc, which moves the debate away from a social issue, a legitimate consideration in its own right, to an urgent business imperative. As the Davies review indicates, the problem is about supply *and* demand; and if the challenge is to be addressed, multiple parties need to act: Chairs of Boards, Chief Executives, shareholders and executive search firms. As a direct response to the recommendations by Lord Davies, we look forward to assessing the disclosures by Chairs of FTSE 350 companies of their aspirational goals in terms of the percentage of women they aim to have on boards in 2013 and 2015, which are due for publication by September 2011. This will give an insight into how realistic it is for the gender imbalance to be addressed in the short term whilst also providing a framework around which engagement between shareholders and companies can take place.

Are changes to the Code needed in order to help achieve more diverse and more effective boards?

Whilst we are not supportive of quotas or regulation, we do consider that a change to the UK Corporate Governance Code is necessary in order to emphasise the importance of robust, and swift, improvements in this area. In our opinion, such a change will compel the boards of UK Plc to move towards improving their gender balance, rather than simply considering the issues, as they will be expected to comply with the change adopted. Therefore, a disclosure requirement in this regard would be beneficial and would help focus the attention of boards, and their Chairs, on the issue. The Code should require listed companies to establish a policy concerning boardroom diversity, in line with the recommendations from Lord Davies' review, as well as the establishment of measurable objectives for implementing the policy, and disclose annually a summary of the policy and progress made in achieving the objectives. Such a narrative on the *actual progress* made will be most illuminating, as the real challenge for boards is to turn targets into reality.

Principle B.2: Provision B.2.4 - reporting by the Nominations Committee

We consider that Principle B.2 is the appropriate place in which to incorporate the changes to the Code and we welcome the FRC's suggestion that there should be specific wording in Provision B.2.4 requiring a description of the board's policy on gender diversity. The suggested wording in Provision B.2.4 of that Principle is appropriate, although we consider considerations on diversity should not be limited to gender, whilst recognising that this is an area that was the focus of Lord Davies' review. Therefore, we would offer the following as an alternative to the suggested wording put forward by the FRC:

B.2.4: *This section should include a description of the board's policy on diversity, in all its aspects, including considerations related to gender balance; any measurable objectives that it has set for implementing the policy; and progress on achieving the objectives.*

Principle B.6 - Board Evaluation

We consider that it is also appropriate to include an additional supporting principle to the Code in Principle B.6 relating to the board evaluation process on the topic of all aspects of diversity. Therefore we would offer the following as an alternative to the suggested wording put forward by the FRC:

Evaluation of the board should consider the balance of skills, experience, independence and knowledge of the company on the board, the board's policy on diversity, in terms of gender and other aspects of diversity, how the board works together as a unit, and other factors relevant to its effectiveness.

Gender Diversity Policy

We agree with the FRC that Lord Davies' recommendation on the *actual* information to be provided by Chairs of boards on the appointment process and how they have addressed diversity does not require a change to the Code. However, we do consider that it would be helpful for the FRC to set out some of the key elements that should be considered in a diversity policy (and not limiting them to gender considerations). One suggestion as to where such guidance might appear would be as an Appendix to the Code. This would provide a helpful framework for companies, such that they would have guidance on what needs to be reported. The importance of transparent reporting in this area, in terms of meeting the requirements, as well as the processes in place to facilitate this, should not be underestimated, especially given that the Code is applied on a 'comply or explain' basis. It would also be helpful to shareholders if the FRC provided some sort of pro-forma on best practice reporting in this area, whilst being cognisant that no two boards are the same and their differences should be recognised.

Timing of changes of the UK Corporate Governance Code

We would prefer that any revisions to the Code were implemented to begin on or after 29 June 2011, especially given that companies would not be required to report on the provisions until 2012, and FTSE 350 companies may, in any event, choose to respond more quickly as requested by Lord Davies. Further delay would give the impression that diversity is not a pressing matter. We would rather not wait for any possible regulation that may be made by the Government to implement Lord Davies' recommendation on reporting the percentage of women on boards, in senior management and throughout the organisation. We are of the opinion that boards will be looking into these issues and will be ready to report on them, especially given that Lord Davies has called on the Chairs of all FTSE 350 companies to announce their aspirational targets by September 2011 and that companies should meet his various recommendations on disclosure around these issues in their 2012 Corporate Governance Statement 'whether or not the underlying regulatory changes are in place'. We think changes to the Code within the timescale indicated would strengthen further Lord Davies' recommendations and compel Boards to meet his requirements voluntarily, instead of being forced to by regulation. The achievement of diversity on boards through best practice processes as opposed to regulatory enforcement is also likely to achieve better quality of improvements in this area, instead of evidence of an increase in the appointments of women on boards to meet regulatory targets.

Additional considerations

We also offer the following suggestions for consideration:

- We would suggest that there be a requirement to explain how a Board will achieve the targets it will set itself under Lord Davies' review; and how it will incorporate considerations on gender diversity and other aspects of diversity into their longer term succession planning processes.
- We consider that there should be separate process in place to address the gender balance in the roles of executive directors and the roles of non-executive board members, as the skill set and experience of each type of directorship is quite different. Such incorporations into the UK Corporate Governance Code will also have the benefit of providing a further framework for shareholder engagement on the issue, given the Code applies on a "comply or explain" basis. We intend to begin to raise these considerations with UK companies in which we invest as part of our engagements with them and will consider if it is appropriate to adapt our UK corporate governance guidelines to indicate our position on this.
- We acknowledge that investors as owners of companies also have a role to play in encouraging greater diversity and the FRC could look into whether there are implications for the Stewardship Code when it conducts the next review of that Code.
- We consider that the brief of Nominations Committees needs to be varied and widened. The work of executive search firms is influential in this regard, in presenting potential candidates to Nominations Committees, and we are encouraged that a voluntary code of conduct has recently been published by leading executive search firms, in response to Lord Davies' Review, which addresses a range of issues related to succession planning and diversity goals and includes a recommendation that 30% of candidates be female¹. However, there is also an onus on independent members of the Nominations Committee to ensure that fair consideration is given to all candidates. The leadership of the Chair of the Board in encouraging diversity is critical in this regard.
- We would also refer the FRC to the work of the 30% Club in the UK², a group of Chairmen and organisations committed to bringing more women onto UK corporate boards. Its members have declared their voluntary support for a goal of 30% of boards being female by 2015, and are taking actions to achieve it. We think this provides a realistic target for change over the near term.

¹ Press notice and Voluntary code available at <http://www.mwmconsulting.com/downloadables/HeadhuntersCode-200711.pdf>

² <http://www.30percentclub.org.uk/press/industry-leaders-endorse-growth-through-diversity/>



We look forward to hearing the outcome of the consultation and we would be happy to meet with the FRC to discuss our response in more detail.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Deborah Gilshan', with a long horizontal flourish extending to the right.

Deborah Gilshan
Corporate Governance Counsel

About Railpen Investments

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