LSEG welcomes the opportunity to respond to the FRC’s consultation on **Proposed Revisions to the UK Corporate Governance Code**. LSEG is a global financial markets infrastructure business with a core focus on being a leading venue for capital formation and facilitator of economic growth as an intermediary between investors and corporate issuers. LSEG believes that the continuous development of strong corporate governance principles is a fundamental cornerstone of successful and sustainable business - both in the public markets and the private business arena - benefitting savers and investors and creating an economy that works for everyone. Our response below is written from the perspectives of being an operator of a number of markets and also as a FTSE-100 company and issuer. In our role as market operator, we are acutely aware of the importance of ensuring the overall corporate governance framework promotes confidence amongst investors but also recognises that a one-size fits all approach does not always achieve the right outcome for companies. In this regard, we have recently consulted on changes to the AIM Rules to require AIM companies to comply or explain against a recognised corporate governance code; recognising that codes such as the Quoted Companies Alliance’s Corporate Governance Code for Small and Mid-Size Quoted Companies serve as an appropriate benchmark for a significant number of companies on AIM, whilst larger companies will seek to achieve the high standards met by their premium-listed peers as set out in the UK Corporate Governance Code.

We encourage the FRC to bear in mind the following two principles when updating the Code:

**1. The UK’s international competitiveness** - We welcome the acknowledgement in the Government’s White Paper that the current strong framework of company and financial markets law is a key asset to the UK’s position as a global centre for capital formation and attracting investment in the UK economy. We encourage the FRC to ensure that their proposed reforms to the Code, particularly with regards to retaining Board talent and access to public markets for smaller companies, recognise the importance of investment and competitiveness to allow the UK to support the growth and financing of a diverse range of issuers of all sizes, whether they are domestic or international businesses. In reforming the Code, we encourage the FRC to be cognisant of the need to maintain UK plc’s global competitiveness by ensuring that the cost of implementation for businesses does not reduce the attractiveness of doing business in the UK. This is particularly
important at a time when the UK is establishing a new trading relationship with the EU and rest of the world.

2. The comply or explain principle – a recognised strength of the UK’s corporate governance framework is a focus on promoting values, behaviours and developing culture in corporate governance practice, which can be explained and publicly reported against, rather than mandating compliance with prescriptive rules. The comply or explain model recognises that strong corporate governance practices may differ in their implementation depending on the specific characteristics of the company and the needs of its stakeholders. This give Boards the necessary flexibility to adapt provisions of the Code whilst applying its fundamental principles, depending on the nature of the business. Applying too prescriptive an approach in revising the Code would be a departure from the original principles-based regime and ‘suggestions’ or further criteria as set out in some of the proposed revisions may ultimately become interpreted by investors and their advisors as requirements.

Section 1 - Leadership and Purpose

Q. Do you agree that the proposed methods in Provision 3 are sufficient to achieve meaningful stakeholder engagement?

We believe the key focus should be how stakeholder views are made known to the Board and company and for the FRC to explicitly state in Provision 3 that companies are permitted to engage the workforce and seek their views in other ways than those suggested.

We support amendments to the Code in Principle C that for a company to meet its responsibilities to shareholders and stakeholders, the Board should ensure effective engagement with and encourage participation from these parties. We also support the introduction of Principle D that the workforce should be able to raise concerns in relation to management and colleagues where they consider that conduct is not consistent with the company’s values and responsibilities.

The new Provision, however, should not preclude further hybrid models which allow a two-way channel between the Board and workforce and these should be considered within scope in Provision 3, especially for companies which may have diverse and global workforces.
The proposed methods in the new Provision do not make allowances for companies that may want to use a combination of these approaches or other equally representative methods to represent the stakeholder voice. This risks mandating approaches and does not allow companies to explicitly engage workforce voices in other ways that would still act in the spirit of the Government’s White Paper. For example, a ‘Board Associates’ model, where individuals are chosen from the different parts of the workforce to attend board meetings, participate in debate and have an obligation to communicate regularly to the workforce, could be an alternative.

We are also concerned to ensure that the Code does not inadvertently conflict with existing laws. For example the current drafting of Principle A, risks diverging from Section 172 of the Companies Act 2006 and risks inadvertently creating a hierarchy of stakeholders.

Q. Do you agree that 20 per cent is ‘significant’ and that an update should be published no later than six months after the vote?

As drafted 6 months is very prescriptive and in certain situations it may not be possible to provide a worthwhile update after 6 months. A better point for an update might be on or before the publication of the next Annual Report. We would also welcome clarification on whether Provision 6 equally refers to proposed resolutions by the Board or by shareholder resolution. LSEG believes that the update should refer only to a resolution proposed by the Board.

Section 2- Division of Responsibilities

Q. Do you agree with the removal of the exemption for companies below the FTSE 350 to have an independent board evaluation every three years? If not, please provide information relating to the potential costs and other burdens involved.

We disagree with the proposal to remove the exemptions regarding board evaluation, annual re-election, and the composition of audit and remuneration committees offered to companies outside the FTSE 350. We feel that prescribing the same requirements for such companies as for those in the FTSE 350 and above, fails to allow for manifest differences such as size, complexity or operating models and maturity of governance structures.
Whilst we realise that the comply or explain model would mean that companies who did not meet the requirements could provide an explanation, removing the exemptions would mean that companies may feel increasingly obliged to meet criteria which could prove unduly onerous for smaller firms. Adopting a one-size-fits-all approach risks reducing the UK’s competitiveness, particularly for small and mid-cap companies seeking to raise finance in the UK. An alternative approach could be to retain the exemptions but include wording within the code encouraging companies to consider the early adoption of such practices where they feel able to.

Placing these additional obligations on smaller companies could result in significant added costs and compliance burdens and remove the incentive for smaller companies from using regulated markets and thus access to a deeper pool of potential investors.

As of 31 January 2018, the largest company on the FTSE All-Share index – HSBC – has a market capitalisation of £150.6 billion. Meanwhile, the smallest company in the index has a market capitalisation of £26 million – 0.02% of its size. The top 10 companies in the index account for 35% of the index’s market capitalisation, which comprises 638 companies in total.¹

Q. Do you agree that nine years, as applied to non-executive directors and chairs, is an appropriate time period to be considered independent? Q8. Do you agree that it is not necessary to provide for a maximum period of tenure?

In respect of time period, LSEG believes the current Code provisions regarding determining independence should be retained as there may be unintended consequences if the new proposed criteria and arbitrary time periods on the independence of non-executive directors and the chair were introduced without further consultation.

In respect of independence more generally, Provision 15 as redrafted risks mandating rather than guiding independence decisions and removes discretion and judgement from the Board in deciding the best experience and skill set for the company. There may be cases where Board directors’ knowledge, insight and experience remain valuable and useful to the company, but it may be difficult for them to continue on the Board with the proposed new test for independence and nine-year rule. Board discretion is also key for succession planning and a nine-year independence period could make recruiting talent internally impossible and exclude candidates with valuable understanding of the business.

Furthermore, we believe that with annual election, shareholders have all the powers required to vote against directors who they believe are no longer appropriate to serve on the Board. Given this ability, it seems redundant for the code to prescribe this requirement on independence.

If this proposed amendment to the Code is applied, we encourage the FRC to consider ‘resetting the clock’ on internal promotions to the chair and that the nine-year period begins again upon the chair’s first election. Otherwise this would make internal succession planning for the Chair role very difficult for the role of Chair and more likely that Chairs will need to be recruited from outside the Board. Additionally, if this provision is adopted in this more mandatory form then we would recommend that the specific criteria in Provision 15 for independence are not specific enough to work as a set of rules and so we request these are clarified. Failure to do this risks uncertainty for the Board on whether these criteria had been successfully met. For example it is not immediately clear how ‘material business relationship’ would be defined.

We also believe it is not necessary to require the chair to be independent after appointment, given the Chair’s hybrid role and due to the fact he has a greater degree of involvement with the executive than the non-executive directors.

Section 3- Composition, succession and evaluation

Q. Do you agree that the overall changes proposed in Section 3 of revised Code will lead to more action to build diversity in the boardroom, in the executive pipeline and in the company as a whole?

We note in Paragraph 78 in the revised Guidance on Section 3 that directors should not undertake external appointments without prior board approval and the suggestion that the nomination committee might want to consider setting an upper limit on the number of significant other non-executive appointments it considers the Chair and other NEDs may take on.

Given the increasingly global nature of companies and the diverse range of geographies and sectors from which they require expertise, we urge caution on guidance being given regarding what constitutes a ‘significant’ other appointment/directorship. These would require very clear and explicit additional guidance if implemented.
Section 4 - Audit, risk and internal control

Q. Do you agree with retaining the requirements included in the current Code, even though there is some duplication with the Listing Rules, the Disclosure and Transparency Rules or Companies Act?

We would encourage Provision 4 to be modified to cross-refer to the relevant legislation as and when it comes into force by the Government and to avoid duplication and the need to comply with overlapping requirements.

Section 5- Remuneration

Q. Do you agree with the wider remit for the remuneration committee and what are your views on the most effective way to discharge this new responsibility, and how might this operate in practice?

The provision that remuneration committee chairs should have served for at least 12 months before taking up the role is sensible.

We agree that the remuneration policies of the wider organisation should be aligned to the company’s strategy and values and that the remuneration committee should determine executive director compensation in the context of these broader policies. However, we are also mindful of the potentially significant extension to the remit and responsibility of the remuneration committee and request clarification on how the FRC would define the duties involved in ‘oversight’ of wider workforce remuneration and policies more generally to avoid the Committee’s role becoming too operational, akin to the role of HR.

Q. Can you suggest other ways in which the Code could support executive remuneration that drives long-term sustainable performance?

We agree that five years is an appropriate vesting and/or holding period timescale to align outcomes with long-term sustainable value creation. However, guiding as opposed to mandating would be
preferred, as companies may wish to utilise other instruments for a similar purpose e.g. minimum shareholding requirements.

The remuneration committee, in conjunction with shareholders, should be able to decide the most appropriate remuneration arrangements for the company to reflect the individual complexities of the business.

**Q. Do you think the changes proposed will give meaningful impetus to boards in exercising discretion?**

Under the existing Code, the remuneration committee should ‘recommend and monitor’ the level and structure of remuneration for senior management. We do not agree with the amended provision in the revised Code which gives the remuneration committee responsibility for setting senior management (defined as the executive committee or the first layer of management below board level, including the Company Secretary) remuneration, which we believe could undermine the role of the Chief Executive Officer. Rather, the remuneration committee should review the CEO’s proposals, and recommend amendments where it feels necessary. One exemption to this could be any executive whose pay exceeds 90% of the CEO’s total – both salary and at target total compensation.

We agree that the remuneration committee, as a delegated committee of the Board, should have the discretion to override formulaic remuneration outcomes.