Corporate Governance and Stewardship mythbuster

Financial Reporting Council

Q.

What is 'corporate governance'?

A.

Corporate governance is the way companies are directed and controlled. It involves a framework of legislation, regulation, codes and voluntary action for companies and their shareholders. It includes important issues such as directors' duties and remuneration, audit, shareholder rights, capital structure and corporate reporting.

The UK Corporate Governance Code also covers these issues as well as matters such as company purpose, strategy, culture, performance, risk and board appointments and decision-making.

Q.

What do we mean by 'stewardship'?

A.

We think about stewardship in two ways: the stewardship of a company by its directors, and the stewardship of assets by investors (including company shareholdings) entrusted to them by their clients, such as pension funds.

The UK Stewardship Code sets high stewardship standards for asset owners and asset managers, and for service providers that support them. High standards of corporate governance and stewardship are essential for integrity, trust, and the efficient and effective functioning of public and private capital markets.

Q.

So who is covered by the UK Corporate Governance Code?

A.

All companies with a Premium Listing on the London Stock Exchange's main market are within the scope of the Corporate Governance Code, regardless of where they are incorporated.

We also know that many other companies and organisations use the Code as a guide to their own approach to corporate governance.

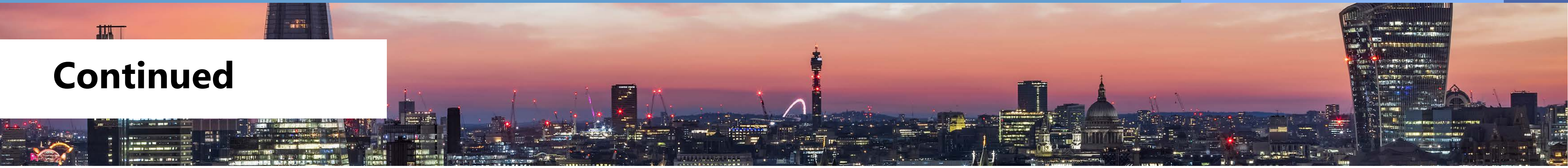
Q.

Why is the UK Corporate Governance Code based on principles, not rules?

A.

Even our largest companies come in all shapes and sizes, stages of development and different business sectors, so can't all be governed in the same way.

Principles offer flexibility for companies to apply the Code in the way that achieves a high standard of governance tailored to their individual circumstances, and demonstrate to their shareholders that they have given this serious consideration through comply-or-explain reporting.



Continued

Q. But what does comply or explain mean? And what if we don't comply?

A. The Code contains high level principles and more detailed provisions. 'Comply or explain' applies to the provisions.

All companies are different and we recognise that there may be circumstances where companies can achieve a high standard of governance without strict compliance with a provision.

If you choose not to comply with a provision, you must say so and explain why. It's important that any explanations are clear and appropriately high-quality. We provide guidance on our website on how to do this.

Q. Does the UK Corporate Governance Code give the FRC powers to enforce against directors?

A. No, it does not.

The Code is a flexible part of a framework that allows companies to develop high quality governance practices for their own particular circumstances which shareholders should understand, engage with and approve.

We do monitor reporting against the Code by selecting a random sample of 100 FTSE 350 and Small Cap companies to assess the quality of reporting, which informs our Review of Corporate Governance Reporting each year.

Q. How does the UK Corporate Governance Code support environmental and social issues?

A. In two ways:

- Through the directors' assessment of risks facing the company
- Decision-making related to directors' duties (particularly the duty to promote the success of the company and the matters needed to be taken into account in doing so)

Both of these involve consideration of environmental and social factors which affect the success of the company.

The code also asks companies to report on workforce engagement and resulting board considerations, board diversity, and progress towards diversity objectives.

Q. What happens if my company is reviewed by the FRC in one of its reviews or thematics?

A. Each year, the FRC assesses the quality of corporate governance reporting from a sample of 100 companies. Our annual review highlights good practice and areas where reporting and action needs to improve.

If a company is found to not comply or provide a high-quality explanation, or has not applied the code principles, the FRC may write to the company indicating how reporting can be improved.

Continued

Q. Our Chair can't meet investors any more – they only send governance people!

A. Most strategic engagement takes place between directors and investment managers at a senior level. Our stewardship research tells us that the quality of engagement is improving.

Investors use a variety of approaches to engage with companies, and engage on a wider range of themes than only those on the AGM agenda.

Q. My investors like the way we do our reporting – how does the Stewardship Code apply?

A. Stewardship is the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society. It exists to set high standards for investors to demonstrate the effectiveness of their stewardship and allows investors to demonstrate successful engagement with companies.

Q. Just suppose our best investors aren't signatories to the Stewardship Code – then what?

A. A large majority of them are! There are currently 179 asset manager signatories to the Code, representing £46.4tn assets under management.

If, however, an investor is not a signatory, FCA rules require them to publicly state their alternative investment strategy.

Q. Isn't this all just box ticking? What value does the Stewardship Code really add?

A. The value of the Code is precisely that it isn't box ticking. It involves a thoughtful approach to the governance of the company and well-informed investor management.

Signatories also need to report every year to ensure that their work on stewardship is an ongoing improvement process – it isn't a 'one and done' approach.

Get in touch

If you have any further queries, please contact us at frccommunications@frc.org.uk

Follow us on Twitter @FRCnews or LinkedIn

FRC
Financial Reporting Council