January – November 2020

Corporate Governance

Key developments

This briefing is the second in our series of briefings on corporate governance and is designed to provide a synopsis of topical corporate governance matters impacting companies in the United Kingdom. This briefing tracks the development of certain matters identified in our first briefing **available here** and outlines new matters of interest.

This briefing focuses on key matters arising since the start of the year. If you would like further details on a topic, please contact a member of our Public Company Advisory team, whose details can be found at the end of this briefing.

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The effect of the COVID-19 pandemic on listed companies' obligations

Summary of measures put into place to support companies during the COVID-19 pandemic

Ongoing

The COVID-19 pandemic has caused vast disruption to the 'ordinary course of business' for companies and their employees. The following provides a summary of measures that have come into place to mitigate the difficulties posed by COVID-19 on listed companies and to provide companies with temporary support in fulfilling their legal obligations during the pandemic. As of the date of this publication, the following temporary measures remain in effect.

Measure		Length of measure
FCA	Threshold for private notifications of net short positions reduced to 0.1%. (Announced 31 March 2020, and renewed on 17 June and 17 September 2020)	Three (3) months from 17 September 2020
	Temporary extension of the deadline for companies to publish annual financial reports from four to six months and half-yearly financial reports from three to four months. (Announced 26 March and 27 May 2020 respectively. Confirmed 5 November 2020)	Until further notice and applicable for reporting periods ending at least up to 31 March 2021
	In line with ESMA's statement of 27 March on financial reporting deadlines, the FCA will not prioritise supervisory actions against listed companies in respect of half-yearly financial reports or annual financial reports. (Announced 27 May 2020. Confirmed 5 November 2020)	Until further notice and applicable for reporting periods ending at least up to 31 March 2021
	Where the Listing Rules require a general meeting to approve a Class 1 or related party transaction, a general meeting need not be held if the company has obtained (or will obtain) written undertakings to vote in favour from a majority of shareholders who are eligible to vote. (Announced 8 April 2020)	Until further notice
	Key modelling assumptions regarding COVID-19-related business disruption which underpin the 'reasonable worst-case scenario' as per ESMA Recommendations may now be disclosed in an otherwise clean working capital statement. Similar guidance applies to supplementary prospectuses and circulars. (Announced 8 April 2020)	Until further notice
UK Government	Under the Corporate Insolvency and Governance Act 2020 ("**CIGA**"), companies are allowed to hold hybrid and /or virtual shareholder meetings and to fulfil quorum requirements without any members being in the same physical location. For more information on CIGA, see further below. (CIGA in effect 26 June 2020. Extended 29 September 2020)	30 December 2020
	Companies can delay publishing their Modern Slavery Statement by up to six months. (Announced 20 April 2020)	Until further notice
	Companies with filing deadlines between 27 June 2020 and 5 April 2021 inclusive can apply for an additional three months to file their accounts with Companies House. (Announced 25 March 2020)	Until 5 April 2021

Measure		Length of measure
	The Equality and Human Rights Commission announced the suspension of the enforcement of gender pay gap deadlines for the 2019 / 2020 year. Reporting of organisations' April 2019 data were originally due by 4 April 2020. (Announced 24 March 2020)	Until 5 April 2021
London Stock Exchange ("**LSE**")	Listed companies may defer a payment of a dividend by up to 30 business days, but not exceeding 60 business days. The company will need to notify the LSE Stock Situations Team and justify the reason for the deferral. (Announced 25 March 2020)	Until 2 November 2020
The Pre-Emption Group	Recommendation to investors to support non-pre-emptive placings by listed companies of up to 20% of share capital on a case-by-case basis. (Announced 1 April 2020. Extended 4 September 2020)	Until 30 November 2020

The Modern Slavery Act 2015

Annual Report on Modern Slavery and review of the Modern Slavery Act 2015

Ongoing

The Modern Slavery Act 2015 (the "**Modern Slavery Act**") requires large businesses[1] to publish an annual statement outlining any steps such business has taken to prevent modern slavery in their operations and supply chains.

On 20 April 2020, the government published guidance for companies on how to approach their Modern Slavery Statements during the COVID-19 pandemic, and has made clear that businesses must continue to identify and address risks of modern slavery in their supply chains and operations. However businesses are permitted to delay publication of statements by up to six months if they can demonstrate COVID-19 related pressures (and provided they state the reason for the delay in the statement).

On 22 September 2020, the Government published its response to its 2019 *'Transparency in supply chains'* consultation. The Government's key proposals are:

- Implement mandatory reporting against each of the six areas listed in s. 54(5) of the Modern Slavery Act, namely:
  1. the organisation's structure, its business and its supply chains;
  2. the policies in relation to slavery and human trafficking;
  3. the due diligence processes in relation to slavery in its business and supply chains;
  4. parts of the business and supply chains where there is a risk of slavery and human trafficking and steps being taken to manage such risk;
  5. the effectiveness of measures put in place against relevant performance indicators; and
  6. the training concerning slavery and human trafficking available to the company's staff.
- Develop an online registry for Modern Slavery Statements where organisations will be encouraged to publish their Modern Slavery Statements once launched.
- Introduce a single reporting deadline of 30 September by which all organisations must publish their statement each year.

Next steps

- Consider whether you need to take advantage of flexibility and delay publishing the Modern Slavery Statement.
- Continue to review your company's modern slavery risk assessments, procedures and policies and bolster if necessary to ensure clear reporting lines and contents.
- Ensure that your company's Modern Slavery Statement is suitably detailed (considering all six areas listed under s. 54 of the Modern Slavery Act 2015) and is prominently displayed on the company website.
- If your company has reported that it has taken no steps to address modern slavery, consider how you will be impacted by a change in legislation and what steps you will need to take to comply.

Further information: Click **here** to access guidance for companies on how to approach their Modern Slavery Statements during the COVID-19 pandemic and **here** for the Government's response to the consultation from 2019.

1 Any body corporate or partnership, wherever formed or incorporated that (i) carries on a business (or part of a business) in the UK; (ii) supplies goods or services; (iii) with a minimum annual global turnover for it and its subsidiary undertakings of £36 million.

Corporate reporting: Non-financial reporting developments

The UK Government's policy on streamlined energy and carbon reporting ("**SECR**") has come into force, the EU Commission has announced a review of the Non-Financial Reporting Directive and the ICAEW has published guidance on non-financial reporting

November 2020, June 2020, March 2020

In April 2019, the SECR came into force, meaning that March year-end companies are the first to have to report under the SECR in annual reports. December year-end companies will have to include the necessary disclosures in their 2020 annual reports.

SECR will impact any companies (including all quoted companies of any size), LLPs and groups that exceed at least two of the three thresholds in the preceding financial year:

- £36 million annual turnover
- £18 million balance sheet total
- 250 employees

Quoted companies will have to report on their annual global greenhouse gas emissions of activities for which the company is responsible as well as underlying global energy use. Further, all companies will have to report:

- **Direct emissions:** the fuel use from transport (where the journey begins or ends in the UK) and combustion of natural gas;
- **Indirect emissions:** electricity purchased and used for operations;
- **Other indirect emissions:** energy use and related emissions from business travels in rental cars or employee-owned vehicles where the company purchases the fuel; and
- **Intensity metric for year-on-year:** tonnes of CO2 emissions per full-time employee.

Companies will also have to provide a supporting narrative which includes methodologies used within the calculation and energy efficiency actions taken. There is also a 'comply or explain' clause, which allows carbon and energy information to be excluded where it is not practical to obtain it, or that disclosure would be 'seriously prejudicial' to the interest of the organisation. A statement explaining what information has been omitted and why must be included and steps to fill gaps must be taken in the future.

In December 2019, as part of the European Green Deal, the European Commission published a consultation concerning an initiative to revise its non-financial reporting regime potentially involving changes to the Non-Financial Reporting Directive ("**NFRD**"). Since 2018, the NFRD has required large listed companies, banks and insurers to publically report information on a broad range of ESG matters on an annual basis.

The European Commission has identified a number of issues with the NFRD including:

- Inadequate availability of public information as to how non-financial and sustainability issues impact companies; in particular that: (i) currently reported non-financial information is not acceptably reliable or comparable; (ii) companies fail to report relevant information; (iii) some companies fail to report altogether; and (iv) non-financial information where reported is difficult to find.
- Companies are incurring unnecessary costs in deciding which information to report due to conflicting disclosure requirements.

Whilst the form of the initiative has not yet been decided, the Commission points to three options which will be analysed:

- Continuing the current approach of issuing non-binding guidelines to supplement the NFRD. This could entail revising the existing guidelines, or publishing new ones.
- Exploring the use of standards, including endorsing an existing set of standards.
- Revising and strengthening the NFRD through several possible means, including specifying in more detail the information companies are required to disclose, or strengthening the enforcement regime and promoting greater supervisory convergence.

If legal changes to the European Union regime only emerge after the end of the Brexit transition period, then it will be for the UK Government to decide whether to amend the existing non-financial reporting provisions in CA 2006 to reflect the aforementioned changes to the NFRD.

On 6 March 2020, the FCA published a consultation on its proposals to enhance climate-related disclosures by listed issuers and to clarify existing disclosure obligations. The new rule proposed by the FCA would require commercial companies with a UK premium listing to "comply or explain" if they have not complied with the recommendations of the Financial Stability Board's Taskforce on Climate-related Financial Disclosures ("**TCFD**").

The TCFD's final report sets out four overarching recommendations with 11 recommended disclosures which provide more granular detail on the information to be disclosed under each of the recommendations. The 4 overarching recommendations cover 4 thematic areas summarised below:

- **Governance:** disclose the organisation's governance around climate-related risks and opportunities.
- **Strategy:** disclose the actual and potential impacts of climate-related risks and opportunities on the organisation's businesses, strategy, and financial planning where such information is material.
- **Risk management:** disclose how the organisation identifies, assesses, and manages climate-related risks.
- **Metrics and targets:** disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.

The FCA's proposed rule would require commercial companies with a UK premium listing to include a statement in their annual financial report setting out whether they have made disclosures consistent with the TCFD's recommendations and recommended disclosures as described above, and where they have not (or have included in another document other than their financial report), an explanation why. The rule would also require details of where in the annual financial report the various disclosures can be found.

On 9 November, HM Treasury published a roadmap which sets out the UKs approach to introducing mandatory-climate related financial disclosures which are aligned to the TCFD requirements by 2025, with a significant portion of mandatory requirements in place by 2023. For premium listed companies, the roadmap envisages that TCFD-aligned disclosure rules will be included in the Listing Rules and notes that the FCA has already consulted on initial proposals for the rules. It is anticipated that premium listed companies will have to report against the TCFD-aligned disclosure rules for financial years starting on 1 January 2021.

On 22 June 2020, the Institute of Chartered Accountants ("**ICAEW**") issued a publication 'Non-financial reporting: ensuring a sustainable global recovery' discussing the need for improved reporting on environmental and social issues. The ICAEW is conscious that businesses need to improve reporting on social and environmental issues and recommends:

- The encouragement of all efforts to establish a single internationally recognised global framework for providing comparability and consistency for non-financial reporting; and
- That current moves to consolidate existing standards need to be accelerated and made more open and transparent.

Next steps

- Ensure you are able to comply with the additional SECR reporting requirements.
- Continue to monitor developments in this area and participate in any consultations to ensure your views are reflected.

Further information:

- Click **here** for the UK Government's streamlined energy and carbon reporting guidance
- Click **here** for the consultation note of the European Commission on Non-Financial Reporting
- Click **here** for the FCA's consultation paper on its proposals to enhance climate-relate disclosures
- Click **here** for ICAEW's report on non-financial reporting

Corporate reporting

FCA to delay implementation of European Single Electronic Format (“**ESEF**”) for annual reports

November 2020, July 2020

On 22 July 2020, the FCA launched a consultation to delay the mandatory ESEF requirements for annual financial reporting under the Transparency Directive by one year.

Under the rules implementing the ESEF requirements, issuers must publish their annual financial reports in the ESEF format from the start of 2021 for financial years beginning on or after 1 January 2020. This would require a significant amount of operational and management time for companies which are already dealing with the effects of the COVID-19 pandemic.

Instead, the FCA proposes that, under the FCA’s DTRs:

- the requirement for all issuers to publish their annual financial reports in XHTML web browser format, replacing the current PDF format, will be postponed to financial years starting on or after 1 January 2021, for publication from **1 January 2022**;
- the requirement for issuers who prepare consolidated annual financial statements in accordance with IFRS to tag basic financial information will be postponed to financial years starting on or after 1 January 2021, for publication from **1 January 2022**; and
- the requirement for issuers who prepare IFRS consolidated annual financial statements to tag notes to the financial statements will be postponed to financial years starting on or after 1 January 2023, for publication from **1 January 2024**.

Notwithstanding the above, the FCA continues to support the ESEF initiative, and issuers can choose to publish and file their annual financial reports voluntarily in the new ESEF if they wish.

The FCA also intends to continue with its programme of investment in the National Storage Mechanism to support the ESEF initiative.

Following the results of the July consultation, the FCA confirmed in a Policy Statement on 5 November 2020 that it will proceed with its proposal to delay the application of the ESEF. The requirement for all issuers to publish and file their annual financial reports in XHTML web browser format (rather than the current PDF format) will be delayed by one year, and will apply to financial years starting on or after 1 January 2021, for publication from 1 January 2022.

The timetable for the tagging of notes to the annual financial statements will not change, so the requirement for issuers who prepare IFRS consolidated annual financial statements to tag notes to the financial statements will apply to financial years starting on or after 1 January 2022, for publication from 1 January 2023.

Next steps

- Ensure you are prepared to publish in ESEF from 1 January 2022 and publish in ESEF from 1 January 2021 if you are already set up to do so.

Further information: Click **here** for a copy of the FCA’s consultation paper and **here** for a copy of the FCA’s Policy Statement.

Section 172 reporting

Updated guidance published on reporting of directors' s. 172 statement

October 2020, August 2020

On 25 August 2020, ICSA published updated guidance on directors' general duties under CA 2006, with a particular focus on s. 172 CA 2006 and the factors directors are required to take into account in their decision making process.

The guidance contains practical advice on the preparation of the s. 172 statement and what it should include, in general terms, as well as in relation to each specific factor under s. 172(1)(a) to (f). The guidance includes the following pointers as to what should be included:

- **long-term consequences of decisions:** information on how consequences have been taken into account in areas such as strategy and business plan;
- **interests of the company's employees:** more detailed disclosures, e.g. the composition of the workforce, how the company engages with its workforce and how the workforce contributes to the business;
- **relationships with suppliers, customers and others:** information on methods used to identify and engage with suppliers, customers and others to obtain their views, and the effect on principal decisions made by the board, on prompt payment to suppliers and on supply chain sustainability;
- **community and the environmental impact:** more detailed disclosures, including how the environmental impact of the company's operations is assessed, monitored and mitigated, the impact on the local community in which the company operates, and how the company communicates with its local community;
- **company reputation:** discussion of business conduct, values and culture, and how the company monitors and mitigates any reputational risks; and
- **acting fairly between members of the company:** discussion of how the company has achieved a balance between major investors and minority shareholders and how it has engaged with these stakeholders.

Deloitte have also published a survey of 25 s.172 statements to highlight emerging practice (the "**Survey**"). Some key elements of best practice were identified:

- All but one company posted a clearly identifiable statement with 80% including it in the strategic report as required.
- In most annual reports the statement was presented as a summary with cross-references to other relevant information. Cross-reference to the strategic report was considered helpful. Examples of reports with cross referencing include William Hill PLC (see page 12 of the Survey) and BP plc statements (see page 15 of the Survey).
- The majority of companies included examples of how they had considered the impact of the company's material decisions on the community, environment and other stakeholders and explained matters that may affect company performance. More insightful statements described how the board had considered trade-offs between different stakeholders, weighing up and evaluating the impacts upon each group.
- The environmental aspect was well addressed by some companies with detailed case-studies focusing on climate impact.
- A few companies made clear that engagement with stakeholders can take place both at the operational and board level. Examples of good practice drew out how the outcome of stakeholder engagement performed at an operational level was considered in the boardroom.

The Survey also identified areas where company reporting could have been improved:

- More than one-third of companies were less precise in cross-referencing their sections and in some cases pointed to whole sections of the strategic report. Companies should provide specific cross-references to sections of the report.
- Long-term consequences of decisions were often missed out of the statement or poorly explained.
- S. 172(1) requires consideration of the company's employees interests by the directors. The UK Corporate Governance Code however has a wider term of the "workforce" and goes beyond the definition of employees to include contractors – more than 50% of companies used this term interchangeably and did not explain clearly whether "workforce" included others in addition to "employees".
- The FRC highlighted reporting on payment to suppliers in October 2019. However, only 40% of companies mentioned supplier payment matters being considered in the s. 172 statement.

On 14 October 2020, the FRC Lab published a set of tips intended to help companies consider what content to include in a s. 172 statement, how to present it and how to facilitate the process of preparing the statement. The tips are classified under three headings. We have summarised the key points of each heading below:

- **building in useful content** – the statement should:
  - not merely be a compliance exercise but instead reflect on how the company met the requirements, explain what is relevant to it and what happened during the year and, where applicable, what the board and management plan to do in the future; and
  - explain the board's reasoning behind why, for example, particular stakeholders are identified as key and why particular engagement methods were effective.

- **presented in a way that makes sense** – the statement should:
  - reflect the strategic link and be clear about the board's role. Companies are also advised to think about where to place the statement so that it is positioned in the most helpful and useful position for investors and logically flows to other information in the strategic report;
  - be clearly labelled and referred to in the contents page of the annual report; and
  - include examples and case-studies of significant strategic decisions taking during the year, explaining how stakeholders were taken into account to bring the statement to life.
- **supported by process** – companies should:
  - start considering their s. 172 statements early in the year and not leave considerations until the end of the year; and
  - consider tailoring board agendas, papers and minutes to include reminders for both the board and management to consider which stakeholders are relevant for decisions.

Next steps

- Consider reviewing the best practice guidelines and the FRC Lab's guidance on drafting the s. 172 statement for next year.
- Review ICSA's updated guidance on directors' general duties under CA 2006.

Further information:

- Click **here** for a copy of FRC Lab's tips on preparing s. 172 statements
- Click **here** for a copy of Deloitte's Briefing Statement
- Click **here** for a copy of Deloitte's Survey on the s. 172 statement
- Click **here** for a copy of ICSA's updated guidance on Directors' general duties under CA 2006

Corporate transparency and register reform

The UK Government has announced wide-ranging reform of its official register of company information

September 2020

On 18 September 2020, the Department for Business, Energy and Industrial Strategy ("**BEIS**") published the Government's response to its consultation on options to enhance the role of Companies House and to increase the transparency of UK Corporate entities to address fraud and money laundering. These issues have been brought into the spotlight following the leak of the FinCEN files. Directors, for example will not be able to be appointed until Companies House has verified their identity. The changes aim to:

- increase the reliability of the data showing who is behind each company so that businesses have greater assurance when they are entering into transactions with other companies; and
- improve the ability of law enforcement agencies (such as the National Crime Agency) to trace activity for suspected fraud or money laundering. Identity verification will take place through a fast, efficient, digital process and is expected to take a matter of minutes.

These reforms should not affect the typical speed at which a company is formed and other filings are completed. Most companies should still be able to be incorporated within 24 hours. To facilitate the new identity verification requirement, Companies House announced that it intends to develop a 24/7 digital verification process to prevent any delays in incorporations and filing.

Additional measures that the government has proposed include:

- compulsory identification for PSCs, general partners in limited partnerships, designated members in LLPs, and all individuals who file information on behalf of a company (e.g. company secretary), in addition to directors;
- only permitting supervised agents to file information on behalf of a company, and requiring evidence of their verification;
- increasing the Registrar's power to allow queries of information submitted to Companies House;
- giving Companies House the power to query and possibly reject company names prior to registration; and
- reforming how and under what circumstances Companies House will issue certificates of good standing.

Key points of reform:

- The proposals will require a significant level of legislative changes as well as changes to Companies House's systems and processes.
- Companies House will be given greater powers to query, investigate and remove inaccurate information.

Further information: Click **here** for the Government's press release in relation to the Companies House reforms and **here** for the complete Government response.

FRC Annual Enforcement Review

FRC publishes second Annual Enforcement Review

August 2020

The FRC has published its second Annual Enforcement Review ("**AER**"). This report follows on from the FRC's debut review, published last year, and is intended to provide a baseline for measuring future enforcement performance as the FRC transitions into the Audit, Reporting and Governance Authority ("**ARGA**"). The key points to note from the AER are as follows:

- Fourteen investigations have been opened this year into auditors, accountants and/or actuaries and £16.5 million worth of financial sanctions have been imposed (before settlement discount). This is a significant reduction in the financial sanctions figure for 2018/2019 (£42.9 million), reflecting improved co-operation and earlier settlement by firms.
- There has been a 14% growth in personnel in the Enforcement Division over the past year, following a 25% increase in 2019.
- There has been an 80% increase in matters identified through horizon-scanning activities. It appears that most cases are generated from horizon scanning activities – namely, searches of RNS updates and review of reports in the financial press. For this reason increased care is needed as to the content of any announcements.

The FRC notes that they give careful consideration to the impact of COVID-19 on the audit market before deciding whether to make further enquiries in order to ensure that the FRC's actions are proportionate and risk-based. In relation to errors in a set of financial statements, the FRC states that they focus on those which would be likely to have a real impact on decisions taken by users of financial statements. For example, marginal errors or errors in highly technical areas of financial statements are unlikely to be of fundamental importance to the measurement of the "underlying financial performance of the entity".

The FRC notes its disappointment that the overall response to last year's Review message that firms should "identify, remediate and report" has been mixed. The AER discusses a number of key themes seeking to address why audit quality review and enforcement seem to be deficient, ranging from over-delegation to junior members to the auditor being too close to management.

Next steps

- Take increased care when preparing RIS announcements and press releases in light of the FRC's increased focus on the review of public information to ensure consistency with previous releases and the accuracy of disclosures.
- The Audit Committee, Finance team and those responsible for preparing the annual report and accounts should be aware of the increased scrutiny surrounding financial reporting and ensure sufficiently robust processes are in place to ensure the accuracy of financial disclosures.
- In light of COVID-19, those preparing the annual report and accounts should be particularly cautious of:
  - the pressure to report unreasonably positive results;
  - the need to obtain proper evidence of procedures undertaken by auditors; and
  - the difficulty in obtaining appropriate audit evidence in light of any current or future restrictions on travel and movement.

Further information: Click **here** for the FRC Annual Enforcement Review.

Financial reporting updates

FRC's Financial Reporting Lab ("**FRC Lab**") publishes Q2 newsletter

July 2020

On 22 July 2020, the FRC Lab published updates on its current projects. The key projects are as follows:

- **Reporting in Times of Uncertainty:** In light of the COVID-19 pandemic, the FRC Lab has issued two reports in relation to reporting in times of uncertainty. Following discussions with a number of individual investors and investor groups, the aim of the reports is to provide guidance and examples of the information sought by investors in a time of financial instability.
- **Reporting on stakeholders and s. 172 statements:** The FRC Lab has issued a Call for Participants for a new project on corporate disclosures of stakeholders. The project will consider the usefulness to investors of disclosures about stakeholders and will focus on the opportunity for companies to provide such information in the s. 172 statement. The FRC Lab published its findings and tips on 14 October 2020 to help companies consider what content to include in preparing s. 172 statements (see briefing on Section 172 reporting).
- **Climate change thematic:** The FRC Lab is coordinating a thematic project to highlight some of the FRC's work in reviewing how companies and auditors assess and report on the impact of climate change. The aim of this project is to put a spotlight on what boards, companies and auditors are/should be doing to consider and report on the climate-related issues they face.
- **October 2019 climate-related corporate reporting paper:** The FRC Lab is taking part in a wider FRC project on climate change in 2020, with companies being required to consider climate change in their financial statements. The International Accounting Standards Board ("**IASB**") has recently issued a briefing paper "In Brief" on IFRS Standards and climate-related risk disclosures. This centres on how to gauge the materiality of these risks.
- **Workforce-related corporate reporting paper:** The FRC Lab's workforce report was released in January. There is a move to companies being required to consider the workforce as a strategic asset. The report recommends that companies include some approved metrics (e.g. engagement scores and turnover), information on workforce composition, and a statement of how the board considers and assesses workforce matters.
- **European Single Electronic Format ("ESEF"):** The FRC Lab is continuing to monitor developments in the European single electronic format. This is the format based on which issuers on EU regulated markets have been required to prepare their annual financial reports for financial years beginning on or after 1 January 2020 (subject to the FCA's proposal to defer this obligation under its rules – see briefing on Corporate Reporting and our client alert on **AGM Insights**). The FRC Lab has been engaging with companies and service providers regarding the opportunities and barriers to effective digital reporting, and conducted a survey on how well-prepared companies were for the regulations.

Next steps

- Companies should continue to monitor developments with regard to climate change reporting and keep a watch on the FRC Lab's areas of focus.

Further information:

- Click **here** for a copy of the FRC Lab's report on Reporting in Times of Uncertainty
- Click **here** for a copy of the FRC Lab's Q2 2020 newsletter
- Click **here** for a summary of the survey conducted by the FRC Lab regarding ESEF.
- Click **here** for the FRC Lab's Workforce-related corporate reporting report
- Click **here** for a copy of the FRC Lab's October Climate-related corporate reporting paper.
- Click **here** for a copy of the IASB's "In Brief" briefing paper on IFRS Standards and climate risk disclosures.

The Corporate and Insolvency Governance Act 2020

The UK Government published legislation introducing temporary relaxations for companies to hold meetings during the COVID-19 pandemic

June 2020

On 26 June 2020, the Corporate and Insolvency Governance Act ("**CIGA**") came into force after fast progression through Parliament. CIGA includes a number of provisions in relation to the holding of meetings of companies as well as insolvency and restructuring (for more details on the restructuring aspects of CIGA, see our separate Client Alert **here**). CIGA was amended on 29 September 2020 with the effect that the following provisions apply until 30 December 2020. The key changes in relation to corporate governance and what they mean in practice are summarised below:

CIGA	Impact
Place: The meeting need not be held at any particular place.	This provision removes the need for a venue to be stated and, for the time being, has the effect of removing any doubt about the legality of virtual meetings.
Virtual meeting: The meeting may be held, and any votes may be permitted to be cast, by electronic means or any other means.	This provision permits a wide range of options, including virtual meetings and hybrid meetings.
Quorum: The meeting may be held without any number of those participating in the meeting being together at the same place.	This provision removes the requirement for a quorum to be together in one place.
Participation: A member of the qualifying body does not have a right: – to attend the meeting in person; – to participate in the meeting other than by voting; or – to vote by particular means.	This provision establishes that meetings can be held electronically and behind closed doors. This provision establishes that the only right a member has in relation to a meeting is to vote and that there is no right to attend to vote in person.
Articles: The provisions of any previous enactment relating to meetings and the provisions of the constitution or rules of the qualifying body are subject to the rules of CIGA.	CIGA is intended to override any conflicting provision in legislation, regulation or a qualifying body's own constitution, including its articles of association.

In addition to the above changes in relation to the arrangements for the holding of meetings, CIGA provides for additional changes including extended timelines for certain corporate actions:

Extension for holding AGM: There is an extension of the time period for companies to hold their AGMs, until 30 December 2020. This applies where the AGM was due to be held during a period ending between 26 March and 30 December 2020.

Other Companies House filings: The Secretary of State is granted the power to extend the deadline for certain common Companies House filing requirements, including the filing of confirmation statements, charges, accounts, and event-driven filings, such as changes in directors or persons with significant control. This power to extend is to last until 5 April 2021. The new deadlines must not exceed:

- Forty-two days, for existing deadlines of 21 days or fewer
- Twelve months, for existing deadlines of three, six or nine months

Retrospective effect: The above measures have retrospective effect from 26 March 2020, with the effect that where a company has already held its AGM in a way that adheres to social distancing measures but is not in accordance with its constitutional documents, it will be deemed to have been held in accordance with the law. CIGA, as extended, applies until the period ending on 30 December 2020, during which these changes would apply.

Next steps

- Publicly listed companies should consider now what changes they want to make for next year. Companies need to consider whether they want to hold a physical meeting (e.g. a meeting behind closed doors at the company's head office with only a quorum of directors present), a virtual meeting (a meeting taking place electronically with the quorum being met by virtual attendance) or a hybrid meeting (a physical meeting with a quorum of directors, with an element of formal electronic participation).
- It is expected that both AGMs and GMs will continue to be impacted by COVID-19, and while shareholders and proxy advisers have been flexible this year (particularly around the lack of shareholder engagement), this may not be the case next year as companies will have had time to put in place appropriate arrangements to ensure that there is sufficient shareholder engagement.
- Companies must consider the extent to which they want shareholders to be able to participate in the meeting. Companies may wish to provide conference lines/webcast facilities to enable shareholders to follow proceedings, or provide a mechanic for questions to be submitted and answered either at the AGM, or promptly after.
- While CIGA may be extended into 2021, companies may wish take advantage of CIGA to convene a shareholder meeting before then to update their articles of association to allow for the holding of hybrid and/or virtual shareholder meetings and the postponement of shareholder meetings as required.

Virtual execution and e-signature

Law Society publishes its position on the use of virtual execution and e-signatures during the COVID-19 pandemic

June 2020

On 18 June 2020, the Law Society published its updated position on the use of virtual execution and e-signatures during the COVID-19 pandemic. This provides further clarity for lawyers and clients on virtual signing which has become common place as a result of the pandemic.

The practice note provides the following guidelines for practitioners and companies:

- **Companies should agree on management of the transaction:** Companies should speak to lawyers on the other side of any transaction to ensure there is consensus on how to manage the transaction and its signing.
- **Verification of identity:** Additional steps will have to be taken to verify the identity of the person signing the document but this depends on common practice in the relevant area or specific regulatory requirements. Where the authenticity of the signature and identity of the signatory cannot be assumed, the Law Society suggests the use of video or photographic evidence as an additional and objective source of verification. Another suggestion is to use a live recording which is then shared with all parties.
- **Evidence:** Ensuring that the evidence of signing is accessible – this may include taking screenshots if the evidence cannot be saved directly onto the system.
- **Report:** Reporting to all parties that the transaction has closed.

It is also important to note that when **executing deeds**, even if performed electronically, a witness must be physically present when the deed is executed. When operating on the extremities of what may reasonably constitute presence, evidence such as a video recording should be collected.

Next steps

- Inform relevant signatories of any documents of the updated guidance and agreed procedures for e-signatures.
- Consider whether your signing policies need to be updated and your signatories briefed on the changes.

Further information: Click **here** for a copy of the Law Society's practice note on electronic signatures (requires login)

Senior Managers and Certification Regime extension

Extension to FCA solo-regulated firms take effect

June 2020

The Senior Managers & Certification Regime ("**SM&CR**") has been extended to FCA solo-regulated firms with effect from 9 December 2019. It also applies to branches of non-UK firms with permission to carry out regulated activities.

The SM&CR has replaced the approved persons regime for most businesses (excluding appointed representatives).

The FCA has noted that:

- All relevant staff must be trained on the FCA's Conduct Rules and how they apply to their role.
- A company must ensure that all staff in certified roles are fit and proper to perform the role and, where appropriate, issued with a certificate.
- Information must be submitted to the FCA for the directory of key people working in financial services.
- Businesses must ensure that they retain records of disciplinary and fit and proper findings.

The deadline for solo-regulated firms to have undertaken the first assessment of the fitness and propriety of their Certified Persons has been extended from 9 December 2020 to 31 March 2021. The Conduct Rules will now also come into force on 31 March 2021, rather than 9 December 2020 as originally planned.

These extensions are to give firms significantly affected by the COVID-19 pandemic time to make the changes they need.

Date	
9 December 2019	SM&CR for solo-regulated firms begins
31 March 2021	Conduct Rules apply to all staff
	Initial Certification assessments completed and certificates issued

The FCA's view, however, is that the majority of firms will not need to use the above extensions and it encourages firms that can complete certification assessments, conduct rules training and directory persons reporting by 9 December 2020, to do so, provided that this does not compromise the quality of their assessments or training.

Next steps

- Regulated firms to update systems, policies and procedures to reflect SM&CR regime.
- Board and Nomination Committee to be made aware of changes to the NED appointment process and requirement to make fitness and proper assessment (not certification) and the factors it considers when assessing people as fit and proper, which include honesty, integrity, competency and capability.

Further information: Click **here** for further information from the FCA on the SM&CR for solo regulated firms and **here** for the Guide for FCA solo-regulated firms.

International Corporate Governance Network ("ICGN") developments

The ICGN published a number of viewpoints and updated guidance in relation to corporate governance issues in light of COVID-19

April 2020 – July 2020

In April 2020, the ICGN published a letter of governance priorities during the COVID-19 pandemic to corporate leaders encouraging leaders to submit to the ICGN Statement of Shared Governance Responsibilities which emphasises the need for companies to:

- Prioritise employee safety and welfare whilst meeting short-term liquidity requirements
- Pursue a long-term view on social responsibility, fairness and sustainable value creation
- Take a holistic and equitable decision to capital allocation decisions
- Communicate comprehensively with all stakeholders

In June 2020, the ICGN published guidance on Executive Remuneration and COVID-19. The guidance encourages companies to focus on the following key issues:

- **Quantum**: maintaining or increasing executive pay where companies are forced to lay off staff or operate with pay cuts could threaten stakeholders' trust and motivation as well as the company's social license to operate. Traditionally investors have focused less on quantum and more on remuneration policies that link pay and performance; however, as a result of COVID-19, investors are now more alive to the issue of quantum.
- **Structures and metrics to guide long-term incentives**: the ICGN emphasises the use of ESG metrics to guide board and investor assessment of long-term performance and sustainable value creation. It notes that it is important to incorporate sustainability-related performance factors that the executive team can be held accountable for and directly influence and look beyond COVID-19.
- **Employees, stakeholders and managing sustainably though the crisis:** the ICGN encourages companies to: stay focused on long-term vision; focus on sustainability issues including working on a strong corporate culture and good relations with local communities; take responsibility for fair treatment of employees and customers; keep staff up to date on how the crisis is affecting the business; and commit to continue providing fair contracts and working conditions.

Further, in July 2020, the ICGN published its Viewpoint on the Board of Directors and Climate Change. The ICGN points out that in practice, despite the rising demands of investors regarding board governance of climate change, few boards can claim to be approaching the subject with the professionalism that they do other core board functions. The ICGN recommends that boards adhere to the World Economic Forum's Climate Governance Initiative which sets out standards for boards to adopt. They are:

- Climate accountability on boards
- Command of the subject through training and education
- Board structure, i.e. whether to seek out non-executive directors with special climate expertise
- Material risk and opportunity assessments to incorporate climate change risks
- Strategic integration to ensure that the company's strategic planning incorporates a 10 – 30 year road map
- Incentivisation to ensure the remuneration policy incorporates the company's long-term climate strategy
- Reporting and disclosure of the plan to achieve net-zero carbon emissions by 2050
- The role of non-executive directors engaging with external stakeholders

The ICGN has also published an update to its ICGN's Statement Guidance on Anti-Corruption Practices. The guidance provides detail on how companies can combat corruption internally through transparency and practices. The latest version of the guidance delineates more clearly between bribery and corruption, which are different terms. Corruption is broader in scope than bribery and the ICGN's approach to anti-corruption includes corruption in areas that are not necessarily illegal. Political donations and lobbying are examples of legal grey areas.

Next steps

- Inform the Board of the ICGN's Statement of Shared Governance Responsibilities and consider signature
- Review remuneration practices to comply with ICGN guidelines
- Consider compliance with the World Economic Forum's Climate Governance Initiative principles
- Familiarise the Board with the updated ICGN guidance

Further information:

- Click **here** for a copy of the ICGN's Guidance on Anti-Corruption Practices
- Click **here** for a copy of ICGN's Statement of Shared Governance Responsibilities
- Click **here** for a copy of the ICGN's Viewpoint on COVID-19 and Executive Remuneration
- Click **here** for a copy of the ICGN's viewpoint on Board of Directors and Climate Change

Executive remuneration

The Investment Association published guidelines for Executive Remuneration for UK listed companies

April 2020

On 27 April 2020, the Investment Association ("**IA**") published new guidelines for remuneration committees to help them navigate difficult decisions on executive pay during the COVID-19 pandemic.

The guidance asks remuneration committees to "sensitively balance" the need to incentivise executives whilst being mindful of the effect of the pandemic on shareholders, employees and other stakeholders. The key points from the guidance are:

- **Adjusting bonus outcomes for FY2019**: Where dividend payments are suspended or cancelled, members expect Boards and Remuneration Committees to consider how this should be reflected in executive pay – either through downward discretion in the bonus pay-out (where payments have not yet been made), or through downward adjustment of deferred bonuses.
- **Adjusting performance conditions**: The IA does not generally expect remuneration committees to adjust performance conditions for the impact of COVID-19. However, the IA notes that where company performance and shareholder experience is not commensurate with executive pay the use of discretion may be appropriate.
- **Windfall gains**: For companies who already granted awards in 2020 and where such awards have been based on a lower share price, no adjustment is needed to Long-Term Incentive Plans ("**LTIPs**") if the share price fall is solely related to COVID-19. However, the IA advises that remuneration committees need to look at the market and share price response during the performance period to ensure that windfall gains do not arise when awards vest. Shareholders will expect the Committee to use their discretion to reduce vesting outcomes where windfall gains have been received.
- **Setting performance conditions and grant levels**: Committees should be considering if it is appropriate to make LTIP grants and whether, given the current market environment it might be more appropriate to postpone the current LTIP grant. There are a number of options depending on the individual circumstances of the company:
  - Granting awards as normal and setting grant size and performance conditions now;
  - Granting awards as normal and setting grant size now, but delay setting performance conditions for up to six months;
  - Delaying awards for up to six months of the normal grant date. Companies should explain the approach taken to shareholders and use discretionary powers to adjust pay to ensure they reflect company and executive performance as well as shareholder and stakeholder experience; or
  - Companies should be careful not to isolate executives from the impact of COVID-19 in a manner that is inconsistent with the approach taken to employees.
- **Adjusting pay outcomes for companies furloughing employees or seeking additional capital**: Where a company has sought to raise additional capital from shareholders, or has required Government support, shareholders would expect this to be reflected in the executives' remuneration outcomes. Failure to be mindful of the wider employee context may have significant reputational ramifications.
- **New remuneration policies**: Companies who are due a new remuneration policy should carry on as planned. The IA does not expect companies to re-write policies but companies should be mindful of the current environment when deciding whether to increase pay.

Next steps

- Remuneration Committee to be aware of the IA's guidelines.
- Remuneration Committee must strike a "sensitive balance" between executive pay and the performance of the company.

Further information: Click **here** for a copy of the IA's guidelines

Institute of Directors' ("IoD") new Centre for Corporate Governance

The IoD has launched a new initiative – the IoD Centre for Corporate Governance

March 2020

In March 2020 the IoD announced the launch of the Centre for Corporate Governance, which will operate at arm's length from the IoD and be guided by an independent advisory board of academics, business leaders and investors. The centre was officially launched at an online event on 30 June 2020. The Centre will act as a hub for discussion of corporate governance and ESG governance issues and will commission and steer research into issues faced by boardrooms.

Members of the advisory board include: Dame Inga Beale, former chief executive at Lloyd's of London; Margaret Casely-Hayford, chair of Shakespeare's Globe Theatre; Andrew Kakabadse, professor of governance and leadership at Henley Business School; and Colin Mayer, professor of management studies at Saïd Business School, Oxford.

Initially the centre will focus on three key topics of study:

- **Stakeholder governance**: examining whether existing corporate governance mechanisms and statutory obligations will allow directors to deliver on expectations of a wider group of stakeholders.
- **Sustainable capitalism**: addressing the feasibility of the UK's objective of a carbon neutral economy by 2050 within the UK's corporate governance framework.
- **Governance implications of AI and emerging technology**: exploring the issues which are likely to arise as corporate decision making becomes increasingly subject to emerging technologies. As AI develops further, it may replace more and more corporate functions.

It is reported that new working groups on other key governance and ESG issues will be established as the centre progresses.

Next steps

- Inform Board of the work of the new Centre for Corporate Governance and consider participating in its discussions.

Further information:

- Click **here** for a copy of the IoD's March press release.
- Click **here** for a copy of the IoD's June press release.

Audit market and corporate reporting

Over the past two years, the Government has commissioned a number of reviews and studies to comprehensively review and update the regulatory framework for audit and corporate reporting. The final reports for each of these reviews have now been published. It is expected that at some point in the coming months, the Government will propose actions to implement audit reforms following consideration of the recommendations from each of these reviews.

On 6 July 2020, the FRC announced its principles for operational separation of the audit practices of the 'Big Four' firms.

- The announcement contains a 22-point plan for structural overhaul and each firm was required to outline how they plan to implement it by the end of October 2020.
- The aim is to improve the quality and effectiveness of corporate reporting and audit in the UK such that it is in the public interest and works for the benefit of shareholders.
- Sir Donald Brydon has now also called on the government to accelerate an overhaul of the sector in the wake of the Wirecard scandal.

Review	Purpose	Status
Independent Review into the Quality and Effectiveness of Audit by Sir Donald Brydon: **Brydon Review**	□ To ascertain what the standards and requirements should be for the UK audit profession in the future □ To provide recommendations as to what more can be done to ensure audits meet public, shareholder and investor expectations	□ Final report published on 18 December 2019
Independent Review of the Financial Reporting Council by Sir John Kingman: **Kingman Review**	□ Independent root and branch review of the FRC	□ Final report published on 18 December 2018 □ Initial government consultation published on 11 March 2019
The Competition and Markets Authority ("**CMA**") market study on the statutory audit market: **CMA Market Study**	□ To address competition problems in the UK audit industry	□ Market study launched in October 2018 □ Update paper published on 18 December 2018 regarding market study of the statutory audit market □ CMA published its final report on 18 April 2019, taking into account recommendations of the Kingman Review □ In July 2019 BEIS issued a consultation on the CMA recommendations
BEIS Select Committee of the House of Commons inquiry on the future of audit: **BEIS Review**	□ Focused on the impact of the CMA market study of the audit sector and the Kingman Review	□ 12 November 2018 – BEIS Committee launched the future of audit enquiry and published its terms of reference □ 2 April 2019 – BEIS Committee published its report □ 7 June 2019 – BEIS published its response □ 19 December 2019 – The Queens' Speech set out the government's proposals to develop a stronger regulator with powers to reform the corporate reporting and audit sector

2 See announcement on operational separation here.

Brydon Review

December 2019

The final report of the independent review by Sir Donald Brydon was published on 18 December 2019. The report contains a substantial number of recommendations which the report recommends should be taken together to stimulate improved quality and effectiveness of audit in the UK. The recommendations are collectively aimed at improving audit and assurance in relation to Public Interest Entities[3] within the FTSE 350.

The report contains a substantial number of recommendations, including:

- **A redefinition of audit and its purpose:** The report notes that the definition of the purpose of audit should reflect its role as a public interest function that demonstrates more than just compliance with laws and rules.
- **The creation of a corporate auditing profession:**
  - Brydon recommends that the audit profession should be distinct from that of accounting and be governed by its own governing principles (The Principles of Corporate Auditing), qualifications and standards.
  - Brydon also recommends that ARGA should be the statutory regulator and should develop a coherent framework for corporate audit that includes the statutory audit of financial statements.
- **Mechanisms to encourage greater engagement of shareholders with audit and auditors**: A number of recommendations are made, aimed at enabling and encouraging a company's shareholders to influence the scope of the audit and to hold the Audit Committee and auditor to account, including:
  - a formal process in which the shareholders are given an opportunity to propose any matters they wish to be covered in the audit.
  - a standing item on audit at the company's general meeting to permit questioning of the Audit Committee Chair and the auditor.
- **A change to the language of the opinion given by auditors:** Brydon recommends replacing "true and fair" with "present fairly, in all material respects" as a descriptor of financial reporting given that corporate accounting increasingly involves the use of estimates and judgements.
- **Introduction of (i) a corporate Audit and Assurance Policy, (ii) a Resilience Statement, and (iii) a Public Interest Statement:** To help frame the role of the auditors and make clearer the extent of all assurance in regard to information they communicate. It is recommended that the directors publish:
  - their **statement of principal risks and uncertainties** before determining the scope of each year's audit and actively seek shareholder and other views on the appropriate emphasis;
  - a **Resilience Statement** that would replace the current Going Concern and Viability Statements. The Resilience Statement will incorporate a going concern opinion for the short term, a statement of resilience in the medium term and a consideration of the risk to resilience in the long term; and
  - a **Public Interest Statement** that explains the company's view of its obligations to the public interest, whether arising from statutory, self-determined or other obligations and how the company has acted to meet this public interest over the previous years.
- **Other stakeholders:** Brydon notes that the statutory audit report provides independent professional insight into the company's financial position and is of great relevance to other stakeholders. He therefore recommends certain steps to be taken to reflect those wider interests, namely that:
  - the Principles of Corporate Auditing should include a statement that auditors act in the public interest and have regard to the interests of the users of their report beyond solely those of shareholders;
  - the audit report should also include a new section in which the auditor states whether the director's s. 172 statement is based on observed reality, on the basis of the auditor's knowledge of the company and its processes;
  - the directors should actively seek the views of employees regarding the scope of any audit activity and report back to them on how their views have been taken into account;
  - with regards to whistleblowing, the statutory auditor should be added to the list of "prescribed persons" under the Public Interest Disclosure Act 1998, thereby allowing employees to legitimately raise concerns with the statutory auditor; and
  - disclosures on supplier payment performance should be brought into the annual report.
- **Fraud:** Brydon suggests a package of recommendations aimed at raising the prominence and transparency of fraud prevention and detection by both directors and auditors. This includes a reporting duty on directors to set out the actions they have taken each year to prevent and detect material fraud and a duty on directors to state how they have assessed this statement.
- **Auditor Transparency:** Several recommendations are made for increasing transparency, including:
  - audit firms to ensure a clear separation between the team that negotiates the audit fees, and the team that carries out the audit(s);

3 For existing UK regulatory purposes, Public Interest Entities include UK companies with equities or debt admitted to trading on a regulated market (including the London Main Market but not the Alternative Investment Market) and credit and insurance firms

- audit firms to be required to publish the profitability of their work from audit, the remuneration of their Senior Statutory Auditors and the attendant performance measures around that remuneration;
- auditors to disclose, within the audit report, the hours spent on each audit by each grade within the audit team;
- clear reasons to be given for any resignation, dismissal or decision not to participate in a retender; and
- auditors and companies to answer relevant questions in a general meeting.

- **Internal controls:** Kingman's recommendation regarding the **establishment of ARGA** is fully supported, as well as the recommendation that consideration be given to **strengthening the framework for internal controls reporting**. It is therefore recommended that the CEO and CFO provide an annual attestation to the board as to the effectiveness of the company's internal controls over financial reporting, with disclosure required when there is a material failure to internal controls. Any failure would lead to the attestation being subject to audit for the following three reporting years.
  - **Technology:** BEIS and ARGA to work with auditors to create the necessary protections and policies for audit to be able to use data from the companies they audit in order to promote better quality audits.
  - **Auditor Liability:** Company law to be amended to provide that any use of Liability Limitation Agreements by company boards, proposed in good faith, does not represent a breach of directors' responsibilities.
  - **APMs and KPIs:** Any Alternative Performance Measures reported by a company and any use of Key Performance Indicators to underpin executive remuneration should be subject to audit.

Next steps

- 'Big Four' to outline how they plan to implement 22-point plan for operational separation by end of October, with four years to put the plan into effect.
- Audit Committee to monitor developments and be ready to adapt to legislative changes.
- Brydon suggests that a follow-up review takes place in 2025 to assess how recommendations in the Brydon Report, those of Sir John Kingman and those of the Competition and Market Authority's report have been implemented.

Further information: Click **here** to access a copy of the final Brydon Report.

Kingman Review

March 2019, December 2018

The Kingman Review's proposals from December 2018, are extensive (83 recommendations) and wide-ranging, including:

- **Replacement of the FRC as soon as possible with an independent regulator** reporting directly to Parliament with the Chair and Chief Executive subject to a pre-approval hearing with the BEIS Select Committee.
- The new regulator (ARGA) corporate reporting review work should extend to cover the entire annual report (including corporate governance statement).
- The new regulator (ARGA) should be given extensive **new powers**, e.g. to direct changes to accounts without having to go to court and to direct the removal of an auditor.
- The government should **review and possibly extend the definition of a "public interest entity"**.
- Corporate governance requirements such as viability **statements** and the **UK Stewardship Code** should be **fundamentally reformed or possibly abolished**.
- The new regulator (ARGA) should promote the **interests of consumers** of financial regulation.
- BEIS officially announced on 11 March 2019 that a new regulator, ARGA, would replace the FRC as the new audit regulator following the Kingman Review recommendations. The same date, BEIS published the government's consultation paper on the recommendations.

Next steps

- Response papers published by CLLS and the Law Society, IA and ICSA.
- Audit Committee to monitor developments.
- Consider including status update in Board and Audit Committee Corporate Governance briefings.

Further information: Click **here** to access a copy of the Kingman Review.

Competition and Markets Authority ("**CMA**") audit market study

April 2019

The audit sector has come under increasing scrutiny following the collapse of BHS and Carillion in 2016 and 2018, respectively, and more recently Patisserie Valerie and Wirecard.

In October 2018, the CMA launched a market study into statutory audit which identified inter alia the following contributing factors to a fall in audit quality:

- **Choice**: The dominance of the Big Four.
- **Long-term resilience of the sector**: The fact that the Big Four are "too few to fail".
- **Incentives**: Between audited companies, audit firms and investors (in particular, the fact that companies pick their own auditor).

In the CMA's "update paper" of December 2018, the following possible remedies were proposed:

- Legislation to **separate** audit from consulting services.
- "Measures" to increase audit chair **accountability/scrutiny** of auditor appointment.
- A "**joint audit**" regime whereby at least two firms (one of which must be outside the Big Four) have responsibility for auditing the UK's biggest companies.
- A **market share cap** on the Big Four's access to major audit contracts.

In April 2019, the CMA published its final report on the UK audit industry with the following key recommendations:

- **Regulation of UK companies' audit committees**: Audit committees should come under greater scrutiny by ARGA with the power to mandate minimum standards, request information from audit committees, appoint an observer and issue public reprimands.
- **Operational split of audit and non-audit practices**: Requiring separate management, accounts and remuneration and an end to profit-sharing between audit and consultancy.
- **Mandatory joint audits**: to increase the capacity of challenger firms to the Big Four. Challenger firms would work alongside the Big Four and be jointly liable for the result to increase choice in the market.
- A **five-year review** of progress by the regulator.

In July 2019, the government published an initial consultation on the recommendations made by the CMA in its final report, in which it:

- agrees with the CMA that there should be clear expectations and standards for audit committees to ensure that they deliver the best results for shareholders, and that there should be a role in this for the new regulator that will replace the Financial Reporting Council;
- recognises the importance of providing meaningful and effective competition and choice for audit clients in the statutory audit market;
- agrees that there is more that the regulator could do to monitor and act on the health of audit firms and is keen to implement a monitoring function that can support the market in an effective and competitive way; and
- recognises the high risk of actual and perceived conflicts of interest that can occur where audit firms provide non-audit services to their audit clients and is determined to identify and implement a powerful and proportionate package of measures to increase choice and capacity in the audit market.

The government sought responses to certain aspects of its initial consultation by 13 September 2019 and is still to publish its responses.

Next steps

- Audit Committee to monitor developments.
- Consider including status update in Board and Audit Committee Corporate Governance briefings.

Further information: Click **here** to access a copy of the final CMA Report (April 2019).

BEIS Committee Report on the Future of Audit

March 2020, April 2019

In March 2020, the BEIS Committee launched a follow-up inquiry on delivering audit reform.

The aim is to map out a path for implementing meaningful reform of the UK's audit industry, following a series of inquiries from the BEIS Committee, the CMA, Sir Donald Brydon and Sir John Kingman.

Oral evidence will be taken from stakeholders in an attempt to determine how serious reform can be delivered.

In April 2019, the BEIS Committee published a report setting out recommendations for audit reform, which includes the following:

- detection of fraud should be a priority within an audit;
- scope of audit should cover the entire annual report;
- the auditor should be required to present at the AGM in order to generate shareholder engagement;
- CMA should aim for a structural split or, at the very least, an operational split between audit and non-audit businesses and if operational separation does not produce improvements, there should be a full structural break-up of the Big Four into audit and non-audit businesses;
- independent appointment of auditors should be considered if audit quality, choice and resilience remain a problem;
- More power given to the FRC (and its proposed successor ARGA) over audit fees; and
- reduced audit rotations to seven-year, non-renewable terms.

The government issued its formal response to the Report in June 2019, welcoming the proposals, but noting that it would be waiting for Sir Donald Brydon's report before considering what action to take.

Next steps

- Response papers published by CLLS and the Law Society, IA and ICSA.
- Audit Committee to monitor developments.
- Consider including status update in Board and Audit Committee Corporate Governance briefings.

Further information: Click **here** for a copy of the BEIS Committee Report.

4 See announcement for follow-up inquiry here.

Governance in the news

"EG Group's bonds fall after auditor's abrupt resignation" (15 October 2020):

The FT reported on Wednesday that Deloitte had abruptly resigned as the petrol station group's auditor because of concerns over its governance and internal controls, citing four people brief on the matter. The company has no external board members, and delays in appointing any were among Deloitte's concerns, a person familiar with the matter said.

"Investors demand greater transparency on ethnic diversity on boards" (9 October 2020)

Investment managers are calling on some of the UK's biggest firms to be more transparent about the ethnic diversity of their boards.

Almost three-quarters of FTSE 100 firms failed to report the ethnic make-up of their boards in this year's AGM season, according to the Investment Association.

L&G, which manages over £1.2 trillion of assets, is thought to be the first big UK investor to threaten to vote against companies that fail to take action on director diversity.

"The Hut Group: matter of standards" (16 September 2020):

THG is unusual for a large domestic UK new listing; it opted for the stock exchange's standard listing and exclusion from the FTSE 100 index.

That is a consequence of the exceptional control that founder Matt Moulding retains in the public company, including a "golden" share blocking unwanted takeovers. But Mr Moulding is not only THG's chief executive and its executive chairman but also its landlord.

"Will digital AGMs replace meeting directors over a prawn sandwich?" (7 August 2020):

Due to the pandemic, 2020 has been an AGM circuit unlike any other. Companies have held closed-door meetings, or hosted digital AGMs over Zoom. Investors say these rapid changes have hurt their ability to participate as company owners, and fear companies will use this precedent to reset annual AGMs to do the "bare minimum necessary" and move online forever.

"Boohoo plans £150 million executive bonus scheme" (26 June 2020):

Boohoo has unveiled a plan to pay bonuses of up to £100m to its two co-founders and £50 million to other executives based only on share performance and with no shareholder vote. The announcement comes just a week after a third of shareholders voted against the company's remuneration report at its annual meeting.

"All-male boards return to FTSE in setback to diversity efforts" (19 June 2020):

The Investment Association issued so-called "red tops" — its highest level of warning — to investors over the lack of gender diversity at both Aston Martin and Domino's. Aston Martin and Domino's are worst for board diversity across the FTSE 350, according to the Hampton-Alexander review

"Exxon shareholders vote against splitting chair and CEO roles" (27 May 2020):

ExxonMobil shareholders have voted against forcing the company to appoint an independent chair. Campaigners wanted it to separate the position from the role of CEO.

"EasyJet founder Stelios loses bid to oust 4 directors" (22 May 2020):

EasyJet founder Stelios Haji-Ioannou has lost his attempt to oust four directors, including the airline's chairman and chief executive. About 58 per cent of shareholders voted against each resolution, compared with about 42 per cent in favour.

"Coronavirus forces investor rethink on social issues" (30 April 2020):

The COVID-19 pandemic has shifted investor focus on how companies treat their employees, customers and suppliers like never before.

Oil, gas, miners, utilities and carmakers have come under intense scrutiny because of their role in global warming, but the coronavirus pandemic means the services sector, financials and healthcare are now under the spotlight.

"Companies urged to hold virtual AGMs to give shareholders a say" (22 April 2020):

Legal & General Investment Management, the UK's largest asset manager, has warned companies it will "hold them to account" if they fail to treat employees and suppliers well as they grapple with the fallout from the coronavirus.

"Investors fear virtual AGMs will shift the balance of power" (12 April 2020):

Investors are concerned virtual AGMs will remove the dialogue between company and shareholders, and allow company boards to 'get away with' a lack of scrutiny from shareholders.

"Annual shareholder meeting season upended by coronavirus outbreak" (28 March 2020):

The coronavirus outbreak has upended the AGM season, many companies are grappling with whether to stage the events when most countries have restricted travel and banned mass gatherings.

"Climate change tops agenda at UK voting season" (5 March 2020):

With more than 450 annual meetings in the UK in the coming months, climate change, executive pay and diversity remain as the most important issues for investors.

"Asset managers demand companies take action on gender diversity" (2 March 2020):

Columbia Threadneedle and RBC Global Asset Management are pledging to vote against board directors of businesses that are failing to promote women to top jobs.

"Shareholder revolts surge at UK companies over executive pay'" (20 February 2020):

Shareholder revolts over pay at FTSE 250 companies rose sharply last year as investors tried to rein in excessive executive remuneration.

The Investment Association said executive pay was top of investors concerns and is set to dominate discussions in 2020.

"Box ticking is bad for corporate governance'" (12 February 2020):

For UK companies to benefit fully from the "comply or explain" approach to corporate governance, they must resist a standardised approach.

Box ticking does little to help stakeholders better understand a company and the challenges it faces.

"Big investors ignore proxy advisers on controversial votes" (8 February 2020):

BlackRock, Vanguard and State Street routinely ignore their proxy advisers' recommendations and vote to block environmental and social action at companies.

"Fear that governance code will spark wave of UK board departures" (3 February 2020):

About a third of chairmen of listed companies in the UK face pressure to stand down from their posts this year after spending more than nine years in the role, raising concerns about widespread disruption at leading British companies.

"Shareholders demand British bosses increase 'skin in the game'" (4 January 2020):

Asset managers, including Schroders, Aviva, and Allianz, are demanding CEOs buy more shares in their own companies to better align their interests with shareholders.

The White & Case UK Public Company Advisory ("**PCA**") team advises UK public companies on their day-to-day legal affairs. In particular, the team engages with listed companies outside of their transaction cycle and provides advice across a range of matters, with particular expertise in corporate governance and corporate advisory. The team is experienced in company secretarial matters and regularly provides support to non-legal functions (as well as legal and company secretarial teams) within PLCs. Our clients range in size and maturity from newly listed companies to mature companies and from small cap companies to global FTSE 350 companies.

The PCA team is part of the network of White & Case offices offering public company advisory services, with specialist practice teams in the US, Germany, Italy and France.

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LON1020067-11