

# Corporate governance report

## Combined Code

The Board has prepared this report with reference to the UK Combined Code of Corporate Governance issued by the Financial Reporting Council as revised in June 2006.

Throughout 2008/09 the Group has complied with the provisions set out in Section 1 of the Combined Code and applied its principles, except in the following areas:

Combined Code provisions	Status	Explanation
<b>A.3.2</b> – at least half the Board, excluding the Chairman, comprise independent Non-Executive Directors.	At the beginning of the year there was one more Executive Director than Non-Executive Directors.	With the retirements of Sir Ken Morrison and Roger Owen in the past year plus the recruitment of Philip Cox as a Non-Executive Director in April 2009, the Board will comprise of a majority of independent Non-Executive Directors.
<b>C.3.1</b> – at least one member of the Audit Committee has recent relevant financial experience.	During the year the Audit Committee did not have a member with recent relevant financial experience.	It is intended that Philip Cox will, after a period of induction, chair the Audit Committee. He has recent and relevant financial experience.
<b>C.3.4</b> – there are arrangements in place for the staff to raise concerns in confidence.	Comprehensive whistle-blowing procedures did not exist throughout the period.	Whistle-blowing procedures were enhanced after the start of the year in February 2008.

## The Board

### a) Membership

On 1 February 2009, the Board comprised of a Non-Executive Chairman, four Executive Directors and four Non-Executive Directors. On 13 March 2008, Sir Ken Morrison retired as Chairman and Director of the Company. Sir Ian Gibson, previously Deputy Chairman was appointed Non-Executive Chairman on this date.

There is a clear division of responsibilities between the Non-Executive Chairman and the Chief Executive (CEO), which has been set out in writing and agreed by the Board.

On 1 February 2009, Roger Owen retired as a Director and on 1 April 2009, Philip Cox will join the Group as a Non-Executive Director. With these changes, the majority of the Board will consist of Non-Executive independent Directors. Details of appointments, roles and backgrounds of the Directors are set out on page 28.

### b) Performance evaluation

The performance of the Board, its committees and its Directors is assessed and appraised throughout the year. The Chairman is responsible for the monitoring of the performance of the Executive Directors. In January 2009, the Chairman conducted an evaluation, without external assistance, of the performance of the Board and the results were shared with the other Directors. The Board was satisfied with its performance and it agreed to act on those areas for which it believed improved processes could be implemented.

### c) Senior Independent Director

Paul Manduca, the Senior Independent Director (SID) is available to shareholders as an alternative to the Chairman, CEO and the Group Finance Director. The SID ensures that he is available to meet shareholders during the year and reports any relevant findings to the Board or Chairman.

### d) Non-Executive Directors

The Non-Executive Directors provide a varied range of skills and experience to the Group. The Board is satisfied that all Non-Executive Directors, including the Non-Executive Chairman remain independent according to the definition contained in the Combined Code. No Non-Executive Director:

- has previously been employed by the Group within the last five years;
- has had a material business relationship with the Group within the last three years;
- receives remuneration other than Director's fees;
- has close family ties with any of the Group's advisors, 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.

All Non-Executive Directors are provided with a comprehensive, formal and tailored induction to the business. The minimum time commitment expected of the Non-Executive Directors is one day per month attendance at meetings, together with attendance at the Annual General Meeting, Board away days and site visits, plus adequate preparation time. The Board is satisfied that each of the Non-Executive Directors commits sufficient time to the business of the Group and contributes to the governance and operations of the Group.

### e) Board responsibilities

The Board is responsible for setting and approving the strategy and key policies of the Group, and for monitoring the progress towards achieving these objectives. It monitors financial performance, critical operational issues and risks. The Board also approves all circulars, listing particulars, resolutions and correspondence to the shareholders including the Annual report, half yearly financial report and interim management statements. The formal schedule of matters reserved for the Board remains unaltered and further details are available in the Investor Relations section of the Group's website [www.morrisons.co.uk](http://www.morrisons.co.uk)

### Operating boards

The Board delegates the operational responsibility to the following three main bodies, with the CEO and the Group Finance Director being members of each:

#### a) Executive Board

The Executive Board comprises four Executive Directors who oversee the day-to-day direction of the retail business. The Executive Board meets frequently through the year. Examples of the matters brought to the Executive Board include store and product performance, brand management, food safety, marketing initiatives and the Group's corporate social responsibilities.

#### b) Property Board

The Property Board consists of three Executive Directors and meets monthly. This Board has oversight of the strategic development and operational management of the Group's property. Matters brought to this Board include development of new stores and facilities, refurbishments and extensions.

#### c) Manufacturing & Distribution Board

The Manufacturing & Distribution Board comprises two Executive Directors, the Manufacturing Director and the Distribution Director plus one other senior executive. This body meets monthly and considers the strategic development of the Group's manufacturing and distribution functions.

### Committees of the Board

The principal committees of the Board are the Audit, Remuneration and Nomination Committees.

Name	Committee membership		
	Nomination	Audit	Remuneration
Marc Bolland	X		
Brian Flanagan	X	X	X
Sir Ian Gibson	X		X
Paul Manduca	X	X	X
Susan Murray	X	X	X
Nigel Robertson	X	X	X

The Directors attended the following numbers of Board and Committee meetings:

	Board	Nomination	Audit	Remuneration
Number of meetings	12	1	6	8
Marc Bolland	12/12	1/1		
Brian Flanagan	12/12	1/1	6/6	8/8
Sir Ian Gibson	12/12	1/1		8/8
Mark Gunter	11/12			
Martyn Jones	12/12			
Paul Manduca	12/12	1/1	6/6	7/8
Sir Ken Morrison	3/3			
Susan Murray	12/12	1/1	6/6	8/8
Roger Owen	11/12			
Richard Pennycook	12/12			
Nigel Robertson	11/12	1/1	5/6	8/8

The Company Secretary organises the appropriate level of insurance cover for Directors to defend themselves against legal claims and civil actions. The level of cover is currently £60m aggregate.

Full terms of reference of the Committees are available on request and on the Group's website [www.morrisons.co.uk](http://www.morrisons.co.uk)

#### a) Nomination Committee

During the year, the activities of the Committee were focused on recruiting a Non-Executive Director with recent and relevant financial experience.

The project culminated in the appointment of Philip Cox, who will take up his position as a Non-Executive Director with effect from 1 April 2009.

The Committee employed executive search agency, MWM Consulting to identify candidates who were then interviewed by members of the Committee. Meetings also took place with other Executive Directors as appropriate. Following this process, the Nomination Committee recommended the appointment of Philip Cox to the Board on 19 February 2009.

#### b) Remuneration Committee

The objective of the Group's remuneration policy is to encourage a strong performance culture and emphasise long term shareholder value creation. The intention is to position remuneration arrangements competitively against the market, with a clear reward structure to enable the Group to attract, retain and motivate the best talent, who are key to the Group's recent and future success.

The Human Resources Director has advised the Group on all remuneration related matters, including pensions and Executive Directors' contracts. Where necessary, this advice was supplemented by external advisors.

The Committee also receives advice from its appointed advisors Hewitt New Bridge Street on remuneration matters, Jardine Lloyd Thompson in respect of pensions, and Ashursts in respect of Executive Directors' contracts.

## Corporate governance report continued

### c) Audit Committee

The Board has delegated to the Audit Committee the responsibility for reviewing on its behalf:

- the integrity of financial reports;
- the effectiveness of the Group's internal control and risk management system; and
- the independence of the external auditors.

The Audit Committee's responsibilities have not changed during the year.

The Audit Committee regularly considers the professional development needs of its members, and whether adequate technical information is being provided. Where necessary, it will seek independent external advice at the Group's expense, with such arrangements made through the Company Secretary. Whilst the Audit Committee was short of a member with recent and relevant financial experience, the Company Secretary had retained, at the request of the Audit Committee Chairman, the services of PricewaterhouseCoopers LLP to advise the Audit Committee at relevant times during the year.

There has been no change in the composition of the Audit Committee during the year and the roles of the members also remained unchanged. It is intended that Philip Cox will chair the Audit Committee after an appropriate period of induction. The Chairman, the CEO, the Group Finance Director, the Head of Risk and Internal Audit and other finance department representatives have attended meetings by invitation.

### ii) Overview of actions taken by the Audit Committee in discharging its duties

The Committee has received and reviewed reports and presentations from senior management to fulfil its terms of reference. To meet its responsibilities in this respect, the Committee considered:

- interim and preliminary announcements, together with any other formal announcements relating to financial performance;
- the accounting principles, policies and procedures adopted in the Group's financial statements including, where necessary, challenging the judgements made; and
- the potential effects of tax and pensions accounting and other significant judgemental and complex accounting issues dealt within the financial statements.

The Audit Committee oversees the Group's relationship with the external auditors. Private meetings are held with the external auditors, without management present. The purpose of these meetings is to understand their views on the control and governance environment and management's effectiveness within it. To fulfil its responsibilities in respect of the independence and effectiveness of the external auditors, the Committee reviewed:

- the terms, areas of responsibility, duties and scope of the external auditors as set out in the engagement letter;

- the external auditors work plan for the Group and its subsidiaries;
- the detailed findings of the audit, including a discussion of any major issues that arose during the audit;
- the letter from KPMG Audit Plc confirming its independence and objectivity; and
- the audit fee and the extent of non-audit services provided by the external auditors.

In this period the external auditors have provided a significant level of non-audit work, primarily to provide the Board with independent assurance in respect of the IT systems replacement. The Board believes that this activity is a reasonable extension of their statutory audit work and that there are safeguards in place to avoid a threat to their independence or objectivity. The Board has a policy on the engagement of the external auditors to supply non-audit services and the Committee has reviewed the scope of non-audit services provided by the external auditors to ensure that there was no impairment of objectivity.

### ii) Internal control

The Board is responsible for setting a system of internal controls for the Group and reviewing its effectiveness. The control system is intended to manage rather than eliminate the risk of not meeting the Group's strategic objectives, whilst recognising that certain inherent risks may be outside the Group's control. Any system of internal control can only seek to provide reasonable, not absolute, assurance against material misstatement or loss.

The Board delegates to the Audit Committee the review of the effectiveness of the Group's internal controls and risk management systems. During the year, the Committee discharged this responsibility by:

- receiving and considering regular reports from the internal audit function on the status of internal control and risk management systems across the Group. The Committee also reviewed the department's findings, annual plan and the resources available to it to perform its work;
- reviewing the external auditor's management letters on internal financial control;
- seeking reports from senior management on the effectiveness of the management of key risk areas; and
- monitoring the adequacy and timeliness of management's response to identified audit issues.

During the year, a Group-wide process for identifying, evaluating and managing the significant risks faced by the business was initiated. This process consisted of various workshops, facilitated by the Head of Risk and Internal Audit, designed to identify formally and document the key risks faced by various business operations in achieving their business objectives. Risks identified as part of this process are evaluated based on the likelihood and potential impact of each risk and where necessary, actions to mitigate the risks were also identified.



In order to further strengthen the internal control environment, the Group introduced whistle-blowing procedures in February 2008 in order to enable colleagues to raise concerns about possible malpractice or wrongdoing. The Audit Committee receives regular reports from the Head of Risk and Internal Audit on any whistle-blowing activity. Whilst there were no significant concerns raised by colleagues, all actions required were discussed and agreed with the Committee.

The Board is satisfied that a continual process for identifying, evaluating and managing significant risks has been in place for the financial year and up to the date of this Annual report. To date, no material financial problems have been identified that would affect the results reported in these financial statements. The Board confirms that if significant weaknesses had been identified during this review the Board would have taken the necessary steps to remedy them.

**Shareholder relations**

The Chief Executive and the Group Finance Director meet regularly with analysts and institutional shareholders. The Investor Relations Director also maintains a programme of work that reports to the Board the requirements and information needs of institutional and major investors. This is part of the regular contact that the Group maintains with its institutional shareholders. All Directors, Executive and Non-Executive, attend the AGM. The Chairs of the Audit, Nomination and Remuneration Committees are available to answer any questions. Additionally, the Group's brokers sought independent feedback from investors following the annual and interim results in 2008. This feedback was reported to the Board.

Performance review

Strategic review

Governance

Group financial statements

Company financial statements

Investor information