CORPORATE GOVERNANCE REFORMS - UK AND OTHER EUROPEAN COUNTRIES

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UK CORPORATE GOVERNANCE REFORMS: BACKGROUND

Context:

- Corporate scandals (impact on workforce, pensioners, suppliers; private as well as listed companies; concerns about excessive pay)
- Political climate (mistrust of business, ‘them and us’)
- ‘Corporate Culture and the Role of Boards’ (Financial Reporting Council, 2016)

Leading to:

- Government regulation (2017-2018)
- Revised UK Corporate Governance Code and guidance (2018)

NEW UK REGULATIONS

Remuneration:

- Gender pay gap reporting (listed and large private companies; first reports published 2018)
- CEO/ workforce pay ratio reporting (listed companies only; first reports will be in 2020)

Stakeholders:

- Requirement to report on how directors have met their duties to stakeholders (listed and large private companies; first reports will be in 2020)

Private companies:

- Large private companies to report on their governance arrangements (first reports will be in 2020)
- Wates Principles (2018) provide a simplified code for private companies to report against

NEW UK CODE: CHANGE OF EMPHASIS

Principle A:

- "A successful company is led by an effective and entrepreneurial board, whose role is to promote the long-term sustainable success of the company, <u>**generating value for shareholders and contributing to wider society**</u>"

Principle B:

- "The board should <u>**establish the company's purpose**</u>, values and strategy, <u>**and satisfy itself that these and its culture are aligned**</u>. All directors must act with integrity; lead by example and promote the desired culture"

CORPORATE CULTURE

UK Corporate Governance Code:

- “The board should assess and monitor culture. Where it is not satisfied that policy, practices or behaviour throughout the business are aligned with the company’s purpose, values and strategy, it should seek assurance that management has taken corrective action. The annual report should explain the board’s activities and any action taken”.

Guidance on Board Effectiveness:

- Identifies questions that boards can ask management and indicators for monitoring culture. Examples include: staff turnover and absenteeism rates, complaints received and resolved, health and safety data, and promptness of payment to suppliers.

- Makes the connection between company’s culture and performance incentives and reward structures for management and staff.

STAKEHOLDERS

UK Corporate Governance Code:

- “The board should understand the views of the company’s key stakeholders and describe in the annual report how their interests have been considered in board discussions and decision-making. The board should keep engagement mechanisms under review so they remain effective”.

- “For engagement with the workforce, one or a combination of the following methods should be used: a director appointed from the workforce, a formal workforce advisory panel, or a designated non-executive director”.

Guidance:

- ‘The Stakeholder Voice in Board Decision-Making’ (ICSA/ Investment Association, 2017) contains guidance on the practical aspects of understanding the views of, and impact on, stakeholders (for example, board composition and training, managing the agenda and board papers, engagement methods and feedback). Available at https://www.icsa.org.uk/knowledge/resources/stakeholdervoice

BOARD EVALUATION

UK Corporate Governance Code:

- "Annual evaluation of the board should consider its composition, diversity and how effectively members work together to achieve objectives. Individual evaluation should demonstrate whether each director continues to contribute effectively".
- The annual report should describe how the board evaluation has been conducted, the outcomes and actions taken, and how it has or will influence board composition.
- Large listed companies should have an externally facilitated board evaluation at least every three years.

Guidance on Board Effectiveness:

- Identifies the different factors that determine board effectiveness which might be included in the evaluation, and makes recommendations on how to design the process to receive maximum benefit.
- The Government has asked ICSA to produce a code of practice for providers of board evaluations, as there are concerns that not all of them are well qualified to undertake the task.

OTHER CORPORATE GOVERNANCE DEVELOPMENTS IN EUROPE

- Other Codes updated in 2018 or currently under review include Austria, France, Germany and Italy.
- Changes include:
  - social and environmental issues (France – the board must consider them in its decision-making process);
  - gender diversity (Italy – minimum one-third of the board);
  - independence and appointment of shareholder representatives (Germany - sets out more detailed criteria for both); and
  - external board evaluations (Austria – at least every three years).
- The revised EU Shareholder Rights Directive must be implemented by June 2019. It introduces new mandatory requirements on remuneration and related party transactions.

Thank you

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