



*CFA UK is a member society of*



Chris Hodge,  
Corporate Governance Unit,  
Financial Reporting Council,  
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Aldwych House,  
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London WC2b 4HN

25<sup>th</sup> July 2011

Dear Chris,

The Chartered Financial Analyst Society of the United Kingdom (CFA UK) welcomes the opportunity to respond to the FRC's consultation on Gender Diversity.

The society represents investment professionals in the UK, most of whom hold the Chartered Financial Analyst<sup>®</sup> (CFA<sup>®</sup>) designation and work as front office investment professionals (managing portfolios, researching securities and advising on asset management). This response has been prepared by CFA UK's Professional Standards and Market Practices Committee. The society has not surveyed members in relation to this consultation.

CFA UK supports any initiative that promotes the highest professional and ethical standards and takes the view that Board effectiveness is an integral part of market integrity. As we stated in our response<sup>1</sup> to the DBIS' 'Long Term Focus for Corporate Britain', "UK publicly listed companies, like any business entity, are allocatively efficient when they generate economic profits... Too often, companies and investors focus on accounting profits – the published net profit figure which is then used to derive earnings per share. Companies and investors should value companies by determining the net present value of future free cash flows to the firm (FCFF) discounted by its weighted cost of capital (WACC – the rate of return required by investors for investing capital in the company)." The governance mechanisms within companies play a crucial role to ensure that these companies are allocatively efficient, otherwise shareholder value is destroyed. Similarly, where Boards are ineffective they should be held to account.

#### About CFA UK and CFA Institute

The CFA Society of the UK (CFA UK) represents the interests of more than 9,000 leading members of the UK investment profession. The society, which was founded in 1955, is one of the largest member societies of CFA Institute and is committed to leading the development of the investment profession through the promotion of the highest ethical standards and through the provision of continuing education,

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<sup>1</sup>CFA UK response to DBIS' 'Long Term Focus for Corporate Britain' - call for evidence  
[https://secure.cfauk.org/assets/2162/CFAUKDBIS\\_Long\\_Term\\_responseSENT.pdf](https://secure.cfauk.org/assets/2162/CFAUKDBIS_Long_Term_responseSENT.pdf)

advocacy, information and career support on behalf of its members. Most CFA UK members have earned the Chartered Financial Analyst® (CFA®) designation, or are candidates registered in CFA Institute's CFA Program. Both members and candidates attest to adhere to CFA Institute's Code of Ethics and Standards of Professional Conduct.

CFA Institute is the global association for investment professionals. It administers the CFA and CIPM curriculum and exam programs worldwide; publishes research; conducts professional development programs; and sets voluntary, ethics-based professional and performance-reporting standards for the investment industry. CFA Institute has more than 100,000 members in 140 countries, of whom more than 90,000 hold the Chartered Financial Analyst (CFA) designation.

## **Response to the consultation**

### **Summary**

Overall, CFA UK acknowledges what the FRC is seeking to achieve, although this should not warrant changing the Code for changes sake. Effective corporate governance is about having the appropriate people with the skill sets that can ensure the company maintains its allocative efficiency and generates value for shareholders.

The FRC should focus on the effectiveness of the Code rather than the extent to which certain groups in society are adequately represented. It would be better for the FRC to focus on more prominent issues such as–

- 1) To what extent does the Code encourage companies to cover the cost of capital?
- 2) How does the Code ensure that Boards select the appropriate Board members?
- 3) What can the FRC do should Boards fall short in their duties?

### **Board effectiveness**

CFA UK welcomes the approach taken by the FRC to incorporate elements of Lord Davies' views on gender diversity on Boards. CFA UK acknowledges the significance of the issue of gender diversity, however it would caution that the spirit of Board effectiveness is not compromised by the sole pursuit of increasing the number of one or more social groups on Boards. The emphasis should be on what the Board member contributes rather than the group they represent.

Boards should ensure their companies are allocatively efficient. Board members should have the capabilities, skills and expertise to ensure that shareholder interests are taken into account and that the executive is generating shareholder value. The effectiveness of the Board will be determined by having the appropriate diversity of skill sets. If attaining the appropriate mix of skill sets results in higher numbers of those considered under-represented on Boards, then this is a welcome secondary benefit. For Boards to have the appropriate diversity of skill sets, more reassurance may be required with respect to the Board selection process.

### **Integrity of the selection process and the supply of Board candidates**

Greater weight should be placed on how Board members are selected and to assess whether or not the process identifies the most suitable candidates available at that

time. Similarly, the selection process should be as transparent as possible so that any barriers that would hinder the identification of suitable candidates are greatly reduced. Where it transpires that Board selection raises concerns there should be a mechanism by which the selection process is subject to an independent review.

It is of course quite possible that the supply of suitably qualified candidates may be limited and this may have a bearing on the quality of candidates available. Here again, further investigation will be required to understand the supply of suitably qualified candidates. Perhaps this is an area where FRC could become more active. In addition, more could be done to train the next generation of Board members so that they learn the lessons from the past and obtain the skills and expertise to become effective Board members of the future.

#### Effective oversight and accountability

CFA UK appreciates that the Code for Corporate Governance is just that - a Code. However, as guardian of the Code, the FRC could do more to ensure that the spirit of the Code is being adhered to when it comes to the effectiveness of Boards. The recent and previous crises have demonstrated corporate governance failure but also market failure, which have yet to be addressed effectively. The FRC has the potential to play a key role in ensuring that Boards are effective in ensuring resources are allocated efficiently and that publicly listed companies generate value.

We trust that these comments are useful and would be pleased to meet FRC staff to explain them or to develop them for committee members.

Yours,

A handwritten signature in black ink, appearing to read 'N. WinterFrost', written in a cursive style.

Natalie WinterFrost, CFA FIA  
Chair Professional Standards & Market Practices  
Committee, CFA UK

A handwritten signature in black ink, appearing to read 'Will Goodhart', written in a cursive style.

Will Goodhart  
Chief executive  
CFA Society of the UK