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Corporate Subsidiary Governance: Leading Edge Practices

Insights from David Allgood, Chief Legal Officer, Royal Bank of Canada

Parent-subsidiary relationships and corporate governance are top-of-mind topics these days for CLOs, and Royal Bank of Canada is implementing leading edge measures that promote best practices in governance for its subsidiaries. A core feature of the company's subsidiary governance practices is its Subsidiary Governance Office (SGO)—a centralized professional corporate secretarial function for the company's nearly 350 subsidiaries. In addition, the company has created a Subsidiary Governance and Oversight Committee chaired by the Subsidiary Governance Officer and comprised of professionals from the multi-disciplinary functions throughout the company to help ensure consistency and coordination in practices and policies relating to subsidiary governance. In this CLO Perspective, David Allgood, Executive Vice President and General Counsel for Royal Bank of Canada, shares his insights on the background and process for creating the SGO, and its composition, mission, function and accomplishments.

Getting Started: Subsidiary Governance Review

Royal Bank of Canada's SGO was created in 2001 following an internal study on how to enhance subsidiary governance. "Prior to undertaking this study, the company had many hundreds of subsidiaries with various dispersed corporate secretaries and individuals performing corporate secretarial functions. In addition, with so many subsidiaries and no formal centralized processes to track and administer information relating to them, preparing a definitive list of subsidiaries with a high degree of confidence was a real challenge. Our new SGO and associated subsidiary governance practices have greatly enhanced our capabilities in this area and have allowed the company to implement best practices in subsidiary governance and managing subsidiary life cycles," explains Allgood.

The six-month study was performed under Allgood's supervision and included a review of legal corporate governance of entities within the company's subsidiary network (which at the time estimated to be 500 in number) as well as a best practices review of subsidiary governance performance of major financial institutions in the United States and United Kingdom, and survey data from leading Canadian corporations. Key findings and recommendations were presented to the Board; among them was the creation of the SGO.

Creating a Subsidiary Governance Office

Asked for thoughts on steps that he considers important in creating a SGO, Allgood lists the following:

>> Appoint a Subsidiary Governance Officer

Royal Bank of Canada's subsidiary corporate governance review identified as a recommended best practice having a professional whose exclusive role is focusing on subsidiary governance. Accordingly, as one of the first steps in creating the SGO, a Subsidiary Governance Officer was appointed to lead the SGO and focus full-time on subsidiary governance issues for the company. The Subsidiary Governance Officer is a lawyer by background and reports organizationally to the company's Corporate Secretary, who in turn reports to Allgood as CLO.

>> Staff the SGO with competent professionals skilled in the corporate secretarial function

In addition to the Subsidiary Governance Officer, the SGO consists of around 19 professionals (including lawyers, paralegals and professional corporate secretaries), who are dedicated full-time to performing corporate secretarial and subsidiary governance responsibilities. Most of the SGO professionals are located at the company's headquarters in Toronto. In addition, SGO professionals are located in Mississauga, London, Guernsey, New York, Delaware and the Bahamas. In addition to the SGO, there are several professionals throughout the organization who act as corporate secretary of various subsidiaries.

>> Identify the company's full portfolio of subsidiaries

This can be a remarkably difficult task—especially for a company with around 500 subsidiaries when the SGO was first created—but is a necessary and critical early step in the overall process of enhancing subsidiary governance

>> Select a software program to help manage subsidiary information

With the universe of subsidiaries defined, having a reliable and centralized method for maintaining, tracking and accessing information is important for ongoing administrative efficiencies and internal controls. Royal Bank of Canada evaluated a number of software product offerings before ultimately selecting the technology that it now uses. Global Corporate Manager is licensed from Datacare Software Group and this database is managed by the SGO and used to store and manage corporate data on all RBC subsidiaries.

Subsidiary Governance Office: Mission and Key Roles

Allgood shares that the SGO's mission includes: promoting best practices in corporate governance in RBC subsidiaries; creating a centre of excellence for subsidiary governance; and maintaining appropriate enterprise-wide subsidiary corporate governance policies. More specifically, the SGO is on point for providing corporate secretarial support, subsidiary governance and life-cycle management for the company's subsidiaries that are wholly-owned or company-controlled (e.g., where the company controls more than 50% of the shares/voting power or has de facto control of the entity). In addition, the SGO plays an important role in affecting active integration of subsidiaries added through strategic acquisitions and alliances.

Royal Bank of Canada's Statement of Corporate Governance Practices and Principles (Governance Statement) describes the SGO as promoting "consistency, simplicity, and transparency in the organizational structure of the bank and its subsidiaries." The company's Governance Statement may be accessed via the following link: <http://www.rbc.com/governance/pdf/ScheduleB.pdf>.

Following are highlights of SGO roles relating to subsidiary governance and life-cycle management.

>> SGO Promotes Corporate Governance of RBC Subsidiaries

The SGO has developed and issued a policy on corporate governance for RBC subsidiaries. Allgood explains, "the vast majority of directors for the company's wholly-owned and controlled subsidiaries are employees of the company. Accordingly, the SGO developed and issued a policy document/manual to help guide them in their roles as directors for subsidiary operations and to enhance consistency in governance of subsidiaries across the RBC enterprise." The policy was approved by RBC's Corporate Secretary and Allgood, and is reviewed annually as part of ongoing continuous improvement initiatives.

Key components of the policy include provisions relating to: Corporate Secretary (appointing, role, qualifications & mandate); directors (appointing, indemnification & insurance, orientation, liabilities and compensation); board of directors (guiding principles, role & responsibilities, structure and composition, delegation); board procedures (meetings, materials, minutes, conflicts of interest, resolutions and shareholders' meetings); 'mind and management' (tax principles); insider reporting; and safekeeping of corporate documents.

>> SGO Evaluates and Manages Subsidiary Life Cycles

"Managing the life cycles of subsidiaries comprises a large part of the SGO's function. A key operating principle for the SGO in managing these life cycles is to ensure that the subsidiary is absolutely necessary. An additional principle is to limit the unnecessary proliferation of subsidiaries," explains Allgood. Accordingly, the SGO has issued a policy and implements procedures and practices relating to subsidiary life cycle management. Key sections of the policy

include: creating a new subsidiary; naming a subsidiary; reorganizations and acquisitions; and terminating subsidiaries.

- **Creating New Subsidiaries:** A new subsidiary may only be created upon recommendation by the SGO and approval of Allgood. Once past this threshold, subsidiary creation must be approved pursuant to other company policies. Allgood shares that, fundamentally, there must be a compelling legal, regulatory or substantive tax reason in order to justify creating a new subsidiary. The SGO policy includes process requirements for incorporation and requires review by the company's legal department.
- **Evaluating Ongoing Needs:** "Keeping inactive subsidiaries isn't costless. There are fees and costs associated with keeping the subsidiary in good standing and administering and sustaining the subsidiary. Accordingly, we continually review the need for each subsidiary," says Allgood. Since the SGO has been created, the company has dissolved around 250 subsidiaries. Allgood states that RBC uses \$40,000 as the estimated internal and opportunity cost per year to maintain an inactive subsidiary.
- **Terminating Subsidiaries:** The SGO's life cycle management policy includes trigger criteria for subsidiary dissolutions, as well as required processes for dissolving a subsidiary. The company's law department, SGO, tax group and project analysis decision support division play key roles, and information on the subsidiary is tracked and archived as appropriate.

Subsidiary Governance & Oversight Committee

In addition to leading the SGO, the Subsidiary Governance Officer organizes and chairs the company's Subsidiary Governance & Oversight Committee. The committee meets four times per year and includes functional representatives from finance, group risk management, compliance, law, tax, internal audit, and treasurers. The committee facilitates coordination of activities and information relating to the company's subsidiaries among functional units, and provides a forum for collaboration among the functions to help ensure appropriate oversight of subsidiary governance.

Closing CLO Insights

"Our company's subsidiary governance practices provide efficiencies and enhanced governance practices across our entire enterprise. They've enabled us to systematically evaluate subsidiary life cycles and dissolve hundreds of subsidiaries for which there was no longer a compelling need at a real cost savings to the company. The business case for creating a SGO is straightforward: it contributes to good governance, process efficiencies, and can accomplish cost and resource savings," says Allgood. An additional benefit of having a SGO: once a SGO is established, synergies can present themselves through the online system as the repository for transfer pricing agreements, legal entity financial statements and legal entity regulatory filings.