



Irish Stock Exchange

**REVIEW OF THE ROLE AND
RESPONSIBILITIES OF THE DEPUTY
CHAIRMAN OF ESB**

Tom Healy

NB The views expressed in this document are those of Tom Healy and not necessarily those of the Irish Stock Exchange.

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Executive Summary

The review of the role and responsibilities of the Deputy Chairman of ESB was conducted within the terms of reference set by the Minister for Communications, Marine and Natural Resources. Set out below are recommendations in relation to the position of Deputy Chairman.

Recommendations

1. It is recommended that the position of Deputy Chairman be discontinued for the following reasons:
 - The current position of Deputy Chairman does not appear to be necessary to the ESB Board structure; and
 - The existence of the position of Deputy Chairman restricts the Board's ability to appoint an independent chair to act in the absence of the Chairman, when it is considered that the Deputy Chairman may have a conflict of interest.
2. In the event of the discontinuation of the position of Deputy Chairman, the following arrangements should be put in place:
 - The 2001 Board Regulations should be amended to expressly state that in the absence of the Chairman, the Board may appoint, from among the non-executive directors, an acting chairman to take the chair at Board meetings;
 - The choice of acting chairman should be guided by the relevant provisions of the 2003 Combined Code relating to the independence of the Chairman; and
 - Where a non-executive director is acting as Chairman for an extended period of time, the terms of reference of the selected person should be extended to include any delegated duties, beyond those arising from the chairing of Board meetings.
3. However, if the position of Deputy Chairman is to be retained:
 - The 2001 Board Regulations should be amended to specify the role and responsibilities of the Deputy Chairman;
 - The position of Deputy Chairman should be subject to the same independence criteria as apply to the position of Chairman (See Appendix I, Section A.2.2 and Appendix II, Section A.3.1);
 - The letter appointing a Deputy Chairman should clearly set out the role and responsibilities of the position; and

- The legislation governing appointments should make specific provision for the appointment of a Deputy Chairman.
4. To the extent possible, the ESB should continue to comply with the Combined Code on Corporate Governance in relation to the chairman or any director who is asked to act as chairman.

Introduction

In February 2005, the Minister for Communications, Marine and Natural Resources (the ‘Minister’) asked Tom Healy, Chief Executive of the Irish Stock Exchange, to examine the role and responsibilities of the Deputy Chairman position in the ESB in the light of current private sector best practice in corporate governance.

In March 2005, the Minister provided terms of references (‘TOR’) which stated that the review should include an examination of the following:

- The continuing need for the position, including an identification of any advantages and disadvantages attached to the role;
- The changes to the role and responsibilities of the Deputy Chairman that might be implemented in the event of the continuation of the position; and
- The alternative arrangements, including those relating to the chairing of meetings in the absence of the Chairman, which might be put in place in the event of the discontinuation of the position.

In preparing the report, background information was obtained from the Department of Communications, Marine and Natural Resources and from interviews with current Board members and senior executives of the ESB.

Background

Composition of the Board

There are twelve members on the ESB Board comprising the Chief Executive and eleven non-executive members. Of the eleven non-executive members, seven were appointed under the provisions of the Electricity (Supply) Act, 1927 for a term not exceeding five years, but re-appointment for additional terms is provided for. The remaining four non-executive members are Worker Directors appointed under the provisions of the Worker Participation (State Enterprises) Act, 1977 for a term not exceeding four years, but re-appointment for additional terms is provided for.

The Deputy Chairman of the ESB Board is a Worker Director who is serving his sixth term on the Board, having first been appointed to the Board in January 1984 under the provisions of the Worker Participation (State Enterprises) Act, 1977.

Position of Deputy Chairman

The position of Deputy Chairman of the Board of the ESB was established in February 1991.

The present incumbent was first appointed as Deputy Chairman in September 2000 by Mrs. Mary O'Rourke, T.D., Minister for Public Enterprise, until the expiry of his term of appointment to the Board on 31 December 2002. He was re-appointed as Deputy Chairman by Mr. Dermot Ahern, T.D., Minister for Communications, Marine and Natural Resources from 1 January 2003 until the expiration of his current four year term as a Worker Director.

Letters of appointment for the Deputy Chairman

The letters of appointment of previous incumbents stated that the appointment was made by the Government and that the Deputy Chairman would, in the absence of the Chairman, preside at Board meetings.

Both letters of appointment of the current incumbent state that the appointment was made by the then Minister but no reference was made to the role of the Deputy Chairman in the absence of the Chairman.

ESB Board Regulations

The ESB Board is currently governed by Regulations adopted in 2001. These Regulations govern the procedures of the Board in relation to matters such as the meetings, voting, Board members and proceedings of the Board and Committees. These Regulations replaced the 1995 Regulations.

Both the 2001 and 1995 Board Regulations were reviewed to determine what (if any) provisions were made in relation to the Deputy Chairman.

(i) *2001 Board Regulations*

Regulation 50 of the 2001 Board Regulations states the following:

'The members may meet together for the dispatch of business, adjourn and otherwise regulate their meeting, as they think fit.....'

There is no provision for, or reference to, the position of Deputy Chairman in the 2001 Board Regulations.

(ii) *1995 Board Regulations*

Regulation 9 of the 1995 Board Regulations states the followings:

'The Chairman of the Board when present shall take the chair and preside at all meetings of the Board. Should the Chairman be absent the chair shall be taken during his absence by the Deputy Chairman and, in the absence of the Deputy Chairman, by the Member present with the longest continuous tenure of office...'

Under the 1995 Board Regulations, the Deputy Chairman should, in the absence of the Chairman, preside at meetings of the Board.

Evaluation of continuing need for the position of Deputy Chairman

The TOR asked for an examination of the continuing need for the position of Deputy Chairman, including an identification of any advantages and disadvantages attached to the role.

Advantages of the position of Deputy Chairman

The key advantage of the position of Deputy Chairman is that it provides clarity as to who will chair Board meetings in the absence of the Chairman. This may provide greater continuity of leadership if the Chairman is frequently unable to attend Board meetings.

Disadvantages of the position of Deputy Chairman

1. It may not be appropriate for the Deputy Chairman to chair Board meetings where he or she has, or is perceived to have, a conflict of interest, e.g. in the case of a Worker Director, matters relating to, or impinging on, staff pay and conditions; and
2. The existence of the position of Deputy Chairman restricts the Board's ability to appoint an independent person to act in the absence of the Chairman when it is considered that the Deputy Chairman may have a conflict of interest.

Continuing need for the position of Deputy Chairman?

As currently constituted, the position of Deputy Chairman does not appear to be necessary to the ESB Board structure.

Recommendation

It is recommended that the position of Deputy Chairman should be discontinued for the following reasons:

1. The position of Deputy Chairman does not appear to be necessary to the ESB Board structure; and
2. The existence of the position of Deputy Chairman restricts the Board's ability to appoint an independent chair to act in the absence of the Chairman, when it is considered that the Deputy Chairman may have a conflict of interest.

Possible changes to the role and responsibilities of Deputy Chairman, if the position is retained

The TOR asked for an examination of the changes to the role and responsibilities of the Deputy Chairman that might be implemented in the event of the continuation of the position of Deputy Chairman.

In the event that the position of Deputy Chairman is retained, the following matters would need to be addressed:

1. Amending the 2001 Board Regulations to document the role and responsibilities of the Deputy Chairman;
2. Amending the Deputy Chairman's letter of appointment; and
3. Amending the legislation governing appointments.

Amending the 2001 Board Regulations to document the role and responsibilities of the Deputy Chairman

(i) Role and responsibilities of the Deputy Chairman

Unlike the 1995 Board Regulations, the 2001 Board Regulations do not provide for or make any reference to the position of Deputy Chairman. To clarify the position of the Deputy Chairman, it would be necessary to amend the 2001 Board Regulations to set out the role and responsibilities of the Deputy Chairman, in the absence of the Chairman.

In documenting the role and responsibilities of the Deputy Chairman, the ESB should consider the guidance in the 2003 Combined Code¹ ('Combined Code'). Whereas the Combined Code does not contain any provisions in relation to the role and responsibilities of Deputy Chairman, the guidance in relation to the role and responsibilities of the Chairman should be applied to the position of Deputy Chairman insofar as the Deputy Chairman may have to act as Chairman, in the absence of the Chairman.

(ii) Independence of the Deputy Chairman

In addition to the Combined Code guidance on the role and responsibilities of the Chairman, the Board of the ESB should also be guided by the Combined Code provisions in relation to the Chairman and independence.

¹ The Combined Code on Corporate Governance published in July 2003 by the Financial Reporting Council.

Under Code Provision A.2.2 of the Combined Code, the chairman should on appointment meet the independence criteria set out in A.3.1. Compliance or otherwise with this provision need only be reported for the year in which the appointment is made².

Code Provision A.3.1 states that the board should identify in the annual report each non-executive director it considers to be independent. In addition, 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, including *inter alia* if the director:

- has been an employee of the company or group within the last five years
- has served on the board for more than nine years from the date of first election

The Combined Code does not contain any provisions in relation to the independence of the Deputy Chairman. However, it is recommended that the Deputy Chairman should be subject to the same independence criteria as apply to the Chairman. The independence criteria of the Combined Code are set out in further detail in the section entitled “Corporate Governance”.

Amending the Deputy Chairman’s letter of appointment

The letter of appointment to the Deputy Chairman would need to be amended to include a detailed description of the position’s role and responsibilities.

Amending the legislation governing appointments

Despite the position of Deputy Chairman existing since 1991, the current legislation governing board appointments (Electricity Supply Act, 1927 or the Worker Participation (State Enterprises) Acts, 1977) does not appear to provide for the position. It would be appropriate to amend the legislation to make specific provision for the appointment of a Deputy Chairman.

Recommendations

If the position of Deputy Chairman is to be retained, the following should be implemented:

1. The 2001 Board Regulations should be amended to specify the role and responsibilities of the Deputy Chairman;

² Appendix I sets out principle (A.2) and provisions (A.2.1 and A.2.2) of Combined Code relating to the Chairman and Chief Executive. Appendix II sets out principle (A.3) and provisions (A.3.1, A.3.2 and A.3.3) relating to board balance and independence.

2. The position of Deputy Chairman should be subject to the same independence criteria as apply to the position of Chairman (See Appendix I, Section A.2.2 and Appendix II, Section A.3.1);
3. The letter appointing a Deputy Chairman should clearly set out the role and responsibilities of the position; and
4. The legislation governing appointments should make specific provision for the appointment of a Deputy Chairman.

Discontinuation of the position of Deputy Chairman

The TOR requested an examination of alternative arrangements, including those relating to the chairing of meetings in the absence of the Chairman, which might be put in place in the event of the discontinuation of the position.

If the position of Deputy Chairman is discontinued, the following arrangements should be implemented:

1. Amend the 2001 Board Regulations to allow the Board members select a non-executive director to act as Chairman; and
2. In the event that the acting Chairman will have to serve for an extended period, extend the terms of reference for the non-executive director selected to act as Chairman.

Amend the 2001 Board Regulations

The 2001 Board Regulations permit Board members to regulate Board meetings as they think fit. These Regulations would therefore appear to permit the Board to determine who should chair a particular meeting, in the absence of the Chairman. For the avoidance of doubt, it is recommended that the 2001 Board Regulations be amended to expressly state that in the absence of the Chairman, the Board may appoint, from among the non-executive directors, an acting chairman to take the chair at Board meetings.

In appointing an acting chairman, the Board should be guided by the provisions of the 2003 Combined Code in relation to the independence of the chairman. This is discussed in further detail in the next section entitled “Corporate Governance”.

Extend the terms of reference for the non-executive director selected to act as Chairman

The Chairman has numerous duties in addition to running the board and setting its agenda. Where the Chairman is unable to fulfil these duties for an extended period of time, they should be delegated to the acting Chairman.

In this situation, the existing terms of reference of the selected non-executive director should be extended to include these delegated duties. This could be done via a letter to the relevant non-executive director, explaining the extended terms and the period during which the performance of these delegated duties will be required.

Recommendations

In the event of the discontinuation of the position of Deputy Chairman, the following arrangements should be put in place:

1. The 2001 Board Regulations should be amended to expressly state that in the absence of the Chairman, the Board may appoint, from among the non-executive directors, an acting chairman to take the chair at Board meetings;

2. The choice of acting chairman should be guided by the relevant provisions of the 2003 Combined Code relating to the independence of the Chairman; and
3. Where a non-executive director is acting as Chairman for an extended period of time, the terms of reference of the selected person should be extended to include any delegated duties, beyond those arising from the chairing of Board meetings.

Corporate Governance

The TOR asked for a review of the role and responsibilities of the Deputy Chairman position in the ESB in view of current private sector best practice in corporate governance. This is taken to refer to corporate governance standards applicable to private sector listed companies, insofar as those standards are applicable to the ESB.

Codes of practice and corporate governance currently adopted by ESB

The 2003 Annual Report states that the ESB complies with the Code of Practice for the Governance of State Bodies (2001) which sets out a corporate governance best practice framework for State Bodies. It also states that the ESB complies with the corporate governance and other obligations imposed by the Ethics in Public Office Act 1995 and the Standards in Public Office Act 2001.

The Combined Code

As the ESB is a statutory body established under the Electricity (Supply) Act 1927 the provisions of the Combined Code do not apply, nor were they designed for such an entity. However, ESB supports the principles and provisions of the Combined Code and states that it intends to comply to the fullest extent possible and report on such compliance in its annual report for the year ended 31 December 2004.

Compliance with the Combined Code

The relevant sections of the Combined Code relating to deputy chairman, chairman and independence have been reviewed to determine if the ESB is adhering to best practice in relation to corporate governance.

Other than Code provision A.1.2³, there is no other reference to Deputy Chairman in the Combined Code. In compliance with this Code Provision, ESB's annual report discloses the name of the Deputy Chairman of the Board.

Given that the Combined Code does not contain any provisions in relation to the independence of the acting/deputy chairman, the position of Deputy Chairman should be considered in the context of the independence criteria applicable to the position of chairman⁴.

³ Code Provision A.1.2 states the following: 'The annual report should identify the chairman, the deputy chairman (where there is one), the chief executive, the senior independent director and the chairmen and members of the nomination, audit and remuneration committees.....'.

⁴ Appendix I sets out principle (A.2) and provisions (A.2.1 and A.2.2) of the 2003 Combined Code relating to the Chairman and Chief Executive.

Appendix II sets out principle (A.3) and provisions (A.3.1, A.3.2 and A.3.3) relating to board balance and independence.

Code provision A.2.2⁵ of the Combined Code states that the chairman should on appointment meet the independence criteria set out in A.3.1.

Code provision A.3.1 of the Combined Code states that the board should identify in the annual report each non-executive director it considers to be independent⁶. The board should determine whether the director is independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the director's judgement. 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, including if the director:

- has been an employee of the company or group within the last five years;
- has, or has had within the last three years, a material business relationship with the company either directly, or as a partner, shareholder, director or senior employee of a body that has such a relationship with the company;
- has received or receives additional remuneration from the company apart from a director's fee, participates in the company's share option or a performance-related pay scheme, or is a member of the company's pension scheme;
- has close family ties with any of the company's advisers, directors or senior employees;
- holds cross-directorships or has significant links with other directors through involvement in other companies or bodies;
- represents a significant shareholder; or
- has served on the board for more than nine years from the date of their first election.

On appointing an acting/deputy chairman, the Board should be guided by the Combined Code requirements relating to the chairman satisfying independence criteria on appointment. Relationships and circumstances which affect or could appear to affect a director's judgement should be considered by the Board in appointing an acting chairman.

⁵ Compliance or otherwise with this provision need only be reported for the year in which the appointment is made.

⁶ A.2.2 states that the chairman should, on appointment, meet the independence criteria set out in this provision, but thereafter the test of independence is not appropriate in relation to the chairman.

Recommendation

- To the extent possible, the ESB should continue to comply with the Combined Code on Corporate Governance in relation to the position of chairman or any director who is asked to act as chairman.

Appendix I

Chairman and Chief Executive

A.2 Chairman and chief executive

Main Principle

There should be a clear division of responsibilities at the head of the company between the running of the board and the executive responsibility for the running of the company's business. No one individual should have unfettered powers of decision.

Supporting Principle

The chairman is responsible for leadership of the board, ensuring its effectiveness on all aspects of its role and setting its agenda. The chairman is also responsible for ensuring that the directors receive accurate, timely and clear information. The chairman should ensure effective communication with shareholders. The chairman should also facilitate the effective contribution of non-executive directors in particular and ensure constructive relations between executive and non-executive directors.

Code Provisions

A.2.1 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.

A.2.2⁷ The chairman should on appointment meet the independence criteria set out in A.3.1 below. A chief executive should not go on to be chairman of the same company. If exceptionally a board decides that a chief executive should become chairman, the board should consult major shareholders in advance and should set out its reasons to shareholders at the time of the appointment and in the next annual report.

⁷ Compliance or otherwise with this provisions need only be reported for the year in which the appointment is made.

Appendix II

Board balance and independence

A.3 Board balance and independence

Main Principle

The board should include a balance of executive and non-executive directors (and in particular independent non-executive directors) such that no individual or small group of individuals can dominate the board's decision taking.

Supporting Principles

The board should not be so large as to be unwieldy. The board should be of sufficient size that the balance of skills and experience is appropriate for the requirements of the business and that changes to the board's composition can be managed without undue disruption.

To ensure that power and information are not concentrated in one or two individuals, there should be a strong presence on the board of both executive and non-executive directors.

The value of ensuring that committee membership is refreshed and that undue reliance is not placed on particular individuals should be taken into account in deciding chairmanship and membership of committees.

No one other than the committee chairman and members is entitled to be present at a meeting of the nomination, audit or remuneration committee, but others may attend at the invitation of the committee.

Code provisions

A.3.1 The board should identify in the annual report each non-executive director it considers to be independent⁸. The board should determine whether the director is independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the director's judgement. 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, including if the director:

- has been an employee of the company or group within the last five years;

⁸ A.2.2 states that the chairman should, on appointment, meet the independence criteria set out in this provision, but thereafter the test of independence is not appropriate in relation to the chairman.

- has, or has had within the last three years, a material business relationship with the company either directly, or as a partner, shareholder, director or senior employee of a body that has such a relationship with the company;
- has received or receives additional remuneration from the company apart from a director's fee, participates in the company's share option or a performance-related pay scheme, or is a member of the company's pension scheme;
- has close family ties with any of the company's advisers, directors or senior employees;
- holds cross-directorships or has significant links with other directors through involvement in other companies or bodies;
- represents a significant shareholder; or
- has served on the board for more than nine years from the date of their first election.

A.3.2 Except for smaller companies⁹, at least half the board, excluding the chairman, should comprise non-executive directors determined by the board to be independent. A smaller company should have at least two independent non-executive directors.

A.3.3 The board should appoint one of the independent non-executive directors to be the senior independent director. The senior independent director should be available to shareholders if they have concerns which contact through the normal channels of chairman, chief executive or finance director has failed to resolve or for which such contact is inappropriate.

⁹A smaller company is one that is below the FTSE 350 throughout the year immediately prior to the reporting year.

The Exchange considers a smaller company to be one that is included in the ISEQ® Small Cap Index throughout the year immediately prior to the reporting year.