

CHAIRMAN'S PREAMBLE

Comply or explain – an effective board

The board spent a day recently debating the fact that many proxy votes were cast against it. They were mostly aimed at the remuneration policy (a very fashionable topic these days), the non-executive directors who have served 'too long' and, me, the chairman on numerous counts.

As the voting at the AGM itself was unanimously in favour of all resolutions, we would be safe ignoring these proxies, cast as they are, largely, by institutional investors and often by their compliance teams and not the fund managers themselves. Nevertheless they raise two issues: have we explained ourselves properly, and does anyone take any notice if we do? We explain ourselves thoroughly in our corporate governance report (page 17) but some are missed by looking too closely at the detail.

The first issue I will address here by going through the FINANCIAL REPORTING COUNCIL GUIDANCE ON BOARD EFFECTIVENESS (Hogg, 2011) line by line and explaining where we do and do not comply. I have used this summary document rather than the full Code as it was published 'to assist companies in applying the principles of the UK Corporate Governance Code'. The principles are the most important thing and we none of us want to get hung up on word interpretation. It may take some time but please read on.

The second issue will become apparent as time goes by.

We are charged with being effective and it is a right and proper responsibility. I will quote the Guidance in italics and say what we do afterwards:

The board's role is to provide entrepreneurial leadership of the company within a framework of prudent and effective controls which enables risk to be assessed and managed¹.

I prefer 'effective' to 'entrepreneurial'; nevertheless the board at Games Workshop sees this as its main responsibility. We comply.

An effective board develops and promotes its collective vision of the company's purpose, its culture, its values and the behaviours it wishes to promote in conducting its business.

In particular it: provides direction for management; demonstrates ethical leadership, displaying – and promoting throughout the company – behaviours consistent with the culture and values it has defined for the organisation²; creates a performance culture that drives value creation without exposing the company to excessive risk of value destruction; makes well-informed and high-quality decisions based on a clear line of sight into the business; creates the right framework for helping directors meet their statutory duties under the Companies Act 2006, and/or other relevant statutory and regulatory regimes; is accountable, particularly to those that provide the company's capital; and thinks carefully about its governance arrangements and embraces evaluation of their effectiveness.

We do all these and take every point very seriously. We comply. The line where some will disagree with us is this one: *creates a performance culture that drives value creation without exposing the company to excessive risk of value destruction³*. We do not have LTIPs or any bonus schemes for senior management. We do have payment schemes designed to encourage store managers to sell more, and we have a company wide scheme that allows all employees to share in profitable growth. It rewards ALL employees not just the chosen few. Both schemes are designed to enhance value. LTIPs and bonuses for senior staff are deemed to be necessary by some to encourage value creation, but more, to ensure longevity of staff and help with succession planning. These are not needed at Games Workshop⁴. Our executive directors both have around 20 years service with the company. Their likely replacements have been here a similar length of time (well over 10 years). And, yes, they will be internal appointments. In fact, we see 10 years as the running-in period. I suspect these schemes are needed in businesses that have an eternal merry-go-round of executives who appear and disappear with monotonous regularity. They are not needed at Games Workshop, and I trust they never will be. Furthermore I believe they are fundamentally self-serving and disastrously value destroying. Nothing leaves a sourer taste in the mouth than executives lining their own pockets and claiming it is for the long term good of the business before moving on to their next golden handshake clutching their golden parachute.

At Games Workshop we employ people with integrity. People with integrity always work as hard as they can and always for the good of the business.

¹ This sounds like a contradiction in terms, and, of course, it is. Entrepreneurial is an odd word to use. Most boards aren't and shouldn't be. Those that are need to be left to get on with it.

² We do this, and I bet we are one of the few who do it properly.

³ Cute use of the word 'excessive'.

⁴ This isn't just theory as we tried it and it was counter productive.

Comply or explain – an effective board continued

An effective board should not necessarily be a comfortable place. Challenge, as well as teamwork, is an essential feature. Diversity in board composition is an important driver of a board's effectiveness, creating a breadth of perspective among directors, and breaking down a tendency towards 'group think'.

We believe we do comply with the intent of this paragraph, whilst acknowledging some may think we do not.

We fully agree that 'group think' is a bad thing. We fully agree that challenge is an essential ingredient in an effective board, as is teamwork. We do not agree that diversity for its own sake is the answer⁵. We believe that each director must be independent of mind. To imply that someone is not independent minded because of time served or sex or ethnicity or religion or whatever else is false.

Worse, it implies that 'diversity' adds value, allowing groups and sub-groups to be added to an eternally growing list until the whole thing is reduced *ad absurdum*.

I recently received a letter congratulating the board on recruiting a woman as NED, to address our diversity issues. How sexist is that? It is not our board that is suffering from 'group think'.

Only independence of mind counts. There are no proxies, no quotas that get around it. Rubbish directors are rubbish directors. The fact that they allow boxes to be ticked on arcane lists doesn't make them effective. Good, independent minded directors are as hens' teeth, gold dust. We have six. Including me.

One thing Hogg makes very clear is: *Ultimately it is for individual boards to decide on the governance arrangements most appropriate to their circumstances, and interpret the Code and guidance accordingly*. Institutions should take this more seriously. Their one-size-fits-all compliance regime is becoming antithetical to the whole process, and risks bringing their industry into disrepute.

Games Workshop – the IP play

Over the years we have been exhorted by some to develop our revenue stream by 'leveraging' our IP. Using our great imagery we could do all sorts of lucrative and exciting value-enhancing (i.e. take private and re-float) deals. Actually, what they really mean is: do a movie!

We have never NOT done licensing deals, as you can see from the steady stream of royalties we earn; it's just that we believe we must do them on our terms and not prostitute the business to any and every deal that comes along. If we do a movie (along with the concomitant abandonment of the toy rights⁶) it will be on terms that do not compromise our business. It isn't likely.

Long term owners will notice a big increase in royalty income this year. Have we sold out at last? No, it's just that working closely with the myriad app developers, and being more precise with the terms we offer, we have increased the number of 'computer'⁷ games in the market.

Tom Kirby

Non-executive chairman
25 July 2016

⁵ 'Diversity' is becoming a group think word itself. The cure for all our ills! Nirvana!

⁶ Anyone doubting this aspect of movies needs to read how Marvel prevented an Iron Man movie having a female as the main baddie because it would hurt the toy sales.

⁷ This covers phone, tablet, PC and console. We have products on all these platforms.