

28 February 2018

Catherine Horton
Financial Reporting Council
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London
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Dear Catherine

UK Corporate Governance Code Consultation

We write with our response to this consultation. Overall, we welcome the approach taken to the proposed revisions to the Corporate Governance Code (new Code). Our comments are:-

- **Independence of the Chair:** we think it would be better to deal explicitly with the requirements for the Chair to be independent on appointment and, other than through time commitment and remuneration from the company itself as its Chair, to maintain their independence throughout their appointment. We wonder whether the change to the composition of the board (now, to include the Chair in the 'independent' majority) was designed to reinforce the independence of the Chair. If so, and in any event, our preference would be to retain the composition of the board as in the existing Code to avoid the Chair being given a swing vote. Please see also below about the impact on non-FTSE 350 companies.
- **Independence:** we prefer the approach in the existing Code which uses, correctly we think, a test of "independent in character and judgement" with a requirement to consider and explain where independence criteria are not met. If one of the concerns underlying the independence criteria in the new Code is that NEDs who have served more than nine years from the date of their first election should not still be capable of being treated as independent in compliance with the Code, this could be made explicit. (Note, if our other points are accepted there will be consequential changes required to the composition of the various board committees.)
- **FTSE 350 exemption:** we see the logic for removing the "small company" exemption for annual re-election of directors and tri-annual external board evaluations. But, the removal of the ability of a company outside the FTSE 350 only to have two independent NEDs and yet remain compliant with the Code in that respect, is, we think, unwelcome. We wonder if a key purpose of removing this exemption is to force those companies outside the FTSE 350 better to consider both the independence and the composition of their boards. If so, and in any event, we think these companies should only have to have an independent

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Chair and two other independent NEDs to be compliant with the Code if they disclose why that composition is considered by the board to be appropriate to the company's circumstances. While companies can choose not to comply with the Code's provisions and give an explanation, we think it puts companies outside the FTSE 350 at a reputational disadvantage not to be able to comply with the Code. Companies outside the FTSE 350 would, if the new Code were adopted as proposed, also face the cost effort of finding additional NEDs (especially for a regulated business) in time for their 2019 financial year.

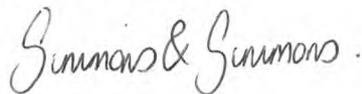
- **Audit and/or Risk:** we think the role of Audit Committee would be better described as 'Audit and Risk' Committee. This is more aligned with its roles and responsibilities. The new Code (Provision 25) does refer to the possibility of a separate board risk committee composed of independent directors. Although not our own idea, we think it is a very good idea to encourage companies (outside the financial services ones already required to have risk committees) to consider establishing a separate risk committee. Among other advantages, it would help the Risk Committee to be more forward looking/less focused on historical financial statements.
- **Workforce views:** we do not think the three methods in Provision 3 should be expressed to be "normal". Instead, we think the requirement should be to establish a method for gathering the views of the workforce, such as through one of these three methods but leaving the flexibility for a company to use some other method of doing so.
- **Investment Association register:** the Investment Association register applies when there is a vote of 20% or more cast against a resolution. The new Code applies where more than 20% of votes have been cast. While the Government's recommendation was more than 20%, we think the new Code should be consistent with the way that the Investment Association is actually operating their register.
- **Governance information:** in the new Code the responsibility for providing information to the board is moved from the Chair to the chief executive. We agree with this, though think that Provision 10 should, instead of referring to "ensuring timely and balanced information", refer to "arranging (with the support of management) accurate, timely and balanced information". ("accurately" is contained in the existing Code and is worth making explicit even if implicit in information being "balanced".) We think that the new Code should include in Provision 10 an obligation on companies to put in place policies and procedures supporting the provision of this information.
- **Senior independent director (SID):** we wonder if the new Code misses an opportunity to enhance the role of the SID. Our proposal is that the SID should be the Chair's deputy and their role should include helping the Chair to facilitate the effectiveness of the board.
- **Board evaluation:** this should include board committees, as well as the board, the Chair and the individual directors.
- **Board evaluation outcomes:** we do not think it is necessary or desirable that, under Provision 23, the annual report should "detail the outcomes" from the board evaluation. If the requirement is to detail (**all**) the outcomes, this could have a chilling effect on board evaluation and cause board evaluations to lose the very candour that is necessary to their value. Better, we think, that the annual report disclosure should focus on improvements to the effectiveness of the board, and should not be an evaluation of whether a board is 'good', 'bad' or 'perfect'.

- **Diversity and inclusion:** we think that under Provision 23 the annual report should include an explanation of not just how diversity supports the company in meeting its strategic objectives but also how “inclusion” does so.
- **Fair, balanced and understandable:** footnote 6 to Principle M extends the requirement to present “fair, balanced and understandable assessments” to “interim and other price—sensitive public records and records to regulators, as well as information required to be presented by statutory instruments.” The wording of the footnote looks dated. Are “price-sensitive public records” in fact “announcements of inside information”? What are the statutory instruments referred to in this footnote and are these in fact information required to be published by statutory requirements or more simply to information which by law must be made public? But, it’s not clear why the Code should seek to regulate the provision of inside information (this is already regulated by the Market Abuse Regulation) and other information which must be made public by law and is regulated by the law which requires its publication.
- **Omissions:** we feel that the following aspects which are omitted from the new Code should be contained in the new Code:
 - Provision A.1.1: Under the existing Code “there should be a formal schedule of matters specifically reserved for [the Board’s] decision”. This is proposed to be moved to the Guidance but we think it better to be retained in the new Code. While having a schedule of reserved matters might be implicit in internal controls we think it’s better to be explicit. It seems to us odd that a company could say that it was in compliance with the new Code but not have a schedule of reserved matters.
 - Under the existing Code (main principle B.4, supporting principles B.4 and provision B.4.2), directors should receive induction, regularly update and refresh their skills and knowledge, the company should provide necessary resources for developing and updating its directors’ knowledge and capabilities and the Chairman should regularly review and agree with each director their training and development needs. We think that development should be contained within the new Code not the Guidance and the focus should include directors’ understanding of the company’s business rather than their knowledge in general (which all directors have).
- **Remuneration Committee Chairs:** requiring these Chairs to serve for at least 12 months on another remuneration committee may be unduly restrictive and would be better qualified by also allowing “or sufficient equivalent experience”. The latter formulation would allow, for example, the global head of human resources to become eligible to become the chair of a remuneration committee directly without having had to serve on that or some other remuneration committee for 12 months. In any event, like the audit committee chair qualifications, presumably the relevant experience needs to be “recent”.
- **Observers, board apprentices and mentees:** subject to confidentiality and other considerations decided by the Chair, we think the Code or the Guidance should expressly encourage companies to consider and disclose steps taken to encourage attendance at board or committee meetings of observers, board apprentices or mentees as part of arrangements designed to encourage understanding of board effectiveness and promote greater diversity and inclusion for potential board appointments generally. (This might also be one means of engagement with a workforce.)
- **More specific comments:** the attached mark-up of the new Code has more detailed comments. There are some instances where the new Code is an opportunity to refresh language that has become dated or could be more precise. In particular, we’ve suggested

avoiding using the word “ensure” in the Provisions. Main Market listed companies are required under the Listing Rules to report whether they have complied with the Provisions and, if not, to explain why not. Our concern about using the word “ensure” is that it works as an absolute; in many circumstances it is referring to making arrangements to “enable” things to be done or not done or would better be expressed in some other form of obligation which is not unconditional and absolute. Unqualified obligations using the word “ensure” risk wrongly creating the expectation that the board can guarantee such matters and therefore could create false expectations.

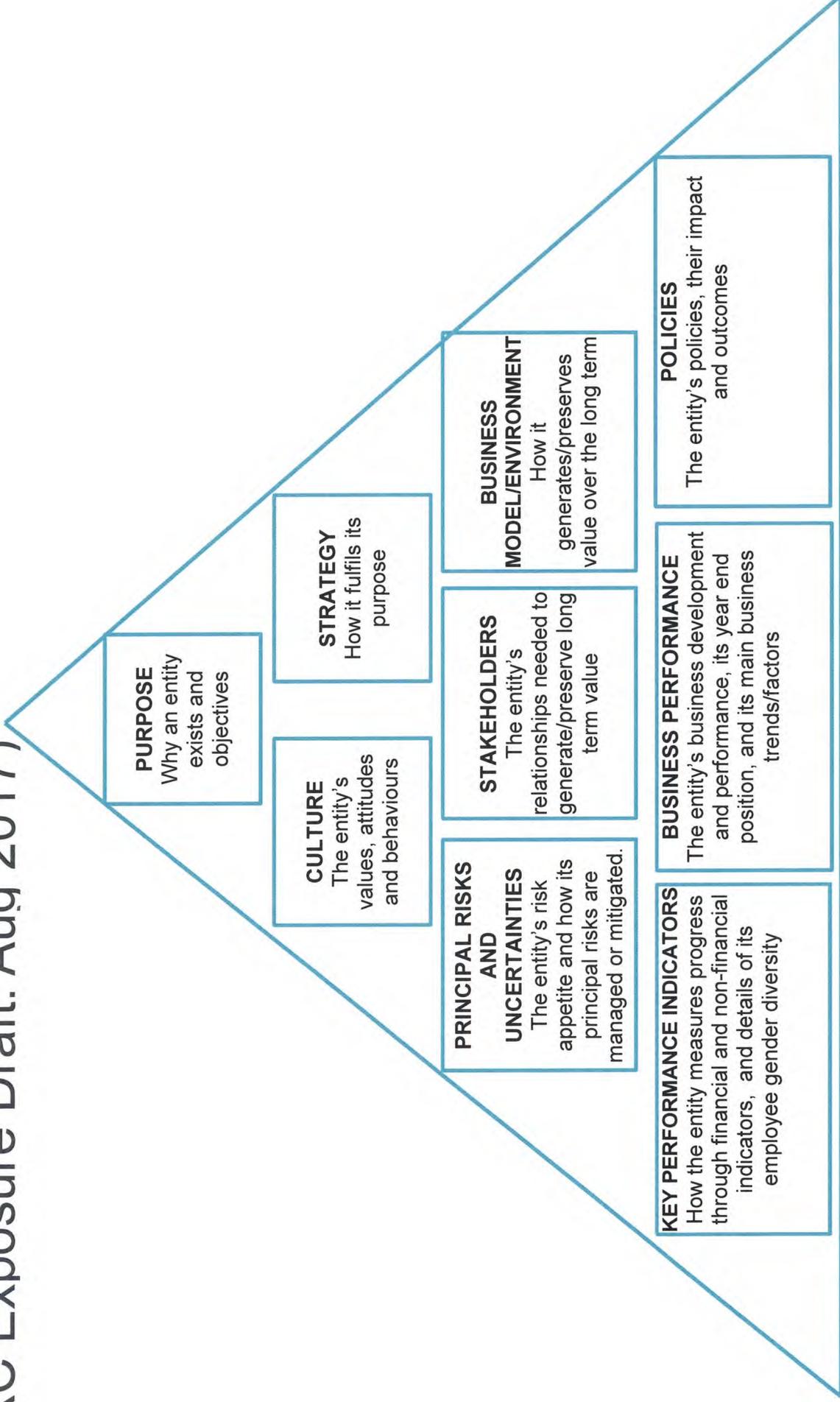
- **Strategic Statements:** we request that the FRC very carefully reviews the alignment between the new Code, the Guidance on board effectiveness and the updated guidance on strategic statements. It’s important that all three work in alignment, to the same architecture, without inconsistency or unnecessary nuances in the key concepts. For the purposes of the architecture, we attach our “governance triangle” produced in response to the FRC’s exposure draft of the updated strategic statement guidance, offered as a helpful way for the reader to understand the architecture.

Yours faithfully

A handwritten signature in cursive script that reads "Simmons & Simmons".

Simmons & Simmons

Strategic Report (FRC Exposure Draft: Aug 2017)



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