Financial Reporting Council
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By email: corporategovernanceprinciples@frc.org.uk

12 September 2018

Dear Sir/Madam,

GC100 response to FRC Consultation on Wates Corporate Governance Principles for Large Private Companies

GC100 is the association for the general counsel and company secretaries of companies in the UK FTSE 100. There are currently over 125 members of the group, representing some 82 companies.

Please note that, as a matter of formality, the views expressed in this letter do not necessarily reflect those of each and every individual member of the GC100 or their employing companies.

General comments

In addition to our responses to the FRC's questions below, the GC100 would like to make a few observations which provide some context to these responses.

As set out in our response to the Government's Green Paper, our view is that companies within a group headed by a company with a premium listing should not be made subject to additional corporate governance obligations (on the basis that any measures introduced should apply to the listed parent company and be reflected in group wide reporting and disclosure). Accordingly, we consider it extremely unfortunate that the new corporate governance reporting requirements in the Companies (Miscellaneous Reporting) Regulations 2018 (the 2018 Regulations) do not contain an exemption for such subsidiaries. However, acknowledging that the 2018 Regulations have now become law, we note BEIS's statements in its Q&A document on the 2018 Regulations which recognise the unique position of subsidiaries of UK listed companies and note that the nature of subsidiaries, and their relationship to the parent company, differ widely. For example, some may be run largely independently whereas others may be part of a more integrated and cohesive group structure (eg a non-trading intermediate holding company) and the appropriate governance arrangements for a subsidiary in scope of the 2018 Regulations will depend on its particular circumstances. As BEIS acknowledges, in some circumstances, it may be appropriate for subsidiaries of a listed company not to apply any governance code because its parent applies the Corporate Governance Code and this is applied throughout the group. As mentioned in our response to question 9 below, we are of the view that, in practice, this will usually be the case for subsidiaries of a listed company which complies with the Corporate Governance Code.

1. **Do the Principles address the key issues of the corporate governance of large private companies? If not, what is missing?**

Yes. We consider the Principles represent a holistic set of arrangements that cover the key issues and can form the foundations for good large private company governance. In particular, the broadly drafted Principle 1, which reinforces the importance of ethical leadership, attitude, mind-set and behavior. We do not consider that anything is missing.

2. **Are there any areas in which the Principles need to be more specific?**

No. We note the broad and non-specific terms in which the Principles are drafted and we take the view that a more prescriptive, one-size-fits-all approach, would not be appropriate. We recognise that they are intended to be a flexible tool that will be interpreted and applied by a wide range of companies. Accordingly, we do not think that there are any areas in which the Principles should be more specific.

3. **Do the Principles and guidance take sufficient account of the various ownership structures of private companies, and the role of the board, shareholders and senior management in these structures? If not, how would you revise them?**

Yes. The Consultation notes that the Principles should be examined in light of the unique requirements of private companies ownership. We consider the Principles and guidance to have been drafted in a broad and non-specific manner so as to facilitate this.

4. **Do the Principles give key shareholders sufficient visibility of remuneration structures in order to assess how workforce pay and conditions have been taken account in setting directors' remuneration?**

Yes. The focus on transparency and targeted disclosures in many areas is clear, including in relation to the visibility of remuneration structures. We agree with the guidance which notes that companies should have a clear policy on the transparency of remuneration structures but believe that this should be for all shareholders, not just key shareholders. We also agree with Mr Wates' reported comments that more extensive disclosure around executive remuneration, specifically of quantum, would not be appropriate in this context.

5. **Should the draft Principles be more explicit in asking companies to detail how their stakeholder engagement has influenced decision-making at board level?**

No. We note the new legislative requirements set out in the 2018 Regulations, including new requirements for certain companies to report annually on how the directors have complied with their section 172(1) Companies Act 2006 duty, engaged with the company's employees and had regard to employees' interests and the company's business relationships with suppliers, customers and others. We consider these requirements to address adequately the concern that there should be increased transparency as to how a company has considered its stakeholders in its decision-making processes. We therefore do not think the Principles need to be made more explicit in this area as this would be duplicative and potentially confusing for companies. If more detail is thought to be required in relation to stakeholder engagement we consider this should be dealt with in the Q&A document which accompanies the 2018 Regulations.

6. Do the Principles enable sufficient visibility of a board's approach to stakeholder engagement?

Yes, and as set out in our response to question 5, we consider any further detail in the Principles in this area unnecessary given the new reporting requirements. In addition, as a very broad spectrum of stakeholders exists across the range of large privately held companies, seeking to include more specificity in this area would not be appropriate.

7. Do you agree with an 'apply and explain' approach to reporting against the Principles? If not, what is a more suitable method of reporting?

Yes. The 'apply and explain' approach assumes companies have chosen to apply the Principles and requires them to explain how this is achieved. We understand that the rationale for this is to move away from a simple 'tick box' approach, to describing how the implemented practices demonstrate improved corporate governance outcomes. In light of the fact that the Principles are broadly drafted and not prescriptive, and therefore not suitable for a more checklist style application, we consider this approach to be appropriate.

8. The Principles and the guidance are designed to improve corporate governance practice in large private companies. What approach to the monitoring of the application of the Principles and guidance would encourage good practice?

The Principles will bring a reference point for shareholders (and other stakeholders) to review the governance arrangements in large private companies. As mentioned above, under the 2018 Regulations certain companies will be required to report annually on how the directors have complied with their section 172(1) Companies Act 2006 duty. This duty is owed to the company, not directly to the shareholders or other stakeholders but has the benefit of the shareholders as a whole as its goal. This is because shareholders are the owners of the company and, ultimately, it is run for their benefit. Accordingly, the monitoring of the application of the Principles and guidance should primarily be by the shareholders of the company (or its ultimate parent company in the context of a listed group). We do not consider any other monitoring should be necessary.

9. Do you think that the correct balance has been struck by the Principles between reporting on corporate governance arrangements for unlisted versus publicly listed companies?

Yes. We consider the Principles have been pitched at the right level and the correct balance has been struck between corporate governance arrangements for listed companies and unlisted companies for whom the adoption of a governance code is appropriate. The Principles cover the key issues and are flexible and non-prescriptive, enabling them to form the foundations of good governance for a range of unlisted companies. We are of the view, however, that the Principles are unlikely, in practice, to be applied by the subsidiaries of a listed company which complies with the Corporate Governance Code.

10. We welcome any commentary on relevant issues not raised in the questions above.

a) The timing of publication of the final Principles (expected December 2018) will be challenging for companies if there are material changes to the draft Principles and guidance set out in the Consultation. In particular, companies with a 31 December financial year end that choose to apply the Principles will have less than one month at what will be a very busy time in the corporate calendar to put in place the necessary procedures. An unintended consequence of this may be that some companies that would otherwise have decided to apply the Principles may choose not to do so.

b) We have some concerns as to what future iterations of the Principles will contain. As they are intended to be the first widely-adopted UK private company code, we hope that the general approach of having non-prescriptive and broadly drafted principles will be retained and that the Principles will not be expanded to cover additional matters or to go beyond what is necessary to improve transparency and governance in private companies.

c) The 2018 Regulations state that a "corporate governance code" is "a code of practice on corporate governance" (Regulation 25 of Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008, as introduced by the 2018 Regulations). We think it would be helpful to rename the final version of the Principles to include the words "code of practice", so as to make it completely clear that applying them satisfies the requirements of the Regulations (as is noted in BEIS's Q&A document).

d) The GC100's guidance on directors' duties is anticipated to be published soon after the final Principles are published. Given the overlap of the areas and themes covered, we consider this will be a complementary, and practically useful, set of guidelines that will be relevant to any company applying the Principles. We would therefore suggest that mention of this guidance be included in what is currently paragraph 15 of the consultation document.

e) The guidance to Principle 3 states:

"*A company's constitutional documents should set out policies and procedures that govern the internal affairs of the company. These include matters relating to the authority, role and conduct of directors, and in some companies may extend to shareholder agreements that set out the rights and responsibilities of shareholders and provide minority shareholder protection.*"

We do not consider that such policies and procedures would usually be set out in a UK company's articles of association, rather these would be contained in internal documents. We therefore suggest that this wording be removed and replaced with the following: "A company should document the policies and procedures that, together with its constitutional documents, govern the internal affairs of the company. Such internal documents could include matters relating to the authority, role and conduct of directors."

f) The guidance to Principle 5 states:

"*The board should establish a clear policy on the transparency of remuneration structures that enable effective accountability to key shareholders.*"

As explained in our response to Question 4 above, we would suggest changing this to refer to "*…accountability to all shareholders.*"

Yours sincerely,

Mary Mullally
Secretary, GC100