

## PROPOSED REVISIONS TO UK CORPORATE GOVERNANCE CODE

### Response to the consultation from Pinsent Masons LLP

We have seen and fully endorse the response to the consultation from the City of London Law Society Company Law Committee.

In addition, we would make the following points of our own.

#### General

1. As a general point, we very much welcome the attempt to shorten the Code which has grown over the years with each successive revision. The FRC has been right to take this opportunity of reviewing the whole Code and deleting or moving many Provisions to the Guidance. As mentioned below, we think there are some other provisions which could equally be moved to the Guidance. We also agree with the removal of the Supporting Principles.
2. We also welcome the continued emphasis on companies, investors and their advisers avoiding a tick box approach. Unfortunately, we fear that the FRC itself at times encourages such an approach, for example by the inclusion of Table 2 on page 4 of the publication, *Proposed Revisions to the UK Corporate Governance Code*.
3. We note that the wording in paragraph 4 of the Comply or Explain section of the April 2016 Code to the effect that "departures from the Code should not be automatically treated as breaches" has been omitted from the proposed new Code. This is a clear statement of one of the main tenets of the "comply or explain" principle and we would urge that this be restored to the new Code (along with the wording on smaller listed companies at the beginning of paragraph 5 of the same section).

#### Provision 3

4. The term "workforce" is not defined and may be interpreted as including a wide variety of individuals who are not employees. The Guidance gives some examples in the context of Provision 3 but it is not clear whether the same examples apply where the term is used in other Provisions of the new Code. Companies will require clarity when they come to report whether they have complied with these Provisions or to explain why they have not. Comparatively few companies subject to the Code are involved in the "gig economy" and so these references to the workforce will have little relevance for them. We therefore suggest that these references to the workforce be replaced with references to employees, and that instead the Guidance be used to urge companies to consider extending these Provisions to the wider workforce where appropriate to do so because, for example, the company uses a lot of independent contractors or agency workers.

#### Provision 6

5. We suggest the opportunity should be taken of amending the requirement for a company to say, when announcing a vote of more than 20 per cent against a resolution, what actions it intends to take to consult shareholders "in order to understand the reasons behind the result". The problems here are that –
  - a. this wording requires an immediate reaction from the company. A better quality response may be forthcoming if the board has time to reflect on what it wishes to say. A time limit of two working days would seem sensible.
  - b. it is right that companies should be required to say what they are going to do to consult shareholders, but the consultation should aim to meet the concerns of shareholders who voted against the resolution. In most cases, the board will understand only too well the reasons why shareholders have voted against

because shareholders will have already expressed those reasons to the board at the general meeting and beforehand. The same reasoning should apply to the six month update, rather than the update be a repeat of what the board is doing to understand the result. We believe most statements are in practice doing this, and it would be preferable for the wording of the Code to reflect this reality.

#### **Provision 11**

6. No reason has been given for the change in approach to the independence of the chairman. Companies understand the provision in the existing Code and no change should be made unless the reason for it can be clearly explained.

#### **Principle G**

7. We believe the reference to non-executive directors offering specialist advice risks suggesting they may stray in to territory which is the responsibility of the executive directors. If a board needs specialist advice, it should obtain it from management or from outside consultants or advisers. Non-executive directors should be seen as generalists providing constructive challenge and strategic guidance to management, not as a resource that can fill gaps in executive knowledge.

#### **Provision 21**

8. Board and director evaluations are important, but it is how those evaluations are carried out, their results and what is done as a consequence which are important, not who has carried out the review. Provision 23 now requires a report on the evaluation. We suggest that the requirement for external facilitation of the evaluation be dropped, at least for companies outside the FTSE 350 and the importance of good reporting each year should be stressed in the Guidance.

#### **Provision 33**

9. The requirement for the remuneration committee to set remuneration for the board means that it will be setting the fees for non-executive directors. That will offend against Principle Q that no director should be involved in deciding their own remuneration. It is true that director fees will often be capped in a company's Articles of Association and any increase will require the approval of shareholders. Non-executive pay will also be dealt with in the remuneration policy which likewise requires shareholder approval. Within the limits set by the Articles and the policy there will, nonetheless, be considerable discretion as to individual non-executive director pay and that discretion should not be in the hands of the non-executives themselves. We suggest the new Code returns to the position of provision D.2.3 in the existing Code which gives such decisions to the full board or to a committee of the board. Alternatively, the Guidance should state how non-executive director remuneration is to be settled.

**Pinsent Masons LLP**

**28 February 2018**