

Komit  for god Selskabsledelse
Sekretariat: Erhvervs- og Selskabsstyrelsen
Kampmannsgade 1
1780 K benhavn
By email to cg-komite@eogs.dk

London, 22 February 2010

Dear Mr Scheibye

Response to the revised Danish code of corporate governance

I am writing to offer Hermes' comments on the proposed revision of the corporate governance code ("the Code") for Denmark.

Hermes is one of the largest pension fund managers in the City of London and is the principal manager of the BT Pension Scheme. As part of its Equity Ownership Services (EOS), Hermes advises and speaks for clients in respect of equities worth around  60 billion. Hermes is closely involved in corporate governance issues and environmentally and socially responsible investing across Europe.

Hermes takes a close interest in matters of company law and regulation because they set the context for the exercise of our clients' rights as part-owners of the companies in which they invest. We seek to safeguard our clients' current rights and also to enhance the transparency and accountability of companies and their directors to their long-term owners.

We acknowledge the comply-or-explain approach embedded in the code which reflects the tradition of market-based regulation in the Danish market. We particularly welcome the active dialogue between owners and companies that these reflect.

Chapter 1 - The general meeting

The revision's chapter 1.3 aims to enhance the dialogue between shareholders and company. Improving transparency and proxy voting facilities will be beneficial for institutional investors. Hermes represents and votes on behalf of clients with investments in more than 8000 companies worldwide. It is our view that improvement and simplification in the voting procedures will benefit both investors and companies. We find the proposals overall in line with our views.

1.4 Takeovers

We find the Code's provisions on the board's recommended conduct in cases of takeovers useful but not complete. A recommendation to companies to develop guidelines of how to act in the event of a takeover situation would be valuable.

Chapter 2 – The role of stakeholders and corporate social responsibility

The proposal advises that the board should develop corporate social responsibility policies. It is our view that a company run in the long-term interests of its shareholders will need to manage effectively relationships with its employees, suppliers and customers, to behave ethically and to have regard for the environment and society as a whole. We would like to stress that the companies should understand and report on issues which are *relevant* for the risk and long term valuation and prosperity. Environmental matters, employees relations, ethical and social issues must be managed and discussed to the extent necessary to understand the development, performance or position of the company. We recommend that directors consider how these factors fit within the context of the reporting to shareholders and stakeholders. Where such factors are important risks to the future success of the company, this will need to be managed and disclosed. Many companies may need to think about environmental impacts and the future costs that these may entail. Consumer-facing businesses are likely to need to discuss customer relations and management of risks to their reputation. Most boards will need to consider discussing the retention and development of key staff. We consider developing policies on these matters as an integral part of directors' and management's responsibilities. Adding it to the Code provisions may be a good way to highlight these expectations. From this it is clear that we seek tailored disclosure and not philanthropic or generic reports.

Chapter 3 – Openness and transparency

We strongly support the proposal that companies provide stock market disclosure in English as well as Danish. In 3.1.4 companies are advised to provide guidance on the future prospects of the company and underlying assumptions. Companies' guidance policy is a difficult topic. We support that companies provide the market with overall projections and assumptions but are careful with detailed guidance of factors which are outside the scope of the management's control. We welcome clarity of companies' key performance indicators and targets related to these, whilst we believe that earnings guidance has a negative impact on stock market behaviour.

Chapter 4 – The tasks and responsibilities of the board

The revised Code recommends that the board annually reassess the company's strategy, the competence of the board, control mechanisms, terms of reference documents and the general communication between board and management. These are all measures of good order that we support. The chapter also recommends that the chair does not engage in work for the company. This is a sound principle to ensure independence and accountability.

Chapter 5 – Board composition

The chapter advises that the board publish its competence profile to the general meeting. We would suggest that the nominations committee describes this in the report put before the general meeting when directors are elected. We support the recommended annual self-assessment process.

5.4 Board independence

We believe that companies are best served when boards have a core of vigorously independent directors on whom shareholders can rely for the independence of their judgement and who can act as agents for change should the need arise. Generally we lean on the Cadbury committee's definition which describes independent directors as being free from any business or other relationship that could materially interfere with the exercise of their independent judgement. We support the Code's requirement that at least half of the directors are considered independent of special interests.

In particular, we note that foundations have significant shareholdings in many listed Danish companies. While we are supportive of the involvement of foundations in the corporate governance of companies they are invested in, we consider that the relationships between the board and all the shareholders should be "at arm's length". We would therefore suggest a definition of director independence that addresses this issue by explicitly including the notion of independence from the controlling foundations.

As part of the report to the annual meeting regarding director elections we would support a statement about the individual board members' independence. We also welcome guidelines which put limits of assignments directors should take on in order to be valuable and dedicated contributors to the board.

5.10 Board committees

Audit committee

We strongly support the recommendation to appoint an audit committee. In several countries this is now a legal requirement. The chapter introduction highlights the importance of committees to prepare the discussion in the boards rather than take the core discussions and decisions away from the overall board. Our impression is that audit committees improve accountability and the efficiency of the board's decision making process.

Nomination committee

We also give our support to the naming of a nomination or election committees. In our view good nominations procedures are pre-requisite for a good board composition. We would have liked to see clearer recommendations of the composition of the nominations committee. In Norway and Sweden the nominations committee consists of shareholder nominated members outside the board. This is a unique model and it would be interesting to get the Danish Code Committee's view on it.

In 5.10.6 the Code advises that information about the committee members should be disclosed. We would like to add that the contact details of the chair of the nominations committee should be stated and investors encouraged to present candidates or profiles for directors.

Remuneration committee

A remuneration committee of independent directors is well placed to discuss executive remuneration on behalf of the board. Actual and potential awards should not be excessive and should be directly related to the success of the company and aligned over time to the returns achieved by shareholders. Discussions about executive remuneration have a tendency to be complex and lengthy. A committee which has the responsibility to prepare the debate can be highly valuable in terms of decision efficiency and quality. We support the recommendation that companies should appoint such a committee.

Remuneration committees should explain proposed schemes clearly to shareholders, justifying the structure of the scheme and the relevance of the performance criteria chosen. Schemes should be structured as simply as possible to ensure they can be understood by participants and monitored by shareholders. The link between company performance and executive reward should be clear. The effect of the scheme should be illustrated with examples showing rewards at various performance levels.

We support the recommendation of a formal self-assessment of the board and would add that the process is used as a basis for the work of the nominations committee.

Chapter 6 – Executive and board remuneration

We welcome the Committee's suggestion that remuneration reports are presented for shareholders' vote at the general meeting. Incentive schemes should be designed to reward exceptional performance. Awards should be scaled against achievement of performance criteria, with a relatively low payout if the minimum target is achieved and full payout only for truly exceptional performance. No award should be made where targets are not met. The measure used will vary depending on the type of incentive but performance should be compared to an appropriate benchmark or peer group. Awards should not be made unless there has been improvement in the underlying real financial position of the company. In 6.1.5 the recommendations give detailed guidelines on variable pay parameters. We find these to be in line with our guidelines and welcome them as a Code provision.

In 6.1.6 it is recommended that board members are not remunerated in by options or share programmes. We would welcome directors to hold shares in the company and thereby assure alignment of interest with owners and would not support this suggestion. This can be ensured by paying parts of the director remuneration in form of shares or that directors are encouraged to invest themselves. We do however endorse the principle suggested in the Code that directors should not participate in options programmes or performance-related schemes as that could reduce the power of accountability.

The Code suggests that share options should have a minimum of three years vesting period. We believe that is a good principle and would also encourage companies to set a strike price at a premium to the current share price.

On the issue of severance pay we believe that two year's pay is generous and we would favour a limit of one year, we can however support the suggested proposal.

We support the various suggestions about enhanced transparency of the remuneration including possible "change-of-control" clauses.

Chapter 8 – Risk management and internal control

We support the requirement to articulate the most critical risk factors to the company's objectives and strategy. It is important to ensure that this should not be a comprehensive list of all possible risks to the business but should focus on those 'principal' ones that are significant enough to be discussed at board level.

We trust that you will consider our views and hope they provide useful input into the revision process. If you would like to discuss our views in further detail, please do not hesitate to contact me.

Yours sincerely,



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