

By email: codereview@frc.org.uk

Response to the FRC's consultation on a revised UK Corporate Governance Code 2017/18

1. Introduction

1.1 This submission is made by Bates Wells Braithwaite ("**BWB**") in response to the FRC's consultation on a revised UK Corporate Governance Code (the "**Code**") issued in December 2017. BWB is a unique City law firm, combining a full service legal practice with a special focus on businesses which are seeking to create a positive social impact alongside value for shareholders. BWB is the first UK law firm to become a B Corporation, which reflects our profit-making and purpose-driven nature.

1.2 Most recently, BWB has worked closely with UnLtd, DCMS, BEIS and Companies House officials on a digital tool, Purposely (see getpurpose.ly) which helps company founders, business leaders and owners to understand and act on the flexibility allowed within S172(2) by embedding company purpose within the articles of association. Purposely was launched in beta version earlier this month.

2. BWB's response

2.1 We welcome the FRC's plans to review the UK Corporate Governance Code and the opportunity to respond to this consultation.

2.2 We agree with the revised Code's encouragement of practices that not only generate value for shareholders but also aim to benefit society. We also consider the inclusion of references to the board's responsibility to consider the needs and views of a wider range of stakeholders to be positive.

2.3 There is an emerging movement of businesses with a focus on impact and purpose. This is part of an overall change in the responsible business agenda, as more and more companies have evolved their thinking about social and environmental impact from community social responsibility to placing social impact at the core of their operations. At the same time, start-up businesses, especially those led by millennials are increasingly articulating missions which are focused on solving challenging social issues. From a corporate governance perspective, this shift has significant implications for the purpose of a company, the duties of directors and obligations in respect of reporting and transparency.

2.4 The revised Code should not only reflect that these types of purpose driven businesses exist, but also encourage and offer guidance so that directors are mandated to make decisions having regard to wider stakeholder interests in order to promote the success of the company in meeting the purposes of the company (in accordance with the flexibility afforded under s172(2) of the Companies Act 2006). There are now a number of listed companies in different parts of the world which take this approach, such as Natura in Brazil and Laureate Education in the US, for example.

2.5 In particular, our comments relate to Principle A (Appendix A) and to Appendix B, as summarised in more detail below:



Principle A (Appendix A)

3. In our view, Principle A in Appendix A – Revised UK Corporate Governance Code could be further clarified to ensure it takes into account and adequately represents the law in not just Section 172(1) Companies Act 2006 (CA 2006) but also Section 172(2) CA 2006.
 - 3.1 Although a director must act in a way that he or she considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, Section 172(2) provides companies with the freedom and flexibility to pursue a stated purpose which could be “*other than the benefit of its members*”.
 - 3.2 Thus, it is perfectly permissible for a company to embed alternative purposes within the Articles of Association and it follows that a director of such a company must act in a way that he / she considers, in good faith, would be most likely to achieve these purposes. This is the approach adopted by the B Corp movement, which now numbers more than 2,000 businesses in over 50 countries.
 - 3.3 As it stands, Principle A and paragraph 10 of Appendix B do not expressly account for a company that chooses to take advantage of this flexibility. We recommend that this is amended so the Code expressly recognises that companies may wish to specify a purpose or purposes instead of or alongside the benefit of members.

Setting the Framework (Appendix B)

4. Although we consider it to be a very positive step in the right direction for the Revised Guidance on Board Effectiveness to state that “*values need to be embedded at every level of the organisation*”, it would be beneficial for the Revised Guidance to explicitly reference the possibility for companies to embed their purpose within its constitution or Articles of Association.
 - 4.1 This suggestion will also limit the potential for cognitive dissonance in the minds of directors which may prevent the company’s purpose from being achieved. For example, when making decisions relating to “*incentives and rewards, promotion and development*” directors may ultimately feel obliged to prioritise the benefit to shareholders required by the Articles of Association over and above any subsidiary policies or procedures. This is likely to result in many cases in the interests of the shareholders being given priority where there is doubt about possible competition between competing interests, with the consequent risk that the purpose of the company and its values are undermined by virtue of the fact that the Articles of Association do not incorporate the purpose or the values.
 - 4.2 Thus, the Revised Guidance on Board Effectiveness’s “Setting the Framework” section could be improved and its effectiveness increased if it includes a suggestion for companies to consider including a purpose within its constitution or Articles of Association.

5. Conclusion

- 5.1 We appreciate the opportunity to respond to this consultation. We would be pleased to meet or to provide further information which may be helpful as you work towards finalising the Code.
- 5.2 For any further information on this response, please contact Luke Fletcher, Partner, Bates Wells Braithwaite on 020 7551 7788, l.fletcher@bwblp.com or Louise Harman, Senior Associate, Bates Wells Braithwaite on 020 7551 7679, l.harman@bwblp.com.

Bates Wells Braithwaite

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