Financial Reporting Council
8th Floor
125 London Wall
London EC2Y 5AS

By email: codereview@frc.org.uk

13th September 2023

Dear Sir / Madam,

FRC Corporate Governance Code Consultation: USS response

The Universities Superannuation Scheme (USS) welcomes the opportunity to respond to the Financial Reporting Council's consultation on the Corporate Governance Code.

About USS

Universities Superannuation Scheme (USS) was established in 1974 as the principal pension scheme for universities and higher education institutions in the UK. We work with around 330 employers to help build a secure financial future for 528,000 members and their families. We are one of the largest pension schemes in the UK, with total assets of around £75.5bn (at 31 March 2023). The trustee of USS is Universities Superannuation Scheme Limited (USSL). It has overall responsibility for scheme management and administration. The trustee is regulated by The Pensions Regulator and has a legal duty to ensure that benefits promised to members are paid in full on a timely basis.

The trustee delegates implementation of its investment strategy to a wholly-owned subsidiary – USS Investment Management Limited (USSIM) – which provides in-house investment management and advisory services to the trustee. USSIM manages 70% of the investments in-house and appoints and oversees external investment managers to manage the rest. USSIM is authorised and regulated by the Financial Conduct Authority. USS is a hybrid pension scheme, which means we have both a defined benefit (DB) part – the Retirement Income Builder – and a defined contribution (DC) part – the Investment Builder.

Consultation response

Whilst we do look to the FRC Corporate Governance Code for good practice guidance and consider this in the way that we run our own companies (USSL and USSIM), neither of these companies are listed entities subject to the Corporate Governance Code. However, as a responsible investor and universal owner looking to invest the pension scheme assets over the long-term, we believe that well run companies that have robust governance structures and processes in place lead to better long-term returns for their shareholders. As such, our voting policies and approach to investment reflect the

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Corporate Governance Code and our response to this consultation is primarily driven by our position as a universal asset owner.

We have provided our views below on the key focus areas of the consultation on which we believe improvements could be made and/or we have specific views which may be useful in your deliberations. Please note also that we have collaborated with Railpen on these issues and are supportive of their overall comments. Our response below highlights the particular areas that USS is supportive of or can see areas for potential improvement. Further detailed responses to the consultation questions are set out in the table on pages 3-8.

Workforce and fair pay issues

Evidence shows that human capital is a material issue for nearly every company in every sector and it is particularly vital that company executives hear the voice of the wider workforce. We were therefore particularly supportive of the changes in the 2018 update to the Code, which emphasised the importance of effective workforce engagement mechanisms.

Strengthening Provision 5 (workforce engagement mechanisms): We note the findings from the 2021 FRC, the Involvement and Participation Association (IPA) and Royal Holloway report on Workforce Engagement and the *UK Corporate Governance Code: A Review of Company Reporting and Practice* that workforce directors in particular are relatively rarely utilised as a workforce engagement mechanism across the FTSE 350. Although a recent guidance document[1] launched in 2023 by Railpen with the support of USS and other asset owners and managers, notes that workforce directors will not be suitable for every company, we would like the Code to further encourage companies to genuinely consider whether a workforce director might be the right approach for them. We think the potential business advantages of such a model (aiding the 1.5 degree transition, reputational protection on fair pay and working conditions, increased talent attraction and retention) are worth adding more weight to the issue of workforce engagement mechanisms. Therefore, please consider the addition of the following wording in Provision 5:

"Regardless of the arrangement chosen, the board should provide a high-level summary as to what assessment they had made of the effectiveness of each of the three engagement methods explicitly mentioned in the Code, and why it reached the conclusion that the others would not be as effective. If the board has not chosen one or more of these methods, it should explain what alternative arrangements are in place and why it considers that they are effective."

Further detailed responses to the consultation questions are set out in the table on the following pages. Please feel free to contact us should you require any clarification or additional information on our comments.

Sincerely yours

[redacted]

[1] Workforce inclusion and voice: investor guidance on workforce directors (April 2023).

FRC Corporate Governance Code Consultation – Request for Comments September 2023: USS Response

Section / subtopic	Question number	Question / topic	USS response and commentary
1: Board leadership and company purpose			
	1	Do you agree that the changes to Principle D in Section 1 of the Code will deliver more outcomes-based reporting?	We agree with change and believe it will deliver more outcomes-based reporting.
	2	Do you think the board should report on the company's climate ambitions and transition planning, in the context of its strategy, as well as the surrounding governance?	Yes, but only where it is material to the company. The company should also report upon any concerns regarding physical risks arising from climate change and how the company is addressing these. It should also report other material/critical environmental/social risks, including the "just transition" where applicable.
	3	Do you have any comments on the other changes proposed to Section 1?	Provision 3. We see this as a positive change from "seek engagement" to "engage", with more emphasis on the doing rather than just attempting to. Provision 6. We would prefer the board to report on the number and type of incidences raised, actioned and closed, with a breakdown of the results and lessons learnt.
2: Division of responsibilities			
	4	Do you agree with the proposed change to Code Principle K (in Section 3 of the Code), which makes the issue of significant external commitments an explicit part of board performance reviews?	USS agrees with the changes, in particular the commitment to other organisations and ability to discharge responsibilities.
	5	Do you agree with the proposed change to Code Provision 15, which is designed to encourage greater transparency on directors' commitments to other organisations?	We acknowledge the constructive change here, and the proposal to improve transparency on the ability of the directors to undertake their role for the company should be encouraged.
3: Composition, succession and evaluation			
Diversity & inclusion	6	Do you consider that the proposals outlined effectively strengthen and support existing regulations in this area, without introducing duplication?	There seems to be some ambiguity between Principle K, which removes the reference "to achieve objectives" and the third bullet point in Provision 24 referring to "progress towards company objectives".

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			We would recommend that Provision 24 be revised to reflect the wording in Principle K.
Diversity & inclusion	7	Do you support the changes to Principle I moving away from a list of diversity characteristics to the proposed approach which aims to capture wider characteristics of diversity?	We acknowledge the constructive change in language here, but we would recommend that the legal definition of protected characteristics be included.
Diversity & inclusion	8	Do you support the changes to Provision 24 and do they offer a transparent approach to reporting on succession planning and senior appointments?	USS is in general agreement but please note the contradiction highlighted in the response to question 6.
Board performance reviews	9	Do you support the proposed adoption of the CGI recommendations as set out above, and are there particular areas you would like to see covered in guidance in addition to those set out by CGI?	We support the implementation of the CGI's recommendations on board performance reviews. We would also recommend, if not covered, any actions undertaken by the company as a result of the review, with a rationale behind such actions.
4: Audit, risk and internal control			
Audit and Assurance Policy	10	Do you agree that all Code companies should prepare an Audit and Assurance Policy, on a 'comply or explain' basis?	Yes.
Audit Committees and External Audit: Minimum Standard	11	Do you agree that amending Provisions 25 and 26 and referring Code companies to the Minimum Standard for Audit Committees is an effective way of removing duplication?	We offer no view in response to this question.
Sustainability reporting	12	Do you agree that the remit of audit committees should be expanded to include narrative reporting, including sustainability reporting, and where appropriate ESG metrics, where such matters are not reserved for the board?	Yes, although we would propose that there be an initial period of transition whilst the companies build the necessary skills within the audit committee. Also, the reporting should reflect the **material** ESG issues.
Risk management and internal controls	13	Do you agree that the proposed amendments to the Code strike the right balance in terms of strengthening risk management and internal controls systems in a proportionate way?	We offer no view in response to this question.

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Risk management and internal controls	14	Should the board's declaration be based on continuous monitoring throughout the reporting period up to the date of the annual report, or should it be based on the date of the balance sheet?	We offer no view in response to this question.
Risk management and internal controls	15	Where controls are referenced in the Code, should 'financial' be changed to 'reporting' to capture controls on narrative as well as financial reporting, or should reporting be limited to controls over financial reporting?	We believe that, as a minimum, internal controls should address climate accounting where material to the company.
Risk management and internal controls	16	To what extent should the guidance set out examples of methodologies or frameworks for the review of the effectiveness of risk management and internal controls systems?	Companies should be free to select the methodology or framework that are best suited to the company. Although the company should clearly explain why the stated methodology and/or framework has been used.
Risk management and internal controls	17	Do you have any proposals regarding the definitional issues, e.g., what constitutes an effective risk management and internal controls system or a material weakness?	We offer no view in response to this question.
Risk management and internal controls	18	Are there any other areas in relation to risk management and internal controls which you would like to see covered in guidance?	We offer no view in response to this question.
Going concern	19	Do you agree that current Provision 30, which requires companies to state whether they are adopting a going concern basis of accounting, should be retained to keep this reporting together with reporting on prospects in the next Provision, and to achieve consistency across the Code for all companies (not just PIEs)?	We offer no view in response to this question.
Resilience Statement	20	Do you agree that all Code companies should continue to report on their future prospects?	We offer no view in response to this question.
Resilience Statement	21	Do you agree that the proposed revisions to the Code provide sufficient flexibility for non-PIE Code companies to report on their future prospects?	We offer no view in response to this question.
5: Remuneration			

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Changes to strengthen links to overall corporate performance	22	Do the proposed revisions strengthen the links between remuneration policy and corporate performance?	We agree there should be a link between the ***material*** E, S and G issues for the company and the long-term incentive plans for executives. There should be greater transparency on the make-up of the metrics, all-encompassing metrics should be avoided, or otherwise detailed and explained. Companies should therefore avoid statements akin to "see an improvement in environment/social/governance performance and/or scores/ratings" and provide the specific details of what is deemed to be an "improvement".
Malus and clawback	23	Do you agree that the proposed reporting changes around malus and clawback will result in an improvement in transparency?	Yes.
Changes to improve the quality of reporting	24	Do you agree with the proposed changes to Provisions 40 and 41?	Yes, we welcome the additional transparency on the reporting of the use of malus and clawback clauses over the previous five years.
Changes to improve the quality of reporting	25	Should the reference to pay gaps and pay ratios be removed, or strengthened?	The reference to pay gaps and pay rations should be strengthened and greater transparency provided. If not allowed for we recommend further transparency on the pay gaps across different levels within a company, as well any potential pay gaps related to ethnicity and gender.
6: Other matters			
Artificial intelligence	26	Are there any areas of the Code which you consider require amendment or additional guidance, in support of the Government's White Paper on artificial intelligence?	We offer no view in response to this question.
Workforce engagement		Workforce engagement and fair pay issues.	Evidence shows that human capital is a material issue for nearly every company in every sector and it is particularly vital that company executives hear the voice of the wider workforce. We were therefore particularly supportive of the changes in the 2018 update to the Code, which emphasised the importance of effective workforce engagement mechanisms. • We would recommend strengthening Provision 5

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			regarding workforce engagement mechanisms. We note the findings from the 2021 FRC, the Involvement and Participation Association (IPA) and Royal Holloway report on Workforce Engagement and the UK Corporate Governance Code: A Review of Company Reporting and Practice that workforce directors in particular are rarely utilised as a workforce engagement mechanism across the FTSE 350. Although a recent guidance document[2], launched in 2023 by Railpen with the support of USS and other asset owners and managers, notes that workforce directors will not be suitable for every company, we would like the Code to further encourage companies to genuinely consider whether a workforce director might be the right approach for them. We think the potential business advantages of such a model (aiding the 1.5 degree transition, reputational protection on fair pay and working conditions, increased talent attraction and retention) are worth adding more weight to the issue of workforce engagement mechanisms. Therefore, please consider the addition of the following wording in Provision 5: *"Regardless of the arrangement chosen, the board should provide a high-level summary as to what assessment they had made of the effectiveness of each of the three engagement methods explicitly mentioned in the Code, and why it reached the conclusion that the others would not be as effective. If the board has not chosen one or more of these methods, it should explain what alternative arrangements are in place and why it considers that they are effective."*
Shareholder rights		Dual-class share structures	We remain hopeful that the FCA will reconsider its proposal to roll

[2] Workforce inclusion and voice: investor guidance on workforce directors (April 2023).

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			back important shareholder rights around significant transactions, related party transactions and – most pertinently for this consultation – the 'one share, one vote' principle. However, should this go ahead, and in light of the importance of equal voting rights to the shareholder voice and companies fully complying with Principle C to "ensure effective engagement with, and encourage participation from, [shareholders and stakeholders]", we would suggest that Provision 3 be amended to explicitly include wording on how – where a dual-class share structure has been used – the board ensures it listens to and acts upon views expressed by shareholders. We would, therefore, suggest the following changes to Provision 3 (changes in italics): "The chair should ensure that the board has a clear understanding of the views of shareholders, and report in the annual report on the outcomes of the engagement which has taken place with them during the reporting period. *Where the company has decided to put in place dual-class share structures, it should report in the annual report what additional measures have been put in place to ensure the views of shareholders are listened to and acted upon, and its assessment of the effectiveness of such measures. This should include any relevant examples and outcomes."*