Corporate governance

The Board of GUS supports the principles of corporate governance advocated by the Combined Code (the Code) and, with one exception, in respect of directors' service contracts, fully complied with its provisions throughout the year under review.

The Board's policy over many years has been to limit the service contracts of executive directors to one-year rolling terms and, to this extent, it complies with the relevant provision of the Code. However, the Board believes that it has to have the freedom to make a judgement from time to time, in the interests of shareholders, where a longer period of contract might be appropriate. GUS operates in a global and highly competitive market for senior executives and it is in this context that the Board has made an exception in the case of Alan Smart, the Chief Executive of its South Africa Retail Division. For the reasons explained on page 26, Mr Smart has a contract which provides for 24 months' notice on the part of both the Company and the executive.

Directors

The Board consists of a Chairman, a Chief Executive plus four executive directors and five non-executive directors. Sir Alan Rudge is the recognised senior independent member of the Board to whom concerns can be conveyed.

The Board met six times during the year under review. It has a formal schedule of matters reserved to it for decision.

The Board is supplied in a timely manner with information in a form and of a quality appropriate to enable it to discharge its duties. There is also a procedure under which directors, in the furtherance of their duties, are able to take independent professional advice, if necessary, at the Company's expense. In addition all directors have direct access to the advice and services of the Company Secretary.

The five non-executive directors and the Chairman are, in the opinion of the Board, independent of management and free from any business relationship which could materially interfere with the exercise of their independent judgement. As reported previously, however, some institutional shareholders deem Lord Harris not to be independent, by virtue of the length of time he has served as a non-executive director of the Company, and, accordingly, he stepped down as a member of the Remuneration Committee in the summer of 2000. The non-executive directors are appointed for specified terms.

The Audit Committee consists of three independent non-executive directors: Oliver Stocken (Chairman), Lady Patten and Sir Alan Rudge. It normally meets four times a year with both the external auditors and the Group Internal Auditor present.

The Board acknowledges that the independence of auditors is a subject that has become increasingly prominent in recent months. It is the role of the Audit Committee to ensure that the auditors' objectivity and independence is maintained. It does this by monitoring the level of fees for non-audit services through a six monthly review carried out against established guidelines. These are as follows:

- Audit related services – the auditors' deep knowledge of the Group's affairs means that they are best placed to carry out such work. This extends to, but is not restricted to, shareholder and other circulars, regulatory reports and work in connection with acquisitions and disposals.
- Taxation services – generally the auditors' knowledge of the Group's affairs provides significant advantages which other parties would not have. Where this is not the case the work is put out to tender.
- General – in other circumstances, proposed assignments are put out to competitive tender and decisions to award work taken on the basis of demonstrable competence and cost-effectiveness.

The Remuneration Committee consists exclusively of independent non-executive directors: Lady Patten (Chairman), Sir Alan Rudge and Oliver Stocken. The application of corporate governance principles in relation to directors' remuneration is described in the Report on directors' remunerations and related matters on page 26.

The members of the Nomination Committee are Sir Victor Blank (Chairman), Lady Patten, Sir Alan Rudge, Oliver Stocken and John Peace.

All directors are subject to re-election by shareholders at the first opportunity after their appointment and thereafter in accordance with Article 76.1 of the Company's Articles of Association. This ensures compliance with the Code by providing that all directors are required to submit themselves for re-election at least once every three years.

Relations with shareholders

The Company recognises the importance of communicating with its shareholders and does this through its Annual and Interim Reports and at the Annual General Meeting. Although it does not have precise rules covering meetings with its institutional shareholders, it is always ready to enter into a dialogue with investors, and meetings take place frequently.

All directors normally attend the Annual General Meeting and are available to answer shareholders' questions. Voting at the Annual General Meeting is by way of a show of hands by members present at the meeting unless a poll is validly called. Following each vote on a show of hands, the level of proxies lodged on each resolution and the number of proxy votes for and against the resolution are announced.

Corporate Social Responsibility

Last year's Annual Report devoted four pages to the subject of Corporate Social Responsibility (CSR). This recognised a growing focus on CSR by institutional investors, the Government, non-governmental organisations and the media.

This year, we have published a separate CSR report as the case to demonstrate corporate responsibility grows even stronger. This is available, on request, from the Company Secretary's office or on the GUS website.

A section on CSR is included on pages 32 and 33.

A growing number of mainstream City institutions has decided to incorporate social responsibility into corporate governance frameworks. They view CSR in the context of risks and opportunities and their impact on shareholder value. Accordingly, these major institutions want assurance that companies they invest in are fully aware of the risks and have effective management systems to deal with them.

The Association of British Insurers has responded to this pressure from its members by developing a set of guidelines, in the form of disclosures which institutions would expect to see included in the annual reports of listed companies. Specifically they refer to disclosures relating to Board responsibilities and to policies, procedures and verification. The guidelines refer to social, ethical and environmental matters (SEE) and do not use the term CSR.

The GUS disclosures are as follows:

(a) With regard to the Board

- The Board takes regular account of the significance of social, environmental and ethical matters to the businesses of the Company. The responsibility for such matters lies with the Company Secretary who ensures that they feature regularly on the Board agenda. He is supported in this work by a CSR Group which meets under his chairmanship and which draws on staff with relevant expertise from across all of the Group's businesses. It includes experts in communication, internal audit, community affairs, consumer rights and environment. It is supported by external advisers.

- The section on internal control, which appears below, includes, inter alia, the Board's confirmation that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Group. This process includes the identification and assessment of the significant risks to the Company's short and long term value arising from SEE matters, as well as the opportunities to enhance value that may arise from an appropriate response. Further explanations appear on page 33.

- The Board receives adequate information to make this assessment and, in this context, reference should be made to the key procedures described below under internal control. Account is taken of SEE matters in any training programmes deemed appropriate on the appointment of new directors.

(b) With regard to policies, procedures and verification

- The Board has identified supply chain issues as an area of potential risk that might significantly affect the Company's short and long term value. GUS has significant buying power, giving it some degree of responsibility for the actions of the companies with which it deals. As GUS takes seriously its own social responsibility, it is only natural that it should want those over whom it has influence to do the same and, in so doing, guard against the risk to its reputation through a potential association with undesirable practices. To this end the Board has approved a set of seven principles that merchandise suppliers and business partners will be asked to endorse. These are set out in more detail in the separately published CSR Report.

- Practice to comply with these principles varies by division. In summary:

  – In Burberry, a programme is being developed as part of a new supplier manual. Burberry management has accepted the seven principles and suppliers are being asked to sign up. The programme is currently being extended to licensees. To monitor compliance, suppliers will be asked to complete a self assessment questionnaire, following which there will be a risk based approach to the identification of suppliers to be visited.

  – In Home Shopping all suppliers have signed up to a policy based on the seven principles. A workshop has been held for senior merchandisers and, to audit compliance, a pilot programme has been put in place with six suppliers using independent auditors.

  – Argos has accepted the seven principles and is including them within its terms and conditions. An audit programme is to be developed concentrating on direct import suppliers.

  – Reality is applying the seven principles in its supply chain, through its Purchasing Manager, who has undertaken to include them in contract terms and subsequently to audit suppliers.

- The Group Internal Audit Department's role is to ensure that adequate procedures are in place effectively to monitor compliance with the seven principles.

- The Company's policies and procedures for managing risks to short and long term value arising from SEE matters are as described below under 'Internal Control'.

- An important aspect of the Company's SEE procedures is that they should be subject to verification and this is reflected in the Group Internal Auditor's membership of the CSR Group. However, it is felt that shareholders would welcome some measure of external verification and the procedures for verification of SEE disclosures are focused on work undertaken by Acona, an independent consultancy practice. This involves a review which has four principal aspects:

  – The extent to which GUS has identified the CSR issues relevant to its business.

  – The adequacy of the policies and frameworks for managing these issues.

  – The comprehensiveness and robustness of the data collection and the completeness and accuracy of the data.

  – Evidence supporting the material claims in the report.

- Taking these points in turn, Acona has made the following disclosures in the separately published CSR Report:

  – GUS has a clear understanding of the CSR 'agenda' and the impact it has on the Group. In all businesses there is a recognition of the need to manage non-financial risks and opportunities, and the principal issues have been identified. We have made recommendations to the Group that this existing process of risk identification be formalised.

  – The policies and systems in GUS are developing fast, and are in some areas incomplete. However, there is a clear commitment within the Company to a structured and comprehensive approach. We have made recommendations on those areas where frameworks should be extended.

Corporate governance

– The CSR Report has data on the Group's environmental impacts, staff numbers, health and safety performance and the work of the GUS Charitable Trust and community programmes. All of the data comes from well-founded systems for recording and control. Data collection for the CSR Report has been audited by the GUS Internal Audit Department, who reviewed the processes for completeness and accuracy. Acona staff specified the scope of the review, have been closely involved in its execution, and have examined the findings in detail.

– The qualitative aspects of the CSR Report have been reviewed via an extensive series of meetings and interviews with GUS staff across the Group. There has been a process of management review and sign-off within each business. We are confident that it is an accurate reflection of the status of CSR management in GUS plc.

Accountability and audit

It is a requirement of the Code that the Board should present a balanced and understandable assessment of the Company's position and prospects. In this context, reference should be made to the Statement of Directors' Responsibilities on page 23, which includes a statement in compliance with the Code regarding the Group's status as a going concern, and to the Report of the Auditors on page 34, which includes a statement by the auditors about their reporting responsibilities.

The Board recognises that its responsibility to present a balanced and understandable assessment extends to interim and other price sensitive public reports and reports to regulators as well as information required to be presented by law.

Internal control

The Board acknowledges that it is responsible for the Group's system of internal control and for reviewing its effectiveness. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can provide reasonable, but not absolute, assurance against material mis-statement or loss. The Board has reviewed the effectiveness of the key procedures which have been established to provide internal control.

Following publication of guidance for directors on internal control (The Turnbull Guidance) the Board confirms that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Group. These include those relating to social, environmental and ethical matters. This process was in place throughout the year under review and up to the date of approval of the Annual Report. The process is regularly reviewed by the Audit Committee which reports its findings for consideration by the Board and is in accordance with The Turnbull Guidance.

The key procedures, which operated throughout the year, are as follows:

- Risk assessment:
  - The Group clearly sets out its objectives as part of its medium term planning process. These objectives are then incorporated as part of the budgeting and planning cycle and are supported by the use of both financial and non-financial key performance indicators.
  - The operating divisions are required to make presentations on risk to the Audit Committee which reports regularly to the Group Board on the risks facing the businesses.
  - The detailed assessment of strategic risks is delegated to the Group Chief Executive. This review is carried out as part of the annual budgeting and the monthly reporting and re-forecasting cycles.
  - The Audit Committee has delegated responsibility for considering operational, financial and compliance risks on a regular basis and receives reports on the controls over these risks biannually. This includes risks arising from social, environmental and ethical matters.
- Control environment and control activities:
  - The Group consists of a number of major trading divisions each with its own management and control structures.
  - The Group has established procedures for delegated authority which ensure that decisions that are significant, either because of the value or the impact on other parts of the Group, are taken at an appropriate level.
  - The Group has implemented appropriate strategies to deal with each significant risk that has been identified. These strategies include not only internal controls but other approaches such as insurance, joint ventures and specialised treasury instruments.
  - The divisions operate within a framework of policies and procedures laid down in organisation and authority manuals, and personnel are required to comply with these procedures. Policies and procedures cover key issues such as authorisation levels, segregation of duties, compliance with legislation and physical and data security.
- Information and communication:
  - The Group has a comprehensive system of budgetary control including monthly performance reviews for each major business and division. These reviews are at a detailed level within the trading divisions and at a high level for the Group Board.
  - On a monthly basis, the achievement of business objectives, both financial and non-financial, is assessed using a range of key performance indicators. These indicators are reviewed to ensure that they remain relevant and reliable.
  - There are clear procedures in the major trading divisions for employees to report suspected improprieties.
- Monitoring:
  - A range of procedures is used to monitor the effective application of internal control in the Group including control self-assessment, management confirmation of compliance with standards and internal audit reviews.
  - The Internal Audit Department's responsibilities include reporting to the Audit Committee on the effectiveness of internal control systems focusing on those areas of greatest financial risk to the Group.
  - Follow-up procedures ensure there is an appropriate response to changes in risks and controls.