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Dear Mark

## **Code Governance Review**

I am an independent researcher and consultant working in the energy, financial services and health sectors. I have a particular interest in the governance of companies and the relationships they have with their shareholders and have co-authored two reports related to this subject for the think tank Tomorrow's Company. For the avoidance of doubt, this response sets out my own thoughts on issues in the review and is not representative of any of my clients.

## **A Generic Governance Issue**

The consultation document on the role of code administrators sets out three corporate governance options for code administration. Each of these involves a relationship between the code administrator and at least one company. The differences in the options relate to the relationship between the code administrator and any company that is a network operator.

The document points out the potential conflict of interest when a code administrator is closely integrated with a network owner. However, there is a more general conflict of interest that will exist in each of these cases. This is centred on the corporate responsibilities of director(s) who oversee the code administration function.

The Companies Act 2006 states that the duty of a director is to promote the company's success. Directors have to act in good faith and advance the company's interests, which in turn is defined as the benefit of its members (i.e. current and future shareholders). Directors are fiduciaries and as such are expected to exercise due care and have an obligation of undivided loyalty to the person(s) to whom the duty is owed. Consequently, the director of a network operator with oversight of a code administration function will have a conflict of interest if the administration is to be conducted impartially. Options 1 and 2 in the consultation document will fall foul of this conflict.

Option 3 as written will also fall foul of this problem; however a variation on this theme, by establishing the independent company as a community interest company (CIC), can provide a mechanism to address the issue.

### Community Interest Companies

CICs are limited liability companies designed for social enterprises. Their primary purpose is to provide benefits to a community (which can be the population as a whole) and a statutory 'asset lock' ensures that the assets of the CIC are either permanently retained within the CIC and used for community purposes, or transferred to another asset locked body.

A CIC could be established for the purpose of administering a code. The purpose can be stated as administering the code in accordance with the relevant objectives as set out in a relevant licence, which would mean that the codes would automatically stay in line with the objectives as stated in the licence.

CICs are flexible arrangements. They can be set up as not for profit entities or as for profit organisations, which would maintain a focus on efficient delivery. Further, a CIC could facilitate either in-house delivery of central systems management or the outsourcing of this function. An obligation could be placed explicitly on the directors of the CIC to review such arrangements regularly and report the findings publicly.

Initially, a CIC could be established for each code, but these could in time be merged as the objectives permitted.

### Panel Members

Those elected to be panel members could also be the directors of the CIC, whose duty to promote the success of the company would then be in line with achieving the relevant objectives of the code. If necessary, particular duties can be built into these arrangements; e.g. to ensure that appropriate analysis is carried out or that the interests of consumers and smaller participants are taken into account.

A corollary of this approach would be that the responsibility of panel members would be to deliver the relevant objectives of the code, rather than being representatives of a particular company or organisation. The publication of reasons for decisions would provide an important safeguard for panel members against claims of furthering the interests of any particular organisation.

I believe this presents a pragmatic and proportionate mechanism for dealing with potential conflicts of interest and would be happy to discuss these comments further with you. If you have any questions, please contact me on 07814 009762.

Yours sincerely

**Arthur Probert**