RYDER COURT, 14 RYDER STREET, LONDON, SW1Y6QB UK
T.44 (0) 20 7024 9000 WWW.KORNFERRY.COM

David Styles
Director, Corporate Governance and Stewardship
Financial Reporting Council
8th Floor
125 London Wall
London EC2Y 5AS

By email: codereview@frc.org.uk

13 September 2023

Dear David,

**Korn Ferry: Response to the FRC's consultation on the UK Corporate Governance Code**

Thank you for the opportunity to provide comments on the proposed changes to the Code.

**Introduction and general comments**

Korn Ferry works closely with the boards of many companies listed in the UK. In general, our clients are supportive of the Code and prefer corporate governance good practice being enshrined through its "comply or explain" approach rather than in legislation or regulation. The Code has been very influential in helping individual companies make improvements to their corporate governance.

In the context of market developments and new trends, ongoing evolution of the Code is critical and we are supportive of the FRC's overall approach in this regard. However, changes should be handled carefully as there is a view from some of our clients (and from companies more widely) that the UK's governance framework – encompassing the Code, Listing Rules, company law, investor and proxy advisor guidelines and expectations, etc – is in combination creating an environment which is increasingly burdensome and which is losing its appeal for some businesses.

Our general preference, therefore, is for Code changes to be kept to a minimum, with new requirements only introduced where necessary. We would also welcome further consideration from the FRC as to how investors and proxy advisors could be encouraged to take a more thoughtful approach to "comply or explain". There is still a widespread perception in some areas that explanations for deviations from the Code are disregarded in favour of a rigid expectation of Code compliance.

**Responses to individual questions**

We set out below our response to selected questions raised in the consultation document.

***Q4 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?***

This is certainly preferred to the alternative option of the Code stating a maximum number of directorships which can be held by any individual. Assessing other commitments within the framework of the board performance review allows for a consideration of all external commitments alongside a broader review of the individual's effectiveness on the board. Among other things this review should consider the individual's attendance record at board and committee meetings plus their wider contributions to the board and company.

It is also important that the review captures all other time commitments, not just roles on other PLC boards. The focus on PLC boards only is one of the drawbacks of the numerical approach adopted by proxy advisors and some investors to evaluate "overboarding".

***Q5 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 have no principled objection to additional reporting of this nature but there is a risk that disclosures will be based around general boilerplate statements about the board confirming that each director has sufficient time to undertake their role effectively. The FRC may need to provide some clear guidance on its specific expectations in order for this reporting to be meaningful and informative.

***Q6 Do you consider that the proposals outlined effectively strengthen and support existing regulations in this area, without introducing duplication?***

We welcome the fact that the proposed Code wording does not introduce detailed new provisions in this area but reiterates the importance of succession planning with an appropriate focus on diversity and inclusion.

***Q7 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?***

In general, yes. There are multiple aspects to board diversity and a focus on only one or two elements risks diverting attention from other relevant areas.

***Q8 Do you support the changes to Provision 24 and do they offer a transparent approach to reporting on succession planning and senior appointments?***

There are no fundamental concerns with the general thrust of these disclosure recommendations. However, companies can naturally be reluctant to detail specific succession plans in annual reports and there should be a recognition of the need for some confidentiality in this area.

***Q9 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 are supportive of the adoption of the CGI recommendations.

***Q22 Do the proposed revisions strengthen the links between remuneration policy and corporate performance?***

We have no comments on the proposed changes to the wording in new Principles O or Q.

With regards to Principle P, the reference to remuneration outcomes being aligned to the successful delivery of ESG objectives implies that to apply this Principle, a remuneration committee must include explicit ESG targets within incentive schemes. While ESG measures are in place at many companies, they are not universal and remuneration committees choose not to adopt them for various valid reasons. We recommend that the FRC clarifies (either in revised wording or in the supporting guidance to be issued alongside the revised Code) that Principle P does not mandate the inclusion of ESG targets in incentives.

***Q23 Do you agree that the proposed reporting changes around malus and clawback will result in an improvement in transparency?***

Many remuneration reports (particularly for Main Market companies) already include detail on malus and clawback, for example in respect of the "trigger events" which may lead these

provisions to be invoked, and the period over which the provisions apply. The proposed reporting changes in new Provision 40 require some extra detail to be disclosed but in most cases this will not lead to materially greater levels of information being provided. We query the necessity of requiring the remuneration report to include a five-year look-back on the use of malus and clawback provisions: requiring disclosure of use in the last reporting period should in our view be sufficient (with prior annual reports publicly available for those who want to look back).

We note the new wording in Provision 39 that “director contracts and/or other agreements or documents which cover director remuneration should include malus and clawback.” In our experience, it is standard for malus and clawback provisions to be included in detail in incentive scheme rules and directors’ remuneration policies (which are subject to shareholder approval) rather than necessarily in directors’ service contracts. In this regard the “and/or” reference in this provision is critical: it would perhaps be unnecessary to expect service contracts to be revised to add in these provisions. A key issue is the enforceability of malus and clawback provisions, which requires the wording in the incentive scheme rules and the directors’ remuneration policy to be aligned, and for companies to make executive directors (and others) aware of the existence of these provisions and their scope.

***Q24 Do you agree with the proposed changes to Provisions 40 and 41?***

The removal of current Provision 40 and the related reporting requirement in current Provision 41 is welcome. Although many companies have attempted to meet the spirit and the letter of the Code in reporting against the Provision 40 factors, the disclosures do not change significantly year on year, and there is limited evidence that investors find the information useful.

With regards to current Provision 41 (new Provision 43):

- In the first bullet, the same point is made as in the answer to Q22 above: the proposed wording has a clear implication that remuneration committees should adopt ESG targets in incentive schemes. The FRC’s position on this should be clarified.
- The simplification/deletion of other bullets in this Provision is welcome.

***Q25 Should the reference to pay gaps and pay ratios be removed, or strengthened?***

In the interests of simplifying reporting obligations and reducing the potential duplication with the legislative requirements on gender pay gap reporting and CEO pay ratio reporting, we support the proposed removal of this reference.

Yours sincerely,