Director, Corporate Governance and Stewardship
Financial Reporting Council
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13 September 2023

Dear Mr Styles

We welcome the opportunity to respond to the Financial Reporting Council's (FRC) consultation document on the UK Corporate Governance Code ("the Code").

About Royal London

Royal London is the largest mutual life insurance, pensions and investment company in the UK, with assets under management of over £150bn. We are a major investor in UK companies through our principally held investments as an asset owner (the Royal London Mutual Insurance Society – RLMIS) and through our asset manager, Royal London Asset Management (RLAM).

RLAM has an extensive stewardship engagement programme with companies held in our actively managed portfolios and funds and has published Stewardship reports every year since 2015. Our response is therefore written primarily from our perspective as an asset manager, and we believe we are well-placed to provide an informed view on the FRC's proposals for the revision of the Code.

Summary of our views

It is vital that changes to the Code enhance transparency and investor confidence whilst being proportionate so they do not result in overly onerous requirements that are costly to implement and maintain. The UK operates in a global environment and particular care should be taken to ensure any changes do not: reduce the attractiveness of the UK as a place to raise capital; damage its economic prospects; or adversely impact its ability to attract global talent.

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To that end, we have **significant reservations** that the proposed requirements over the new Board declaration on controls are **disproportionate**. There is a high risk that the proposals will be interpreted differently to the FRC's stated view that this is not a US Sarbanes-Oxley type approach given the similar deficiency disclosure and materiality requirements. This is exacerbated by widening the scope to incorporate non-financial reporting, which we consider to be too broad. As a major investor in UK companies, we are concerned that the increased costs of compliance relative to the perceived benefit will **impact on the UK's attractiveness** to current and future issuers and **negatively impact shareholder returns**.

Our concerns are compounded by the absence of a clear framework for the Board's declaration, or any related guidance. We are concerned that this will lead to a significant divergence in the approaches firms take to comply with the new requirement. **We cannot support this proposal without further guidance being issued that is subject to consultation**. We expect this to necessitate a longer or phased implementation period.

We support the intent of maintaining flexibility with a 'comply or explain' basis. However, if the additional requirements and associated guidance (once issued) result in obligations on firms that are not proportionate, we are concerned that **companies may elect to explain their non-compliance with elements of the Code**, rather than providing useful disclosure, thus undermining the FRC's desired outcomes. Dual reporting companies may choose to solely apply the US Sarbanes-Oxley framework, which again would not meet the FRC's desired outcomes for the Board to consider non-financial reporting controls. If the FRC insists on dual reporters following both regimes this will inevitably drive firms away from the UK, further impacting the attractiveness of the UK.

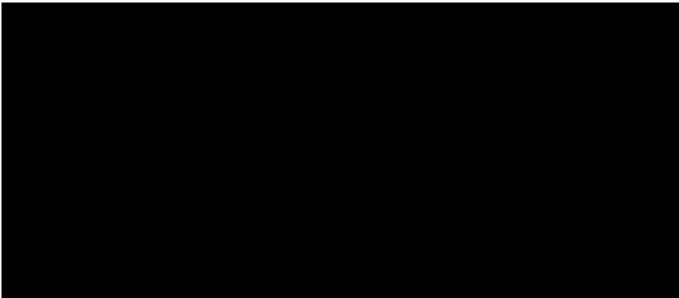
We acknowledge the aims of the FRC in broadening the scope to include non-financial reporting. The **scope of 'reporting' controls needs to be clearly defined in the guidance** and it should be sufficiently principles-based to allow organisations to define and explain their interpretations of this scope as part of their internal control declarations. The scope of the new requirements should be limited to the annual report and other published financial reporting. We do not believe the benefits of a more general broadening would outweigh the additional costs.

The declaration should be based at the date of the balance sheet. Extending it to the whole period would go further than US requirements and put the London market at a **competitive disadvantage**. Further extending it to the annual report date is **not practical**, would be inconsistent with other content in the annual report and result in duplication in subsequent periods.

With regards to the other elements of the Code, we are supportive of the overall direction of the proposals in sections 1-3 and 5 and our detailed responses to the consultation questions on these sections, as well as those on section 4, are provided in the appendix.

In summary, we support the need to update the Code to improve investor confidence, but we have significant reservations that the Board declaration on controls reforms could have far-reaching consequences for UK business. We believe further consultation on the associated guidance is vital to achieving a successful outcome. Given the guidance is not due to be issued until December 2023, we strongly believe a longer or phased implementation period is necessary.

I trust that these comments are useful, and I would be pleased to engage further on any aspect of our response if that would be helpful.



APPENDIX

Section 1 – Board leadership and company purpose

Q1: Do you agree that the changes to Principle D in Section 1 of the Code will deliver more outcomes-based reporting?

We are supportive of the changes proposed to Principle D and the focus on outcomes over process.

We believe this is a fundamental and necessary shift in the purpose of corporate reporting, as undertaken several years ago for the investment industry with the UK Stewardship Code. Whilst reporting on actions and procedures is important; having disclosure focused on the impact, outcome and consequence of governance actions is more valuable to shareholders and other stakeholders. In our view the changes to the Code will help deliver this change, however from our experience of Stewardship Code reporting this shift will necessitate a full review of how and what is reported and may take several years to embed.

To support the embedding process, it may be useful for the FRC to introduce guidance on outcomes-based reporting which could provide best practice examples for firms to understand what may be expected from them when making these disclosures. This does not have to be prescriptive guidance.

Q2: 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?

We are supportive of the inclusion of climate ambitions and transition planning into provision 1.

We have been engaging with our investee companies to encourage the incorporation of climate and Just Transition into their strategy and annual reporting for a number of years. As such, we are supportive of the express inclusion of this in the Code. We would recommend that these disclosures should be linked to the other issues, for example, any external social impacts that the transition may create. We also believe that the governance of this process is key and would not remove the reference to this from provision 1.

There is also a lot of ongoing work from the government and other regulators including the FCA and PRA incorporating climate into the Board's work. This includes PRA SS3/19, the work of the transition plan taskforce (TPT) as well as the sustainability work being led by the FCA including DP23/1. The FRC should ensure that its proposals are aligned to this work. As well as avoiding duplication for firms subject to these additional requirements, the FRC should work to ensure that every sector that will play a meaningful role in meeting the UK's statutory net zero targets is obliged to report adequately.

Q3: Do you have any comments on the other changes proposed to Section 1?

As an investor, we do not consider that for most companies shareholders wish to engage with committee chairs regularly. However, where key shareholders do wish to engage, we believe committee chairs must engage. We do not consider it practical to engage with shareholders generally. The proposed changes should therefore be clear that engagement is only required where key shareholders seek engagement.

We would be supportive of disclosure of any engagement which results in amendments to disclosures.

In Provision 6 we welcome reporting of the effectiveness of the operation of whistleblowing (and similar) procedures but do not believe that the board should review the outcomes which should remain highly confidential to the whistleblowing champion and the Chairman to ensure that employees have confidence in the confidentiality protections.

Section 2 – Division of responsibilities

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?

We are supportive of the inclusion of external board appointments as an explicit part of board performance reviews.

We would also suggest that the definition of 'significant' be extended to all forms of employment, including but not limited to private companies, charities, public bodies or other groups involving substantial time commitments. Current disclosures are often limited to public company boards and can often be misleading when the director in question may in fact have significant private commitments.

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?

Whilst we understand the intention of the proposed changes to Provision 15, as drafted there is a significant risk of the addition of a voluminous amount of additional information in the Annual Report for no clear benefit to shareholders and investors.

We consider that the Nominations committee should set out the process it applies to consider directors' aggregate commitments on an ongoing basis and whether they have sufficient time to

fulfil their responsibilities. Additional reporting should then be by exception where the Nominations committee has particular concerns. In such cases, there should be proportionate disclosure of concerns and an action plan to address those concerns over a sensible timeframe.

Section 3 – Composition, succession and evaluation

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

We agree that the proposals outlined strengthen and support existing regulations in place, without duplication.

The revisions are likely to drive accountability and scrutiny and should improve transparency on diversity and succession planning, thus informing investment decisions. The split of Provision 17 into two new Provisions emphasises the importance of developing diverse pipelines through effective succession plans.

As the joint DEI consultation paper from the FCA and PRA has yet to be issued, there is the risk that these proposals will lead to duplication in the future. We are supportive of the consideration by the FRC to avoid duplicative disclosures and encourage it to continue to ensure this remains a key consideration.

In addition, the recently updated Parker review (2023) announced expectations that each FTSE350 listed company publicly report a target for ethnic diversity of their senior management team, to be achieved by December 2027. Given these expectations, we consider it important to align Provision 24 to include gender balance and ethnic minority representation in senior management and their direct reports to ensure greater alignment and progress in broader representation as is intended with the proposed changes to Principle I.

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?

We are supportive of the proposed approach aiming to capture wider characteristics of diversity.

With gender and ethnicity generally receiving the most focus, the revised wording has the potential to help drive companies to establish tangible actions, measures and accountabilities for both protected and non-protected characteristics beyond the current areas of focus. We fully support the principle that companies should have due regard to the need to eliminate unlawful discrimination and to advance equality of opportunity.

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

We agree with the changes to Provision 24, expanding and clarifying the role of the nomination committee in the annual report.

The importance for companies to implement arrangements to maintain the continuity of its operations has rightly been stressed, and we believe the new emphasis on improved clarity on approaches to succession planning should hopefully reduce the use of boilerplate language in disclosure.

We consider the point around the effectiveness of a diversity and inclusion policy unnecessarily repetitive of the language employed in current Provision 23. However, the reference to 'adherence to established initiatives' should prompt firms to report on meaningful outcomes, an area that, in our experience, is often inadequately addressed in current disclosure.

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 generally supportive of the adoption of the CGI recommendations as set out in the Code revisions.

While it is difficult to assess whether the adoption of the term 'board performance review' will shift mindsets in terms of determining the purpose of such reviews, there is scope for firms to focus on aspects of board performance that require improvement. We also support the recommendation that the chair should commission, rather than consider, a performance review to further clarify the purpose of the review and as a natural progression of current Code Principles.

Further, the newly introduced reference to directors' time commitments in Principle K will serve to increase transparency in disclosures allowing stakeholders to make an informed assessment on directors' abilities to carry out their functions.

Section 4 – Audit, risk and internal control

Q10: Do you agree that all Code companies should prepare an Audit and Assurance Policy, on a 'comply or explain' basis?

We are supportive of the AAP requirement and believe that shareholder/ stakeholder engagement on this is beneficial.

We are supportive of the introduction of an Audit and Assurance Policy requirement for Code companies and fully support the 'comply or explain' basis. We believe companies should adopt a

policy that is tailored to their specific circumstances and not subject to a strict rules-based approach, so long as there is adequate disclosure detailing the chosen approach.

We agree with the suggested triennial AAP approach, with annual implementation disclosure in the Annual Report. Our view is that normal oversight of audit and assurance should be delegated to the audit committee, however we consider it essential for shareholders to be able to engage with companies on these annual implementation disclosures, should the need to do so arise. We do not, however, advocate for audit committee engagement with shareholders to be mandated or for the AAP to be subject to any form of shareholder vote.

The new requirements to prepare an AAP will require focus from management to support. We would urge the FRC to carefully consider the cost benefit of additional assurance needs which may be required.

Q11: 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 agree that the reference to the Minimum Standard for Audit Committees is an effective way of removing duplication and avoiding conflicting statements/requirements.

Q12: 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?

We support the proposed expansion of the audit committee's remit to include narrative reporting on sustainability reporting and ESG metrics only where a Company does not have a separate committee focussed on such reporting or where such matters are not reserved for the board.

Other narrative reporting should be appropriately allocated to individual directors (e.g. the Chairman's statement or the CEO's statement) or specific non-executive committees if not reserved for the Board.

Q13: 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 do not support the changes proposed. They appear to go substantially further than US Sarbanes-Oxley (S-Ox) requirements, with potential negative consequences for shareholders and the attractiveness of the UK for issuers.

Our main concerns are as follows:

1. The open-ended nature of the proposed declaration combined with the very broad scope appears to go substantially further than US Sarbanes-Oxley (S-Ox) requirements. It could result in a material increase in cost and complexity for firms that would outweigh the benefits, would not be in the best interests of shareholders and risks negatively impacting the international reputation of the UK. Clarifying the requirements through further guidance is critical in avoiding these risks and ensuring a proportionate and consistent outcome across firms. Consultation on the guidance is an absolute necessity.

2. The proposed implementation timetable is too short for the significant changes proposed and risks undermining the desired outcomes. This is exacerbated with the additional guidance not expected until December 2023. We strongly believe a longer or phased implementation period is necessary.

3. Whilst we support the intent of maintaining flexibility with a 'comply or explain' basis, there is a risk that more firms choose to 'explain', also undermining the desired outcomes. Additionally, requiring firms to provide detailed explanation of non-compliance appears more rules based rather than principles based.

4. The proposed disclosure of details of material weaknesses during a period, even if resolved during the period, runs the risk of leading to confusing disclosures and/or not supporting a transparent culture with respect to controls within companies.

5. The prescribed focus on material controls could impact the ability of firms to maintain existing broader risk-based assurance activity, potentially leading to elevated risk in other areas.

6. The proposals are expected to result in greater responsibility for directors and may make board roles in relevant firms less attractive, with potential unintended consequences, such as a smaller pool of willing directors.

Q14: 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?

The declaration should be based at the date of the balance sheet. Extending it to the whole period would go further than US requirements and put the London market at a competitive disadvantage. Further, the period up to the date of the annual report date is not practical, would be inconsistent with other content in the annual report and would result in duplication in subsequent periods.

Although the current Code isn't specific, it appears to be a point in time assessment of control effectiveness, in line with US S-Ox requirements. In that sense, a declaration based on continuous monitoring is a significant change.

Q15: 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?

Greater clarity would arise by referring to financial reporting.

We acknowledge the aims of the FRC in broadening the scope to include non-financial reporting and we understand there is a need for the control framework to support this. However, the scope of 'reporting' controls needs to be clearly defined to avoid diverging practice and lengthy disclosures which are not comparable across as well as being onerous and costly to implement.

Whilst many firms will already be focused on controls around narrative reporting as part of the annual report or where it links to TCFD/ESG reporting, the scope of this change needs to be clearly defined in the guidance and it should be sufficiently principles based to allow organisations to define and explain their interpretations of this scope as part of the internal control declarations.

The scope of the new requirements should be limited to the annual report and other published financial reporting. We do not believe the benefits of a more general broadening to all narrative reporting produced by firms would outweigh the additional costs.

Q16: 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?

Examples of appropriate frameworks or methodologies would be beneficial to include in the guidance to help inform firms' future approach, but care is needed to ensure that this does not create expectations that only certain frameworks are permissible or sufficient. Allowing flexibility for firms to select the most appropriate approach for their circumstances is important.

It will be important to ensure consistency with other relevant guidance, and collaboration with other bodies may be needed to avoid inconsistency or confusion. An example of this is the Internal Audit standards provided by the IIA, for which a consultation on new Global Internal Audit Standards is ongoing in 2023.

Q17: 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?

Definitions should be sufficiently broad to enable companies to interpret them as appropriate to their circumstances. Guidance should be flexible and proportionate and not be overly prescriptive.

The example definitions for material weakness and deficiency included in the consultation paper meet these criteria and appear reasonable. As well as the areas included in the question, definitions should include other potentially subjective terms such as 'assurance' (e.g. to what extent does it include oversight teams within the 1st Line), ‘continuous monitoring’ or those used in defining scope such as 'operational', 'compliance' or ‘all material controls’. It will be important to avoid inconsistency with definitions included in other relevant guidance from bodies such as the IRM or IIA.

Additional guidance and or examples of what is considered to be “material” in practice would be welcomed, given this is not clearly defined. It would also be helpful for the FRC to provide additional guidance on the application of “materiality” as part of the new proposed requirement for Board declarations to be applicable up to the date of the annual report.

Q18: Are there any other areas in relation to risk management and internal controls which you would like to see covered in guidance?

No, the proposed topics for guidance set out in the consultation appear comprehensive.

Q19: 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 agree that the current Provision 30 should be retained so that all Code companies report on the adoption of the going concern basis of accounting.

PIEs could meet the Code requirement by cross-referencing to their Resilience Statement.

Q20: Do you agree that all Code companies should continue to report on their future prospects?

We agree that all Code companies should continue to report on their future prospects as this is important information for current and potential investors as well as other stakeholders.

Q21: 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 agree that the proposed revisions provide sufficient flexibility for non-PIE Code companies.

We acknowledge that the proposed revisions allow non-PIE companies to report on their future prospects without having to apply the incoming Companies Act Resilience Statement requirements applicable to PIEs.

Section 5 - Remuneration

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

We agree that the proposed revisions strengthen the links between remuneration policy and corporate performance.

We are supportive of the suggested amendments to provisions P, Q and R. We have long advocated for the increased transparency of remuneration and would particularly emphasise the need for simplicity. There is an inclination towards overly complex remuneration structures in the UK, relying on intricate combinations of performance metrics. We note that ‘simplicity’ under provision 40 has been removed from the Code, we would prefer to see this concept retained and included, for example under the new provision 34.

We welcome the changes to Provision R (now Q) stating the remuneration committee as a whole, rather than individual directors should exercise judgement and discretion when authorising outcomes, and we are also supportive of the express inclusion of ‘workforce pay and conditions’ into this section.

We are also in favour of the changes to Provision Q (now P) which clearly articulate the importance of aligning with company strategy, including ESG objectives. ESG metrics in remuneration can be tokenistic and we support the principle that metrics should be included only if it is appropriate to do so and there is a clear, measurable link to strategy.

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

We believe the proposed changes will provide more consistent reporting on malus and clawback provisions.

We support the inclusion of the minimum circumstances in which malus and clawback should be operated. We believe this will lead to an improvement in the level of disclosure provided by

companies, away from the “buckets” of circumstances that may lead to malus / clawback and more towards the underlying detail. It should also help improve consistency (across plans, contracts and the market) and the enforceability of such provisions.

We support the disclosure of minimum periods and agree this would result in increased transparency.

In terms of detailing the use of malus and/or clawback, our view is that this should be disclosed in the year of operation as part of the letter from the Remuneration Committee Chair and captured in the single figure of remuneration disclosures and share-based disclosures (as relevant). We question the value of including details surrounding the use of malus and clawback over a five-year period, given their application is relatively rare (and therefore the disclosure table would be blank for many companies).

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

We are largely supportive of the suggested changes but believe references to ‘simplicity’ should remain.

As already mentioned in our response to Q.22 we believe there is a need to include ‘simplicity’ in some form within the proposed changes. This is the only element within the old Provision 40 that we do not consider to be adequately covered with the other proposed changes.

Although we note that there is a desire to remove duplication with the removal of the explicit reference of pay ratios and pay gaps within the Code as companies report these elsewhere, we still believe these are an important element to consider when setting a remuneration policy. We would suggest these two references are included as an example within bullet 3 of Provision 41, or as a footnote that these elements are included within the definition of ‘overall company pay policy.’

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

We believe that pay gaps and pay ratios should remain referenced under the Code. We believe that this can be achieved through appropriate disclosure on company websites.

Q26: 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?

At this time we do not consider there to be any areas of the Code requiring amendment in relation to AI.