Changing the world of work for good

Corporate Governance Code consultation: TUC response

February 2018

Introduction

The Trades Union Congress (TUC) is the voice of Britain at work. We represent more than five and a half million working people in 49 unions across the economy. We campaign for more and better jobs and a better working life for everyone, and we support trade unions to grow and thrive.

The TUC has long recognised the influence of the UK's corporate governance framework on the way in which business is conducted and on the discussions and priorities of the boardroom. The corporate governance framework therefore has a significant impact on the lives of our members and all those working within the private sector. Our aim is to promote a corporate governance system that promotes long-term sustainable company success based on good workforce and stakeholder relationships. We continue to believe that the most effective way of establishing workforce voice in corporate governance is through elected worker directors on company boards, while workforce interests are best represented through collective bargaining with trade unions.

We welcome this opportunity to respond to the Financial Reporting Council's (henceforth FRC) consultation on its Proposed Revisions to the Corporate Governance Code and the Stewardship Code. The previous version of the Corporate Governance Code (henceforth Code) focussed almost entirely on the relationship between shareholders and the board and executive pay; workforce relationships and relationships with other stakeholders were simply absent. In the wake of a number of high-profile corporate scandals in which poor treatment of the workforce and other stakeholders led to widespread public and political criticism, it has become increasingly clear that corporate governance must include a clear focus on stakeholder, and in particular workforce, relationships. The revised Code includes a recognition of the importance of good stakeholder relationships for corporate governance. This is a fundamental and welcome change.

However, for the revised Code to be judged a success, its words must translate into meaningful improvements in corporate practice. It is therefore vital that the Code and related Guidance go beyond warm words and include clear guidance for companies on how they can build and manage positive workforce and stakeholder relationships based on respect and trust.

In this context, it is deeply problematic that neither the revised Code nor the Guidance that accompanies it mentions trade unions at any point. To discuss workforce engagement while not acknowledging unions as the main means through which this currently takes place is a serious omission. At best, it will blunt the effectiveness of the new Code, but at worst it could lead to a dilution of workforce interests and representation within companies. It is essential that this omission is rectified in the final version.

UK Corporate Governance Code and Guidance on Board Effectiveness

Q1. Do you have any concerns in relation to the proposed Code application date [accounting periods on or after 1 January 2019]?

No.

Q2. Do you have any comments on the revised Guidance?

In the first point of its introduction, the Guidance says it "is intended to assist companies in applying the principles of the UK Corporate Governance Code". It makes clear that it is not mandatory and is intended to promote good practice. Given this, the Guidance should be more ambitious in some areas, in particular on workforce engagement (see below).

It is welcome that the Guidance opens by setting out directors' duties as set out in section 172 of the Companies Act and seeks to remind directors that value is dependent on stakeholder relationships. It is right that the Guidance should point to the benefits of boardroom challenge and diversity, and the need to consider stakeholder views and impacts in decision-making as well as the importance of a clear decision-making process.

Gathering the views of the workforce

However, the TUC is greatly concerned that the Guidance's section entitled 'Gathering the views of the workforce' reflects a distorted view of the reality of workforce engagement and as drafted will not promote good practice. There are significant problems with the section as drafted:

- It focusses primarily on individual engagement. The examples that are discussed in the text are whistle-blowing, individuals speaking up and engagement surveys. There is nothing on how to go about two-way collective engagement with the workforce.
- Linked to this, there is no mention of trade unions in the whole section, despite the significant role that unions play in delivering effective workforce engagement[1]. It is particularly bizarre that a box labelled 'some examples of workforce engagement activities' lists nine 'examples', but fails to mention trade unions.
- In addition, the section includes no suggestions or information on how boards could go about implementing Code provision 3 on 'gathering the views of the workforce' and the three options suggested for this. The Guidance simply repeats what is in the Code.

The omission of unions fails to recognise the role that unions play both within many of the UK's most successful companies and in highlighting situations in which there are problems and abuse. For example, without Unite's campaign at Sports Direct, neither the media, nor the public nor the BEIS Parliamentary Committee that issued an excoriating report on the company would have had the information on which to base their reports. That information

[1] See for example the chapter on workforce representation in Patrick Brione Working Well: Perspectives on Good Work and why it matters IPA February 2018, https://www.ipa-involve.com/Handlers/Download.ashx?IDMF=42bd215c-cd49-43c1-9297-1805349b99de

stemmed, directly or indirectly, from Unite. Ryanair is another example where union campaigning has brought poor and abusive employment practices to public attention. On the other hand, many of the UK's most successful companies work with unions and value their role in gathering and representing the views of the workforce. Evidence shows that unions deliver benefits for both workers and employers[2].

The Guidance should be amended to address these weaknesses.

Firstly, the Guidance should include some **core principles of good quality workforce engagement**, which should include the following:

- Workforce engagement must be a two-way and regular dialogue. Initiatives that are one-way and/or one-off are not sufficient, though some, such as whistle-blowing mechanisms, can be useful additions.
- For the workforce to be able to hold a dialogue with management (or the board) it is essential that they are able to form collective views, independent of management. The formation of a collective voice allows workers to express views anonymously, and therefore generates a more accurate representation of workforce views. In addition, it is simply not possible for management or the board to engage with every worker on an individual basis, so collective consultation has significant practical advantages. And importantly, a collective approach gives the workforce greater power and legitimacy.
- Trade unions are the main means through which workers form a collective view independent of management and the role of trade union representatives is to represent workforce views and interests to management. It is essential that the role of unions is clearly referenced within the Guidance.

Secondly, the Guidance should include good practice recommendations for implementing the Code provision 3 on 'gathering the views of the workforce', which should include the following:

Worker directors

- Companies should ensure that they have a minimum of two worker directors on their boards to avoid worker directors being a 'lone voice' on the board.
- Worker directors should be elected by the workforce, with candidates nominated by unions where they are present, alongside nomination by a specified number of workers. A worker director appointed by the board or by management is a contradiction in terms.
- Worker directors should be given training and paid for the time needed to undertake their role.

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[2] For summaries of recent quantitative research on the impact of unions, see https://www.tuc.org.uk/sites/default/files/The%20added%20value%20of%20trade%20unions%20RS.pdf and https://www.tuc.org.uk/sites/default/files/WERS%20study%20WLB%20SR%20format%20RS.pdf
For an analysis of the impact of unions on productivity, see chapter on unions in Joe Dromey Involvement and Productivity The missing piece of the puzzle? IPA https://www.ipa-involve.com/Handlers/Download.ashx?IDMF=e0209cd6-05d5-414a-ac22-c1d61af403f7

- Worker directors would share the same fiduciary duties as other directors and would be there to bring a workforce perspective to the boardroom, rather than to directly represent the interests of the workforce. Direct representation of workforce interests is the role of trade unions through collective bargaining.
- The Guidance should make it clear that worker directors can be members of a unitary board and that introducing worker directors does not require the introduction of a two-tier board.

The TUC has developed proposals for the introduction of worker directors which address many practical points of implementation and it would be helpful if the Guidance could reference this.

Workforce advisory committees

- A workforce advisory committee must be able to represent the collective views of the workforce. It is also important, for the reasons set out above, that the workforce has the opportunity to form collective views independent of management.
- The best way to set up a workforce advisory committee is through trade union recognition and dialogue. Trade unions exist to represent the collective views of the workforce and are therefore well-placed to contribute to a workforce advisory committee.
- It is essential that workforce advisory committees do not cut across the role of unions where they are present, which could undermine workforce representation and interests within companies. Where they are present, union representatives should be automatically included on workforce advisory committees.

A designated non-executive director (NED)

- The Guidance should invite boards to consider the signal that it will send to the workforce if they choose to designate a non-executive director as a means of establishing workforce voice, rather than allowing workers to speak for themselves.

Whatever mechanism is chosen or adopted, it would be useful for the whole board to undertake training on Section 172 of the Companies Act and specifically on understanding the value and impact of workforce relationships. This should include a focus on the nature of the employment model used by their company.

Additional points

Paragraph 19 stipulates that 'where appropriate' the board should consider input from the workforce and other stakeholders. The Guidance should make it clear that given the clear link between the success of the company and the interests of its workforce, all significant strategic decisions should seek a workforce view. It should not be limited to issues that have an immediate and direct impact upon jobs. In addition, input offered or available from the workforce and other stakeholders should always be considered.

The Guidance explains the importance of engaging with the indirectly-employed, as well as directly-employed workforce, which we welcome. However, it then uses the word 'employee' instead of 'workforce' in several places - paragraphs 35 (text and box), 36 (box), 40 (box), 45 (box, 46 (3rd box), 61, 106 (box) and 113 (box). This should be amended.

In paragraph 24, we would recommend that the sentence: 'the annual report is an important means of communicating with shareholders' is amended to '...shareholders *and other stakeholders*'.

Paragraph 26 should be expanded to reference the value to the company of fostering positive relationships with the workforce and other stakeholders.

In paragraph 40 (box on tell-tale signs of a culture problem), we would suggest adding in:

- A short-term focus
- An inability to consider implications for stakeholders
- A lack of long-term discussion and planning

Paragraph 45 (box on sources of culture insights) should include the workforce and trade unions.

Paragraph 46 (on how NEDs and chairs can reach out to the workforce) should include talking with trade union representatives and asking trade union representatives to arrange meetings with staff. In addition, we suggest that 'future leaders' is a very vague term.

Section 2, on division of responsibilities, should include a section on 'The Role of the Workforce Director'. The TUC would be very happy to contribute to further discussion on what this should include.

Section 3, on composition, succession and evaluation, should include an explanation of why publicly advertising board roles is important for boosting diversity. This can be linked to paragraph 77, which states that terms and conditions of NEDs should be made available on the company's website.

Paragraph 95, on board evaluation, should include reference to the board's understanding of the sources of value on which the company's success depends, including the quality of workforce relationships and other stakeholder relationships. It should also refer to the board's understanding of the company's chosen employment model.

In the light of Carillion and other corporate failures in which poor audits have played a role, we would suggest that section 4 will require revision to reflect the lessons arising from those experiences.

Q3. Do you agree that the proposed methods in Provision 3 are sufficient to achieve meaningful engagement?

The TUC believes that the best way of introducing workforce voice in corporate governance is to require that one third of the board should comprise worker directors, elected by the workforce. We believe that this would generate both economic and social benefits, boosting the long-term performance of companies and the interests of workers in the private sector.

The case for elected worker directors and our proposals for their introduction in the UK are set out in full in *All Aboard Making worker representation on company boards a reality*[3], as well as in our submissions to the government's consultation on corporate governance and to the BEIS Parliamentary Committee inquiry into corporate governance[4]. Given the government's proposals on corporate governance published in August 2017 and the FRC's role in implementing these proposals, we will not repeat this case here.

It is worth nonetheless stating briefly why the proposals for workforce engagement in provision 3 are inadequate in the TUC's view.

On **worker directors**, the wording is ambiguous about how worker directors should be chosen. A 'worker director' appointed by management is a contradiction in terms and it should be made clear that worker directors must be elected by the workforce and that unions, where they are present, should be included in the process by being invited to nominate candidates for election. In addition, it is important that more than one worker director is included to help challenge groupthink and prevent the worker director from being a 'lone voice' on the board. It is a serious weakness of the draft Code that a board could simply pick one member of the workforce to become a director and in theory be in compliance with the Code; it is important that this is addressed.

The role of worker directors is to give input from a workforce perspective on company discussions, rather than to directly represent the interests of the workforce. A parallel here (which many businesses have experience of) is trust-based pension schemes, on which one third of the trustees are nominated by scheme members while one third are nominated by the employer. All trustees, however, share the same fiduciary duties to scheme members, regardless of how and by whom they are chosen. Another parallel is the role of parent governors on school governing bodies, who are there to give a parent's perspective on issues facing the governing body, rather than to directly represent all parents at the school.

The importance of worker directors is that they enable the workforce to have an input into strategic discussions and have involvement in the earliest stage of company decision-making.

Alongside this, the direct representation of workforce interests with company management is also essential for meaningful engagement with the workforce to be achieved. This is best done through collective bargaining with trade unions, for the reasons set out above. Trade unions enable the workforce to express a collective view independent of management, allowing workers to speak anonymously and with one voice. Anonymity is essential if views are to be accurate and speaking collectively gives the workforce voice greater legitimacy and power.

Therefore the TUC believes that worker directors on company boards alongside collective bargaining with trade unions provide in combination the most effective channels for workforce voice and engagement.

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[3] https://www.tuc.org.uk/sites/default/files/All_Aboard_2016.pdf

[4] http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/business-energy-and-industrial-strategy-committee/corporate-governance/written/42540.pdf

A **workforce advisory committee** risks falling between the two and creating confusion. If companies do not appoint worker directors and decide that they would prefer to engage directly with workforce representatives, they should engage with trade union representatives, who have long experience of representing workforce interests and views. As noted above, if companies do establish a workforce advisory committee, it must include trade union representatives where these are present in the company and additional representatives should be elected by the workforce. For a company that does not currently recognise trade unions, their first step should be to seek to open discussions to rectify this and offer unions access to their workplace.

Finally, a **designated non-executive director** is, in the TUC's view, particularly problematic. Workforce voice at board level (or any other) can best be provided by the workforce. Appointing others to speak for them risks sending a signal that boards do not trust their own workers and will be widely regarded as a continuation of the status quo.

In summary, for meaningful workforce engagement, companies need both workforce voice in strategic decision-making through elected worker directors and the direct representation of workforce interests through collective bargaining. The proposals do not provide this.

Additional comments on the workforce in the draft Code

Benefits to companies of independent workforce voice

As stated above, the TUC welcomes the additional focus on workforce and stakeholder relationships in the revised Code.

The emphasis within the draft Code, in particular in Principle C but also more broadly, is on the responsibility of the company towards its stakeholders. This is important and should be retained, but should be balanced by a greater emphasis on the benefits of independent voice within companies to make clear that effective workforce engagement is in the interests of companies themselves. This theme could be explored within the introduction and then reinforced within the principles. The TUC would be happy to discuss this further if that would be useful.

Workforce voice should be wider than raising concerns

Principle D refers to the workforce being able to raise concerns in relation to management and colleagues. This is too narrow and workforce views and engagement should be sought on wider company strategy and governance.

Q4. Do you consider that we should include more specific reference to the UN SDGs or other NGO principles, either in the Code or in the Guidance?

The TUC believes that clear references to the SDGs and other relevant principles would strengthen the draft Code. Alongside the SDGs, we would recommend reference to the UN Guiding Principles on Human Rights and the OECD Guidelines for Multinational Enterprises. Many companies and their stakeholders are already familiar with these standards and their incorporation within the Code will support coherence in terms of company practice and reporting. In addition, the UK government has undertaken a commitment at the UN to the

SDGs and it therefore makes sense to reinforce them through their incorporation within the Corporate Governance Code.

We would particularly highlight the importance of SDG 8 on decent work. This goal includes commitments to uphold core International Labour Organisation (ILO) conventions – including on the right to collectively bargain and against discrimination – as well as to support jobs with decent conditions with fair pay. This has particular relevance for companies given their significant role as employers.

Q5. Do you agree that 20 per cent is 'significant' and that an update should be published no later than six months after the vote?

We agree that given the dispersed share ownership pattern of the UK stock market, a 20% vote against a pay resolution is significant. However, we would support an update being published sooner than six months (which is half-way to the next AGM) and would recommend that this is changed to two months or three at most.

The 20% vote should apply to the independent votes, in order to prevent situations where a substantial vote against management is diluted by the votes of a controlling or insider shareholder.

Q7. Do you agree that nine years, as applied to non-executive directors and chairs, is an appropriate time period to be considered independent?

The TUC believes that independence stems primarily from the approach taken by the board member to the company and the board. Some people will be able to take an independent and challenging approach on a board after nine years, while others may not act in this way even though they have been a board member for considerably less than nine years. Having people with a range of backgrounds and experience on the board is more important, in the TUC's view, in terms of challenge and preventing 'groupthink' than time limits for tenure. Having said that, if a time limit for independence is to be applied, nine years is already widely used and seems a reasonable timeframe.

Q8. Do you agree that it is not necessary to provide for a maximum period of tenure?

Yes.

Q9. Do you agree that the overall changes proposed in Section 3 of the 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 do not believe that the changes proposed in section 3 as drafted will lead to increased diversity in the company as a whole, as its focus is clearly on the board and to a lesser extent senior management.

It would be useful if the Code could promote and encourage all types of diversity, including sexual orientation, transgender status, disability (of all types), age and religion, in addition to those currently mentioned in the Code (gender, social and ethnic backgrounds, cognitive and personal strengths).

In addition, the Code should promote diversity across the company as a whole, recognising that diversity within the board and executive pipeline can only be achieved if diversity has been achieved at all levels of the company. Diversity cannot be a bolt-onto at the top.

The importance of all those involved in recruitment undertaking equal opportunities training should be emphasised.

It has widely been recognised that at present board members are drawn from a narrow range of backgrounds. Public advertising of all board positions is important in addressing this by ensuring that a wider pool of potential candidates are aware of, and can therefore apply for, board vacancies. Reliance on search consultancy firms as a replacement for (rather than alongside) open advertising can simply reinforce the barriers that outsiders face. We would strongly suggest that the Code should stipulate that companies should advertise all board positions publicly. This is considered basic equal opportunities practice for other positions and there is no justification for treating board positions differently, especially when their record in terms of diversity has been poor.

If external search agencies are to be used, we believe that a stronger framework for their conduct with a focus on tackling discrimination and promoting diversity in recruitment should be put in place.

Q10. Do you agree with extending the Hampton-Alexander recommendation beyond the FTSE 350? If not, please provide information relating to the potential costs and other burdens involved.

Yes, the TUC would welcome this.

Q11. What are your views on encouraging companies to report on levels of ethnicity in executive pipelines? Please provide information relating to the practical implications, potential costs and other burdens involved, and to which companies it should apply.

The TUC would support this and believes it could play a useful role in terms of focussing attention on tackling the barriers that BME workers face in being promoted to senior positions within companies. However, this must be complemented by measures focussing on recruitment and promotion throughout the company as a whole in order to improve ethnic diversity throughout all levels of the company.

In addition, as argued above, the Code should reference all types of diversity and encourage companies to promote a diverse workforce at all levels. Companies should improve monitoring across all equality strands and devise strategies to tackle the barriers faced by particular groups.

Q14. 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?

It is important to note that remuneration committees have been required to take account of workforce pay and conditions when setting executive pay since 1995, but have spectacularly failed to do. We support the aim of widening the remit of the remuneration committee to address this failure, but it is very important that the wider remit does not undermine or cut across collective bargaining arrangements. Collective bargaining has been shown to be the best way of boosting workforce pay[5] so to undermine it would be entirely contrary to the aim of this proposal. This should be stipulated clearly in the Code.

The remuneration committee should engage with trade unions, who can feed in information on workforce pay and conditions and give a workforce view of executive pay.

The TUC has long called for workers to be represented on remuneration committees, and this role could be carried out by workers directors. It is important to note the increasing support for workforce representation on remuneration committees from organisations such as the High Pay Centre and the Local Authority Pension Fund Forum.

It is important that remuneration committees look at the whole range of workforce policies and practices that contribute to the relationship that a company has with its workforce. The TUC has developed the Great Jobs Agenda[6], which sets out six core standards of good employment practice. Based on these, the TUC recommends that issues for consideration by remuneration committees should include the following:

i) Are workers directly employed or are they employed through an intermediary such as an agency, umbrella party or personal service company? Does the company make use of self-employment as a means of employing people?

ii) If employed through an intermediary, what is the justification for this and what has the company done to assure the terms and conditions under which the workers are employed? If the company makes use of self-employment, can the company provide a justification for this? What role do these employment patterns play in the company's employment model?

The considerations below should apply to the entire workforce, not just those who are directly employed.

iii) Variable hours contracts, such as zero-hours and short-hours contracts - how many and what proportion of workers are on these, and do they have the option of transferring to a standard contract within the organisation? How much control do staff have over their working hours and what notice is given of shifts patterns? Are staff paid for shifts cancelled at short notice?

iv) If variable hours contracts are used, what is the justification for this and what role do these employment patterns play in the company's employment model?

v) Levels of pay - what are the median and lowest decile of workforce pay? Is the company a Living Wage employer? What is the company's pay ratio?

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[5] See for example https://www.tuc.org.uk/sites/default/files/The%20added%20value%20of%20trade%20unions%20RS.pdf and Özlem Onaran et al Working for the economy: The economic case for trade unions Greenwich Political Economy Research Centre Policy Brief 05-2015 http://gala.gre.ac.uk/14102/1/PB052015_Onaran_etal.pdf

[6] https://www.tuc.org.uk/sites/default/files/The_Great_Jobs_Agenda_2017_AW_Digital.pdf

vi) Workforce pension arrangements, including the employer contribution level, appropriateness of scheme design and auto-enrolment opt-out rates. If opt-out rates are high, what is the reason for this?

vii) Does the company recognise trade unions and negotiate with them over pay and conditions for the workforce? Does the company consult the workforce and its representatives over a) pay and pensions b) wider workforce terms and conditions c) work organisation d) company plans and strategy?

viii) Training - what proportion of the workforce received training or started an apprenticeship in the last year and five years, and how was training distributed? Did senior staff receive more training?

ix) Does the company have family-friendly and flexible working practices available for all its workers?

x) What is the company's record on health and safety? Does it have a health and safety committee that includes trade union representatives?

xi) What is the company's record on diversity at all levels of the company? Are there strategies in place to address areas of weakness? What is the company's gender pay gap and what steps have been taken to close it?

xii) Does the company have robust policies and practices to address bullying? What is the evidence that these are working?

Where applicable, the remuneration committee should compare the terms and conditions of staff with those of company directors, including in relation to pay, the level of pension contributions and notice periods. Remuneration committees should ensure that the company's pay ratio is no higher than twenty to one and that there is parity in terms of the level of pension contributions and notice periods.

Q15. Can you suggest other ways in which the Code could support executive remuneration that drives long-term sustainable performance?

The TUC believes that remuneration consultants have generally contributed to boosting executive pay to unjustifiable levels and increasing the complexity and opacity of remuneration arrangements. The Code should discourage their use. In addition, to avoid conflicts of interest, the Code should stipulate that firms used for remuneration services should not have any other business relationship with the company.

There is no evidence that variable pay plays any useful role in incentivising improved performance of directors, and increasing evidence that it does not[7]. On the other hand, there is very clear evidence that executive pay does not reflect company performance. The Code should therefore discourage the use of variable pay. Directors' remuneration should consist wholly (or at least primarily) of annual salary, which would be simple, easy to understand and predictable. It would not require the use of remuneration consultants and would at a stroke make the remuneration report dramatically shorter and easier to

[7] https://www.pwc.co.uk/services/human-resource-services/insights/making-executive-pay-work.html

understand, thus freeing up the time of both remuneration committee members and investors.

In addition, the Code should stipulate that company directors should be in the same pension schemes as their staff and on the same terms.

Finally, the Code should stipulate that notice periods for company directors should be in line with those for other staff in the company. It is unacceptable that directors who have far greater control over the company than their workforce should have greater protection from problems that may arise. This is exactly the type of behaviour that has done so much to damage public trust in companies, and the Code should make clear that this two-tier approach is not acceptable.

UK Stewardship Code Questions

The TUC is a founder member of Trade Union Share Owners or TUSO, an initiative through which union funds collaborate on using their shareholder rights to promote high standards of corporate governance and practice. This gives us an interest in the Stewardship Code from an investor, as well as a trade union, perspective.

Q17. Should the Stewardship Code be more explicit about the expectations of those investing directly or indirectly and those advising them? Would separate codes or enhanced separate guidance for different categories of the investment chain help drive best practice?

The TUC does not support separate codes for asset owners and managers, but we recognise different actors in the investment chain may have different roles in relation to stewardship. We believe that this issue is best tackled through making it clear within the Code or related guidance where the Code Principles would apply differently to asset owners, managers and advisers.

Q18. Should the Stewardship Code focus on best practice expectations using a more traditional 'comply or explain' format? If so, are there any areas in which this would not be appropriate? How might we go about determining what best practice is?

The TUC believes that it would be helpful if the Stewardship Code was more explicit about its expectations of 'best practice'. Determining 'best practice' should be subject to further consultation with all relevant stakeholders, ensuring that the industry does not exert undue influence on this. It will be important to place asset owners and company stakeholders at the centre of this discussion.

Q19. Are there alternative ways in which the FRC could highlight best practice reporting other than the tiering exercise as it was undertaken in 2016?

Tiering is a useful exercise that should be retained.

In addition, building on the point about 'best practice' above, the FRC should clearly indicate when asset managers are not compliant with the Stewardship Code. This would provide useful information for asset owners who wish to take stewardship into account when appointing and engaging with asset managers.

Q20. Are there elements of the revised UK Corporate Governance Code that we should mirror in the Stewardship Code?

It is vital that the themes that have been introduced into the revised Corporate Governance Code should be reflected fully in the revised Stewardship Code. The emphasis in the revised Corporate Governance Code on Section 172 of the Companies Act, the role of workforce voice and the contribution of the workforce to company success, and the importance of wider stakeholder relationships, should all be reflected in the Stewardship Code.

Failure to align the two codes would contribute to incoherence between the expectations and role of shareholders in relation to corporate governance and the expectations of other company stakeholders. Currently, the gap between the role and expectations of investors, company stakeholders and the wider public is a significant factor contributing to public distrust in business and addressing this should be a central aim of the forthcoming revision of the Stewardship Code.

Q21. How could an investor's role in building a company's long-term success be further encouraged through the Stewardship Code?

Please see the response to the previous question. The Stewardship Code should encourage investors to see their role as supporting company boards and others to promote long-term company success through developing positive relationships with the workforce and other stakeholders. While investors with shorter time horizons and differing views of their role clearly exist, the role of the Stewardship Code should be to promote stewardship by encouraging investors to play a stewardship role in relation to their investee companies and to allow asset manager clients to evaluate how effectively different asset managers perform this critical talk.

In addition, the Stewardship Code should address areas of investor practice which may have the effect of undermining long-term company success or at any rate run contrary to a stewardship approach. For example, the Stewardship Code should ask investors to set out the policies and practice on short-selling and on the approach they take to mergers and takeovers.

Q22. Would it be appropriate to incorporate 'wider stakeholders' into the areas of suggested focus for monitoring and engagement by investors? Should the Stewardship Code more explicitly refer to ESG factors and broader social impact? If so, how should these be integrated and are there any specific areas of focus that should be addressed?

Again, please refer to the answers to questions 20 and 21 above.

It is essential that there is coherence between the Corporate Governance Code and the Stewardship Code in terms of company purpose, sources of value and responsibilities. Just as the revised Corporate Governance Code recognises that companies have responsibilities to their workforce, their stakeholders and wider society, so this should be recognised by the Stewardship Code. Equally, both Codes should recognise that stakeholder relationships, especially workforce relationships, are an important source of value for companies, and that societal reputation is part of a company's license to operate.

The Stewardship Code should address workforce relationships and workforce voice explicitly and encourage investors to engage with investee companies over the quality of their workforce relationships. The range of issues relating to the workforce that investors should discuss with investee companies should mirror those that remuneration committees discuss in carrying out their expanded remit. This is explored further in response to question 28 below.

The revised Corporate Governance Code now explicitly includes workforce voice in corporate governance. Investors have an important role to play in supporting this and the Stewardship Code should reflect this.

Q23. How can the Stewardship Code encourage reporting on the way in which stewardship activities have been carried out? Are there ways in which the FRC or others could encourage this reporting, even if the encouragement falls outside of the Stewardship Code?

The quality of reporting on stewardship activities is very variable and generally poor. This is particularly the case with public reporting, as some asset managers report more fully to their clients.

The TUC believes that the Stewardship Code should explicitly promote good quality reporting on stewardship activities, reflecting the points below.

- Investors have significant rights in the UK's corporate governance system and this gives them an important stewardship responsibility towards their investee companies. How investors discharge their stewardship role is therefore a matter of public interest and the public has a right to know how investors, individually and collectively, have acted to influence investee companies. Investors should, therefore, report publicly on both their voting record and their engagement activities.
- It is unacceptable that some major investors still do not disclose their voting record. This should not be compatible with being a signatory of the Stewardship Code and the Code should make this clear.
- It is important that stewardship reporting focuses on activity and outcomes, rather than just policies, which do not necessarily reveal much about what has actually taken place.
- Engagement outcomes should be an important focus of disclosure to enable readers to assess the effectiveness of engagement initiatives.

In addition, the TUC agrees that there are other ways in which the FRC could encourage improved reporting on stewardship, including through events, publications highlighting good practice and seeking discussion with investors whose stewardship reporting is poor.

Q27: Would it be appropriate for the Stewardship Code to support disclosure of the approach to directed voting in pooled funds?

The Stewardship Code should go beyond supporting disclosure on this and should make clear that it is good practice for asset managers to allow directed voting in pooled funds.

Small pension funds, which have less resources to deploy on managing their investments, are increasingly making purchases in pooled funds provided by asset managers, which generally carry lower management charges than segregated funds. Currently, the majority of asset managers refuse to allow clients in pooled funds to express their voting rights, and the asset owners have to follow the voting policy of the asset manager, even where this contradicts their own views or policies. This is an undemocratic practice which does nothing to promote responsible investment and is incompatible with accountability to beneficiaries within the investment chain.

The refusal of asset managers to allow clients to direct voting in pooled funds has proved problematic for initiatives like Trade Union Share Owners and Red Lines Voting that have established a common voting platform to provide small asset owners with a cost-effective means of ensuring that their voting practice is compatible with their values and policies as a fund.

In the case of Trade Union Share Owners, voting recommendations based on our agreed policies are generated centrally in relation to all voting items at FTSE 350 companies on an ongoing basis. This means that all an asset manager has to do is to apply the voting recommendation to the asset owner's share of the pooled fund; no additional assessment of the company is required. However, to date, most asset managers have refused to do this.

It is unacceptable that asset owners should be unable to exercise their voting rights in relation to their investments and reflects a serious democratic deficit in the UK's investment chain. The Stewardship Code should be require asset manager signatories to allow clients to direct voting in pooled funds and those that do not should be designated as non-compliant.

Asset managers often raise administrative concerns about the voting execution required to allow clients to ensure their own views are properly represented. It there are investments in technology that would facilitate this, the FRC should work with the Investment Association to encourage asset managers to collaborate on a joint approach to address the issue.

Q28: Should board and executive pipeline diversity be included as an explicit expectation of investor engagement?

The expectations of investor engagement relating to the workforce should include, but go beyond, diversity. As argued above, the quality of workforce relationships contributes directly to company performance and, at the same time, companies have important responsibilities towards their workforce. The poor treatment of workers by some companies is key reason for low public trust in companies and behind the government's and the FRC's consultations on corporate governance. It is important that investors play their role in raising standards in this important area.

The TUC has developed the Great Jobs Agenda[8], which sets out six core standards of good employment practice. Based on these, the TUC recommends that workforce issues on which investors should engage with investee companies should include the following:

i) Are workers directly employed or are they employed through an intermediary such as an agency, umbrella party or personal service company? Does the company make use of self-employment as a means of employing people?

ii) If employed through an intermediary, what is the justification for this and what has the company done to assure the terms and conditions under which the workers are employed? If the company makes use of self-employment, can the company provide a justification for this? What role do these employment patterns play in the company's employment model?

[8] https://www.tuc.org.uk/sites/default/files/The_Great_Jobs_Agenda_2017_AW_Digital.pdf

The considerations below should apply to the entire workforce, not just those who are directly employed.

iii) Variable hours contracts, such as zero-hours and short-hours contracts - how many and what proportion of workers are on these, and do they have the option of transferring to a standard contract within the organisation? How much control do staff have over their working hours and what notice is given of shifts patterns? Are staff paid for shifts cancelled at short notice?

iv) If variable hours contracts are used, what is the justification for this and what role do these employment patterns play in the company's employment model?

v) Levels of pay - what are the median and lowest decile of workforce pay? Is the company a Living Wage employer? What is the company's pay ratio - is it more than twenty to one?

vi) Workforce pension arrangements, including the employer contribution level, appropriateness of scheme design and auto-enrolment opt-out rates. If opt-out rates are high, what is the reason for this? Are company directors members of the same pension scheme as their staff and on the same terms?

vii) Does the company recognise trade unions and negotiate with them over pay and conditions for the workforce? Does the company consult the workforce and its representatives over a) pay and pensions b) wider workforce terms and conditions c) work organisation d) company plans and strategy?

viii) Does the company's board include at least two worker directors elected by the workforce?

ix) Training - what proportion of the workforce received training or started an apprenticeship in the last year and five years, and how was training distributed? Did senior staff receive more training?

x) Does the company have family-friendly and flexible working practices available for all its workers?

xi) What is the company's record on health and safety? Does it have a health and safety committee that includes trade union representatives?

xii) What is the company's record on diversity at all levels of the company? Are there strategies in place to address areas of weakness? What is the company's gender pay gap and what steps have been taken to close it?

xiii) Does the company have robust policies and practices to address bullying? What is the evidence that these are working?

xiii) Is there parity between the notice periods for staff and for company directors?

Q29: Should the Stewardship Code explicitly request that investors give consideration to company performance and reporting on adapting to climate change?

Yes. The TUC believes that the Stewardship Code should ask investors to encourage investee companies to take a 'Just Transition' approach to climate change, and use collective bargaining and social dialogue to address the challenge of reducing emissions while investing in training and redeployment to protect jobs and livelihoods[9].

Q30: Should signatories to the Stewardship Code define the purpose of stewardship with respect to the role of their organisation and specific investment or other activities? Q31: Should the Stewardship Code require asset managers to disclose a fund's purpose and its specific approach to stewardship, and report against these approaches at a fund level? How might this best be achieved?

We believe it would be useful for Stewardship Code signatories to set out their approach to stewardship and how they believe this is realised in their investment activities. If different funds within an asset manager take different approaches to stewardship, this should be done on a fund by fund basis.

Additional issues

The TUC would support reducing the share ownership requirements for filing shareholder resolutions to make it easier for asset owners to file resolutions as a legitimate way of influencing corporate practice. This is explored further in TUSO's submission to the BEIS Parliamentary Committee inquiry into corporate governance[10].

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[9] For more information on Just Transition, see https://www.oecd.org/environment/cc/g20-climate/collapsecontents/Just-Transition-Centre-report-just-transition.pdf

[10] Available here http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/business-energy-and-industrial-strategy-committee/corporate-governance/written/41868.pdf