

## Financial Reporting Council

### Proposed revisions to the UK Corporate Governance Code consultation

#### Consultation response by Prism Cosec

For the attention of: Catherine Horton  
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We welcome the opportunity to respond to the Financial Reporting Council's review of the UK Corporate Governance Code. Prism Cosec is a company secretarial and corporate governance practice, and part of the Equiniti Group. We act as company secretary to a significant number of companies across the spectrum from FTSE100 to AIM and private companies of all sizes. An important part of our role involves advising the board of directors on corporate governance compliance and best practice.

Our responses to specific questions asked are as follows:

*Q1. Do you have any concerns in relation to the proposed Code application date?*

We have some concerns in relation to smaller companies and those below the FTSE 350. Some of the revisions in terms of board composition and director independence require long term planning and these companies may be unfairly judged (irrespective of 'comply or explain') by proxy voting agencies if they are not compliant by the required date.

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

It is to be welcomed that the more routine requirements under the current Code are now included in the Guidance. The focus on directors' s172 duties will reinforce directors' responsibilities. The use of questions in the Guidance for boards to consider is very helpful.

Whilst we acknowledge that the Guidance is mentioned in the introduction to the New Code we would urge the FRC to publicise extensively the existence of the Guidance. In our experience when advising companies, the Directors themselves, can very often just focus on only the Code itself and forget there is guidance available on its application. Given this New Code relies heavily on moving items to the Guidance referring to the Guidance by the Board needs to be more instinctive.

We disagree with the suggestion that board minutes should document details of discussion that led to a decision and evidence of challenge. The New Code already provides that Directors can have their concerns recorded in the Board minutes should they have concerns. The requirement to record each

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challenge and query will lead to a more verbatim form of minuting. Minutes should record enough of the context and background to enable the reader to understand the outcome but detailed recording will prevent open and free discussions in the boardroom.

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

We suspect that many companies will use the appointment of a designated non-executive director (NED) to gather views of the workforce. There is a danger that the quality of this work will rest with one individual's response and effort. Therefore, guidance on the designated NED's remit is important to establish the parameters of this work and whether it should be remunerated.

*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?*

If reference is made to any NGO principles this should be in the Guidance not in the Code. If they were to appear in the Code there is a risk that companies would be expected to comply (or explain why not) with these principles.

*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?*

Whilst guidance on what can be considered 'significant' is welcome we question the use of an absolute number. This does not take account of individual companies' shareholder base. If a company has a significant shareholder and effectively only a 25% free float, a 10% vote against may be considered 'significant' as it would represent a large portion of the minority shareholder. The 20 per cent should therefore be for guidance only and 'significant' as a concept should remain.

Updating six months later is sensible.

*Q. 6 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.*

As providers of board evaluation services we believe in the evaluation process and that it can add genuine value to board effectiveness so we do support the extension of the requirement below the FTSE 350. However, the new Code should make it clear that external evaluators should be independent of the company. Whilst this is implied by the requirement to state any connection with the evaluator it does not preclude those who are not independent from acting at present. Further, we believe that a Code of Practice is required to ensure that only suitable practitioners are carrying out evaluations and to a set of minimum standards. The draft Code of Practice supplied by Advance Boardroom Excellence in January 2014 was a good starting point and, when finalised, compliance with

such a code would need to be supervised by an independent body such as the FRC, rather than any organisation which offers evaluation services.

The cost of doing an internal evaluation every second and third year will be modest (especially if it is conducted via a questionnaire). There are some expensive evaluators but it is possible for companies to shop around and get a quality review for a reasonable price.

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

We don't agree with this provision. There is some frustration that very good and impartial NEDs are being classified as non-independent just because of a particular anniversary. This is seen as arbitrary and not based on any data. Independence of a director will vary from company to company and person to person. It would be preferable to have a window of time say 9-12 or even 9-15 years within which companies are required to explain why continuing NEDs should be considered as independent by reference to character, judgment, evaluation outcomes, lack of other conflicts of interest etc. Whilst there is understandable focus on refreshment of boards there is also an argument that continuity and experience are very valuable for boards. Communication of a company's long term plan and strategy is key to keep investors on-side particularly at difficult times.

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

Yes. A maximum period of tenure is unhelpful and we would strongly disagree with any proposal to implement this. Every company and director is different and the experience of a long serving NED can be very useful.

*Q9. 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?*

Yes. All actions that increase focus and raise awareness of shortcomings in diversity will help to drive improvements and ensure that companies have access to the widest and best quality pool of executives and workforce.

*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. Costs should be minimal and research has shown that it makes good business sense to have diverse management and board.

*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.*

This is to be welcomed. Many companies already have to collect and report on gender pay so this will be an extension of the data collection process rather than setting up anything new. It should apply at least to FTSE 350 companies.

*Q12. 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?*

Yes. Many companies chose to use the Code as their corporate governance guide even though they are not listed on the Main Market and therefore including key items in the Code is important. For those companies who are listed it highlights the importance of these areas.

*Q13. Do you support the removal to the Guidance of the requirement currently retained in C.3.3 of the current Code? If not, please give reasons.*

Yes. Ensuring the terms of reference are available is now standard practice and audit committee reporting appears elsewhere in the new Code.

*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?*

Yes. Having in the Guidance the need for regular reports to the remuneration committee on workforce pay, incentives, performance management, training and flexible working practices particularly at the time of reviewing executive pay would assist in ensuring it receives the appropriate attention.

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

Much consideration has been given by government, investor relation bodies and others as to how executive remuneration can be used to sustain long-term performance. The extension of long term incentive performance and holding periods and meaningful use of discretion to restrain pay outcomes are ways of achieving this. However, investors need to allow companies and boards time to perform at a steady pace and not call for immediate and ever increasing returns. Communication of longer term plans is therefore key and the Code and/or Guidance should encourage communication with investors and others about such longer term plans.

*Q16. Do you think the changes proposed will give meaningful impetus to boards in exercising discretion?*

We assume the question refers to new Provision 37 – so that boards can override remuneration outcomes. We are not sure about how this would work in practice and also the fact that Executive Directors are on the board but not on the remuneration committee goes against the ethos of having an independent committee reviewing executive pay. These matters should be the responsibility and

acted on by the remuneration committee. The ability to override formulaic outcomes is however welcomed provided the discussion and authority sits in the correct forum.

*Other*

We strongly disagree with the approach taken in the new Code on independence of the Chairman. Many 'controlled' companies have a Chairman who is non-independent on appointment and on a continuing basis because they are connected with the major shareholder. Such Chairs are usually well placed to call the executive team to account more so than unconnected Chairs and it seems nonsensical to make the non-independence of the Chairman automatically a breach of the Code, even if it is explained. The current approach is more logical because conventional wisdom is that a Chairman cannot be easily truly independent once they are appointed due to the amount of time and activities required by their role. The current approach of discounting the Chairman in the calculation of the balance of the Board between independent and non-independent directors is more appropriate.

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