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Dear Mr Greenwood and Ms Le Gal,

LAPFF – response to FRC Corporate Governance Code consultation

Thank you for your submission to the FRC Corporate Governance code consultation. We received over 270 responses to the consultation which were overwhelmingly positive. We welcome all responses to the specific questions which will be analysed and reported on in due course. We are concerned, however, that there are a number of inaccuracies and errors in your published introductory remarks and are anxious to dispel these so that others have a more informed understanding. For that reason, we are taking the unusual step of providing responses to your assertions.

For ease of reference we have answered the main points you made in your introductory remarks in the attached note. It is our intention to make these public.

I hope this clarifies matters for you. I would be happy, along with our Chief Executive Officer Stephen Haddrill, to meet you and your key local authority representatives to discuss this further. However, given the clarifications we have provided, accuracy when LAPFF makes public comment on the activities of FRC, is essential.

We are writing to you under separate cover with an update to the consideration our Board has given to the more substantive issues you have raised in respect of True and Fair etc.

Sir Winfried Bischoff

Chair

FRC RESPONSE TO THE LAPFF CORPORATE GOVERNANCE CODE CONSULTATION SUBMISSION

1. **LAPFF:** The FRC needs to be disbanded and a replacement body reconstituted under primary legislation (p1).

FRC: The status of the FRC and its regulatory responsibilities is a matter for government. This will no doubt form part of the review of FRC mentioned recently by the Secretary of State. BEIS have said: “The UK is admired around the world for its corporate governance regime”. (BEIS media response 21st March 2018)

2. **LAPFF:** The FRC has been designated a public body since 2004 but has avoided the obligations that stem from this status (p1).

FRC: It is correct that the FRC has been classified as a public body since 2004 but it is incorrect to say that the FRC “*has avoided the obligations that stem from this status*”. From 2004 the FRC has worked with the DTI and its successor bodies to establish whether the classification recommended by the ONS (and later confirmed by the ONS) was correct.

During that period the FRC has been part of the whole of government accounts and has provided detailed financial information to and maintained a close working relationship with its sponsoring department, has participated in various government initiatives and has reported to the Secretary of State and Parliament each year on its activities.

3. **LAPFF:** The FRC..is.. a collaboration between the Confederation of British Industry (CBI) and the Consultative Committee of Accounting Bodies (CCAB) with seats on the FRC board to those parties as the result for funding it (p1).

FRC: This is an incorrect statement and illustrates the dangers of drawing arguments from historic documents. It is correct to say that when the FRC was established in 1990, the CCAB and CBI Presidents held representative positions on the Board and the Council but it is incorrect that this was in return for funding. Moreover, the FRC’s governance was changed in 2007 to bring an end to any representative seats on the Board and to abolish the Council.

The Chair of the Board and Deputy Chair are appointed by the Secretary of State. Other appointments to the FRC Board are now undertaken following an open selection process and the nomination of an Independent Assessor. Board members are recruited to ensure the FRC has a broad range of skills and experiences in line with its role as the UK’s independent regulator of audit and accountancy and working in the public interest.

4. **LAPFF:** FRC has been noticeably reticent in any criticism of Long Term Incentive Plans (LTIPS) (p1). LAPFF believes this consultation avoids the opportunity to redefine the debate on executive remuneration. The Forum is concerned the current remuneration system is broken (p4).

FRC: The FRC has consulted on a number of significant enhancements to the role and operation of remuneration committees including their scope, the use of discretion, vesting and post vesting holding periods for all share-based awards, alignment of policies across the organisation and engagement with the workforce. The proposals

and the opportunity to comment has provided ample opportunity for debate on remuneration matters.

5. **LAPFF:** ...accounting practice has clearly taken the wrong direction, under the auspices of the FRC, and has come adrift from Company Law (P1).

FRC: FRC does not set IFRS and the use of IFRS is explicitly mandated or permitted by Company Law which, again, is outside our remit. We are active, as are other regulators and stakeholders in the UK and Europe, in influencing the development of IFRS and the process of robust assessment before endorsement.

Your assertion that accounting practice has taken the wrong direction in this context is an opinion, and one that is not shared by the majority of stakeholders who participate in the public consultations that precede the incorporation of new or amended IFRS into EU and, by regulation, UK law. The draft endorsement advice prepared by EFRAG is open to consultation. It is finalised in light of the comments received and then published alongside a feedback statement.

If, after considering this advice, the European Commission propose to adopt the standard this is subject to scrutiny by representatives of the democratic governments of each of the EU Member States and the European Parliament. When this process is complete the IFRS is part of Company Law.

6. **LAPFF:**...the Code consultation is almost entirely divorced from any reference to accounting matters, including in the context of pay (p1).

FRC: The Corporate Governance Code is an essential part of the framework in which companies are directed and controlled. It does not establish the accounting framework under which directors report to shareholders. Accordingly, the Code consultation is not an appropriate channel of communication for accounting matters.

7. **LAPFF:** ...It should not have taken the high-profile collapse (of Carillion) for the FRC to get the law right (p1)

FRC: We welcome the view that you concur with our understanding of S172 (Director duties) or S393 (True and Fair view) but refute any assertion that our view of these Company Law requirements has changed.

8. **LAPFF:** FRC has internal cultural problems (p2).

FRC: We do not recognise your reference to “internal cultural problems” and note that you do not provide any evidence in support of this contention beyond your own previous broad and unsubstantiated statement and out of date criticisms of the FRC’s governance.

9. **LAPFF:** There will be a layer of staff at the FRC who will not have been recruited according to appropriate public sector norms and this includes members of the board itself

FRC: The processes for the selection and appointment of Board members is set out in the FRC’s Governance Bible and as noted above, the Chair and Deputy Chair are appointed by the Secretary of State. The FRC follows all relevant laws and regulations as well as any applicable guidance from HM Government when recruiting members of the Executive.

10. **LAPFF:** ..the FRC Chief Executive stated the position of the government incorrectly (Bompass opinion)...cited the government position without the government having cleared it.

FRC: The FOIA material provided to you included details of a discussion between HM Government officials and the FRC. This included commentary on the approach to be taken in published statements as opposed to any disagreement on the substance. The material provided to you clearly shows that agreement was reached in respect of that response.

11. **LAPFF:** FRC convened a meeting (with the 6 largest accounting firms), for which no minutes exist, to agree a position, that most accounting firms adopted in response to the LAPFF. (p2)

FRC: In response to communication from LAPFF regarding distributable profits, the audit firms wrote to FRC, and at their request a meeting was convened to discuss the FRC guidance. The firms agreed with the guidance provided by FRC and with a note that was attached to a letter from FRC to the firms. FRC also wrote to the firms' INEs explaining that a meeting had been held and the guidance confirmed.

12. **LAPFF:** The FRC position on IFRS as a suitable basis to determine going concern was defective, for the simple reason that IFRS is not prudent (P2)

FRC: Your assertion that IFRS is not prudent is a matter of opinion not fact. There may be differing opinions on IFRS are prudent, but it is not meaningful to say that IFRS is not prudent. As discussed above, before IFRS are adopted for use in the EU, their assessments are subject to public consultation and comment. The decision to endorse and add to European law is made by the European Commission and is subject to democratic oversight. This assessment includes reference to the European public good and the presentation of a true and fair view.

13. **LAPFF:** Only two Board members can be considered independent (p4).

FRC: Incorrect. The FRC has assessed and continues to assess the independence of its Board members in accordance with the provisions of the Corporate Governance Code. In addition, the FRC's Articles of Association and terms of reference for its various committees and councils include various restrictions on the membership of those bodies to ensure independence.

European legislation dictates that no member of a regulatory Board should have practiced as an accountant within the three years prior to his or her appointment. The members of the FRC Board who have accountancy experience all more than meet this requirement. All relevant Board members ceased to be practising accountants within a regulated accountancy firm at least seven years ago.

14. **LAPFF:** It is difficult to understand why the FRC board is only first told of a (public sector status) classification problem in December 2016 (p4)

FRC: Incorrect. The Board has been kept informed of all recommendations and decisions relevant to its classification since 2004.

15. **LAPFF:** ..we can only conclude there was a 'board within a board', with executives and some non-executives knowing more than others (p5).

FRC: The FRC Board has always been kept informed of developments regarding classification and there is nothing to suggest otherwise in the minutes to which you refer. Furthermore, there is no suggestion in the minutes that the Executives "run" the Board and you provide no evidence to substantiate that assertion.

Executive Directors take certain matters forward in accordance with Board decisions and keep the Board informed on progress, which is the way Boards and Executives' typically work.

16. **LAPFF:** It is very odd for employees of a public body...being delegated the function of determining the role of the board...(p5)

FRC: This assertion bears no connection to the reality of our governance processes.

17. **LAPFF:** Correspondence from both the FRC and DTI reveals...the model for board selection...resembles a club (p6)

FRC: This is an inaccurate assertion. See answer to point No (3) above.