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Proposed Revisions to the UK Corporate Governance Code 2023

Dear Code Review Team

We welcome the opportunity to respond to the consultation on the FRC's proposed revisions to the UK Corporate Governance Code. We are broadly supportive of the proposals and welcome the aim to strengthen controls and their associated reporting.

Our response focuses on our key points on the proposed revisions, cross referenced with the *proposed* Principles and Provisions (rather than providing responses to the individual questions posed). Our key areas of comment are:

- i. The explicit focus on outcomes and exception reporting is likely to improve narrative reporting (Proposed Section 1).
- ii. There is sufficient coverage in the current wording for directors' commitments; the additional proposed wording would likely create issues due to the sensitivity of the underlying information (Proposed Provision 15).
- iii. Greater clarity is needed on the core functions and processes of the Nomination Committee (Proposed Section 3).
- iv. Improved diversity definition (Proposed Principle I).
- v. The opportunity to define Board members' skills, experience, and knowledge (Proposed Principle J).
- vi. Although Board evaluations could be re-named to reviews, we do not think it would facilitate the intended aim of enhancing the continued process improvement focus of evaluations. Additionally, there is sufficient coverage in the current wording for directors' commitments in regard to Board evaluations. We propose a further amendment to the evaluation principle to highlight the key composition input. (Proposed Principle K, Provision 22 and Provision 24).
- vii. Additional control definition is welcomed (Proposed Section 4 and proposed Provisions 26 and 27).
- viii. Additional control definition is welcomed with a suggested addition of long term focus to remuneration committee's independent judgement (Proposed Section 5, Principle Q and Provision 43).

This commentary is a combined response of the Exeter Centre for Leadership and the Department of Finance and Accounting, from the [University of Exeter Business School](#), and the [University of Exeter Law School](#):

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Yours sincerely

University of Exeter

Response to Consultation

i. **Outcomes focused** (Proposed Section 1)

We support the proposed wording in section 1, in particular the new Principle D which explicitly states the requirement to report on outcomes and meaningful exception reporting. This should improve the narrative reporting throughout the Annual Report and Accounts.

In the next full review of the Code, we would suggest that consideration be given to further amendment of Principle A. We suggest that the first sentence should end with '**generating value and contributing to wider society**'. We do not believe that generating value for shareholders and contributing to wider society are mutually exclusive and the suggested change moves from a pure shareholder centred position to considering value in a more generic way.

ii. **Directors' Commitments** (Proposed Provision 15).

A focus on directors' commitments is welcome. However, director commitments are sensitive and commercially confidential issues, we do not believe that behavioural or reporting outcomes would be improved under the proposed changes.

The wording in current Provision 15 and current Provision 18 sufficiently encompass:

- The reporting of significant appointments and the confirmation that directors have sufficient time to undertake their duties.
- The reporting of director biographies and significant appointments.
- Board approval of additional significant appointments.

If enacted, the proposed Provision 15 wording should be reviewed to reflect a number of underlying issues:

- As noted within the consultation document, it is challenging to compare different time demands and expectations of board roles. This is particularly so due to personal and market sensitivity of the underlying information. Additionally, there are inherent difficulties in reporting on external companies potentially affecting directors' availability. These market and personal sensitivities would make public reporting of related actions challenging, potentially negating any meaningful reporting.
- Any actions taken to address directors' commitments should rest with the leadership of the Chair, assisted by the Nomination Committee, and ultimately under the approval of the board. The proposed wording does not assist in clarifying these responsibilities.
- While it is important to assess directors' commitments, we contend that the Chair, assisted by the Nomination Committee, should focus on the resultant collective resources available to the board which is not included within the current or proposed wording.

The related annual review of directors' commitments (Proposed Principle K) is discussed in the section on Board evaluations.

iii. **Core Functions and processes of the Nomination Committee** (Proposed Section 3)

We welcome the strengthening of wording in the proposed section; however greater clarity is needed on the core functions and processes of the Nomination Committee.

Although we appreciate that the Code gives firms flexibility in their approach, we suggest that the core purpose of composition, succession and evaluation be highlighted, alongside key diversity considerations in these activities. This will start to address three inherent description issues which are present in both the current and proposed wording–

- The Committee name does not describe the underlying function.
- The key activities are only described fully within section 3's heading and the reporting requirements.
- There is ambiguity between the underlying processes.

We suggest five further enhancements to start to address these issues:

- Extension of Provision 17 to include an overall remit of the committee – '***The nomination committee oversees composition (including appointments), succession and evaluation with the aim of enabling a diverse and effective board.***' We believe 'oversees' gives sufficient flexibility of approach while addressing the ambiguity surrounding the committee's function.
- The proposed Provision 18 goes part of the way to address the ambiguity via appointment and succession considerations. We suggest that composition be added to appointments to highlight that composition reviews can encompass at least annual reviews which can include independence, diversity, tenure, and rotations; these are important to the health of the Board and much wider than intermittently required appointment processes. We suggest an amendment to the first sentence of proposed Provision 18 – '***The nomination committee should lead the process for composition including appointments.***'
- As composition can be separate to succession processes, we suggest that it would also be useful within Provision 18 to amend the proposed text to include '***The nomination committee should plan for orderly succession ...***'.
- The proposed Provision 22 could be amended to start with '***The nomination committee ensures a formal and rigorous annual evaluation***'. This highlights the key evaluation responsibilities of the committee while allowing the flexibility for the Chair to lead the process.
- Extend the reporting requirement to include composition reviews, which are normally included within narrative reporting and therefore reflects normal practice. Amend the proposed Provision 24, bullet two: '***The composition of the Board and the appointments...***' and reorder the bullet so this comes as the first bullet point (aligning with the overall section name).

In the longer term, further work is needed to delineate composition and succession processes and how they interlink with each other and evaluation. The University has initiated a project on this, and we will keep the FRC informed of progress. Early findings of this project highlight that nomination committee's remit can also consider provisions within section 2 as part of their composition, succession, and evaluation work (such as independence reviews, division of responsibility, and directors' commitments) which needs to be understood further within the overall processes.

We welcome planned committee guidance from the FRC. This may give an opportunity to provide more detailed advice on underlying processes and examples of best practice reporting.

iv. **Diversity definition** (Proposed Principle I)

We welcome the change of emphasis in the definition of diversity.

In our response to the 2018 Code consultation, we highlighted that the inclusion of cognitive, and personal strengths in the current list dilutes the emphasis on equality and conflates the issue of constructing a team (cognitive and personal strengths) with diversity characteristics. Therefore, although we welcome the clarification of protected and non-protected characteristics, we reiterate

that including '*cognitive and personal strengths*' should not be included within the diversity principle. We suggest that this be *removed* from the proposed Principle I.

To assist with the delivery of the new definitions, it may be useful within the updated Guidance on Board Effectiveness to include examples of protected and non-protected characteristics and expand the detail of constructing the Board as a team.

v. **Board members' skills, experience, and knowledge** (Proposed Principle J)

We believe that the current revision has missed the opportunity to provide definitions of skills, experience, and knowledge expected of board members. In particular, the extended remit of board oversight and corporate reporting (see e.g. proposed Provision 1) covering the topics pertaining to social and environmental issues (climate change risks, in particular) is likely to necessitate relevant skill sets for board members beyond what has been expected to date. For instance, while to date, it might have been reasonably expected that board members have sufficient financial expertise, the current remit of the board role is likely to require expertise in environmental issues (from at least some of the members) to assure oversight of the corresponding issues and of reporting in this domain.

vi. **Board evaluation / reviews** (Proposed Principle K, Provision 22 and Provision 24).

We welcome that references to evaluation of performance and effectiveness have remained in the proposed wording to assist with understanding and it is intended that evaluation guidance be enhanced. Although Board evaluations could be re-named to reviews, we do not see how this would affect the intended aim of ensuring that assessments would focus on continued self-improvement. This may be achieved more meaningfully by strengthening the related sections in the Guidance on Board Effectiveness.

We agree that the Board evaluation should (and normally would) include a directors commitment review. However, we do not believe that the additional wording in proposed Principle K is necessary as the current wording covers how each director demonstrates their effective contribution. Should the additional sentence be included in the updated guidance, we propose that this would be more meaningful within the description of the requirement in the proposed Provision 22.

Consideration should also be given to whether proposed Principle K should be extended to include '*how the evaluation influences current board composition and future board composition*'. This wording is currently within the reporting requirements of the committee only. This would also link to the prior response (v) on board skills, experience, and knowledge.

Finally, we contend that the addition of *future* within the last bullet of proposed Provision 24 may change the emphasis of reporting to only future composition changes when prior and future actions undertaken should be of equal merit.

vii. **Audit and Risk controls** (Section 4 and proposed Provisions 26 and 27)

We welcome changes to Section 4, particularly as these fill a hiatus created since the consultations on restoring trust in audit and governance.

In proposed Provision 26, bullet five, we would welcome a further amendment to the reference to stakeholders. We suggest this be amended to 'engaging with shareholders and stakeholders', removing reference to '*other*' as this removes emphasis and places them as secondary. However, we query how engaging with stakeholders would be enacted in practice and note that the more traditional role of engaging with shareholders where appropriate on external audit is included without mention of stakeholders in the newly published 'Audit Committees and the External Audit: Minimum Standard'.

We agree that the remit of audit committees should be expanded to include narrative reporting, including sustainability reporting, and where appropriate ESG metrics, where such matters are not

reserved for the board (as per Question 12 of the consultation document). Therefore, we welcome the revisions to the currently proposed Provision 27 with its explicit reference to ESG issues.

viii. **Remuneration** (Proposed Section 5, Principle Q and Provision 43)

We welcome changes to Section 5 including the additional specification of remuneration committee duties and the updated annual report wording in proposed Provision 43. In particular, we welcome the expectation of companies to align their remuneration policies with the company strategy and environmental, social and governance objectives.

We agree with the deletion of current Provision 40 and the related new proposed text in proposed Provision 34. However, we note that within the deleted current Provision 40, we no longer have the benefit of the more detailed definition of proportionate and its link to long term performance of the company. We suggest that the committee explicitly considers longer term impact to re-emphasise this key issue. We propose the following amendment: “taking into account company and individual performance, workforce pay and conditions, **long term impacts**, and wider circumstances”.

In line with greater focus on stakeholder reporting, we also propose to re-phrase the third bullet point of the proposed provision 43 as follows: “what engagement with shareholders and **stakeholders (including the workforce)** has occurred and what the impact this has had on remuneration policy and outcomes, including the alignment with executive remuneration and the overall company pay policy”.