

Catherine Horton
Financial Reporting Council

Management and Investment Services

Roliscon Limited
PO Box 62
Chislehurst
BR7 5YB, UK

Tel: 020-8295-0378
Int: +44-208-295-0378
Web: www.roliscon.com

Via email: codereview@frc.org.uk

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Response to Consultation on Proposed Revision to the UK Corporate Governance Code

Dear Ms Horton,

What follows is a response to the above consultation based on my experience of investing in public companies over many years, and dealing with many abuses in such companies. It is apparent from events in the last few years that the Corporate Governance Code needed further improvement and I welcome most of the proposed changes.

Responses to Consultation Questions

What follows are my responses to each of the consultation questions:

UK Corporate Governance Code and Guidance on Board Effectiveness Questions

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

Answer: No.

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

Answer: No.

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

Answer: I doubt that a “designated non-executive director” would be as effective as the other two methods. I suggest companies should justify why the others are inappropriate.

Q4. Do you consider that we should include more specific reference to the UN SDGs or other NGO principles, either in the Code or in the Guidance?

Answer: No because the Code and the Guidance should be self-contained documents and not require reference to other documents to understand them.

Q5. Do you agree that 20 per cent is ‘significant’ and that an update should be published no later than six months after the vote?

Answer: I suggest 10 or 15% would be more appropriate levels to trigger an update to shareholders. Where there is general support for a resolution, they usually pass with over 95% in support, so opposition of more than 10% indicates that there is some controversy over the proposal which should be understood by boards and their shareholders.

Q6. Do you agree with the removal of the exemption for companies below the FTSE 350 to have an independent board evaluation every three years? If not, please provide information relating to the potential costs and other burdens involved.

Answer: Yes. I doubt the benefit of such evaluations.

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

Answer: Yes, I strongly support this proposed change to include chairmen.

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

Answer: No I disagree. As the proposed nine-year time year period only applies to “independence” and there is nothing to prevent a board from including non-independent directors that means there is nothing to prevent certain directors from retaining their position for many years. This allows current poor practices where directors stick around for way too long, and become stale, to persist.

Even with the current Code, on a “comply or explain” basis we get feeble excuses for the retention of directors past the nine- year period. The Code should be toughened to exclude excuses such as “their experience is valuable to the board”.

Q9. Do you agree that the overall changes proposed in Section 3 of revised Code will lead to more action to build diversity in the boardroom, in the executive pipeline and in the company as a whole?

Answer: Perhaps but statements such as “appointments...should promote diversity of gender, social and ethnic backgrounds” effectively mandates discrimination which is contrary to law. I suggest that needs to be removed or reworded.

Q10. Do you agree with extending the Hampton-Alexander recommendation beyond the FTSE 350? If not, please provide information relating to the potential costs and other burdens involved.

Answer: No, this is an unnecessary burden on management.

Q11. What are your views on encouraging companies to report on levels of ethnicity in executive pipelines? Please provide information relating to the practical implications, potential costs and other burdens involved, and to which companies it should apply.

Answer: Am not in favour of this simply because of the difficulty in defining ethnicity in a population made up of a great mixture of ancestry.

Q12. Do you agree with retaining the requirements included in the current Code, even though there is some duplication with the Listing Rules, the Disclosure and Transparency Rules or Companies Act?

Answer: Yes

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

Answer: Yes.

Q14. Do you agree with the wider remit for the remuneration committee and what are your views on the most effective way to discharge this new responsibility, and how might this operate in practice?

Answer: I support the proposals, but I would like to see more specific definition of which remuneration schemes represent “clarity” and “simplicity”. There are way too many over-complex schemes that neither non-executive directors nor shareholders understand.

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

Answer: I very much doubt that incentive schemes that pay out over long periods have much impact at all on management performance. Bonus schemes need to pay out very quickly if they are to be recognised as “valuable” to employees. All LTIPs are therefore by their very nature ineffective and have to be excessively generous to be valued at all, that is why I think they should be scrapped altogether. There should be limits on the ratios of pay-outs from incentive schemes to basic pay – no more than 100% in any one year. It’s simply a mirage for boards to believe that aggressive bonus schemes drive higher performance from executives, particularly when the outcome of any bonus scheme often depends on external factors beyond the control of the executive.

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

Answer: I doubt it because there is bound to be conflict with employment contracts – ones already in place if not future ones. It’s also very psychologically difficult for boards to impose retrospective adjustments to bonus schemes in this way.

UK Stewardship Code Questions

Q17. Should the Stewardship Code be more explicit about the expectations of those investing directly or indirectly and those advising them? Would separate codes or enhanced separate guidance for different categories of the investment chain help drive best practice?

Answer: I would support this suggestion although more explanation on this would be helpful.

Q18. Should the Stewardship Code focus on best practice expectations using a more traditional ‘comply or explain’ format? If so, are there any areas in which this would not be appropriate? How might we go about determining what best practice is?

Answer: I agree that would assist to improve standards. But it is probably best for others to comment on specific approaches.

Q19. Are there alternative ways in which the FRC could highlight best practice reporting other than the tiering exercise as it was undertaken in 2016?

Answer: No comment.

Q20. Are there elements of the revised UK Corporate Governance Code that we should mirror in the Stewardship Code?

Answer: No comment.

Q21. How could an investor's role in building a company's long-term success be further encouraged through the Stewardship Code?

Answer: The Stewardship Code could support the development of Shareholder Committees for companies to improve shareholder engagement.

Q22. Would it be appropriate to incorporate 'wider stakeholders' into the areas of suggested focus for monitoring and engagement by investors? Should the Stewardship Code more explicitly refer to ESG factors and broader social impact? If so, how should these be integrated and are there any specific areas of focus that should be addressed?

Answer: It is difficult to see how ESG factors can be directly incorporated except by reference to what is in the interests of companies and their investors.

Q23. How can the Stewardship Code encourage reporting on the way in which stewardship activities have been carried out? Are there ways in which the FRC or others could encourage this reporting, even if the encouragement falls outside of the Stewardship Code?

Answer: No comment.

Q24. How could the Stewardship Code take account of some investors' wider view of responsible investment?

Answer: No comment. Do not understand the question.

Q25. Are there elements of international stewardship codes that should be included in the Stewardship Code?

Answer: Am not aware of any, but that seems likely to be so. A detailed review is required. It would seem wise to try and develop an international standard to avoid duplication of effort in reporting and Code maintenance.

Q26. What role should independent assurance play in revisions to the Stewardship Code? Are there ways in which independent assurance could be made more useful and effective?

Answer: No comment.

Q27: Would it be appropriate for the Stewardship Code to support disclosure of the approach to directed voting in pooled funds?

Answer: Yes, absolutely.

Q28: Should board and executive pipeline diversity be included as an explicit expectation of investor engagement?

Answer: I would be opposed to this as it should be adequately covered in the Corporate Governance Code and it is not something investors should engage on unless a company is not in compliance with that Code.

Q29: Should the Stewardship Code explicitly request that investors give consideration to company performance and reporting on adapting to climate change?

Answer: Adapting to climate change is just one of many factors that investors need to give consideration to and engage with boards on if required. But it would be wrong to impose such obligations on investors which might result in excessive “micro-management” of company policies, strategy and operations. What factors are important for consideration are likely to change over time so it would be wrong to set priorities on which should be considered by investors.

Q30: Should signatories to the Stewardship Code define the purpose of stewardship with respect to the role of their organisation and specific investment or other activities?

Answer: It would certainly be helpful to do so as at present it is often unclear.

Q31: Should the Stewardship Code require asset managers to disclose a fund’s purpose and its specific approach to stewardship, and report against these approaches at a fund level? How might this best be achieved?

Answer: This would also be helpful.

Further Comments

In addition to the answers to your specific questions, I have these additional comments on the proposed Governance Code:

Section 1 – Provision 5. It mandates regular engagement with “major shareholders” but says nothing about engagement with smaller institutions or individual shareholders. Bearing in mind the large diversity in the shareholdings of companies (very few public companies have any one investor with more than 2% of the shares) this concept of “major shareholders” is no longer viable. There needs to be recognition that there is a much more diverse shareholder base even just considering institutional investors and there also needs to be some obligation to engage with private shareholders who might represent over 10% of the shareholder base and where there are two representative groups that could be consulted. A formal way to deal with this would be the establishment of Shareholder Committees.

Section 1 – Provision 6. There should be a requirement to specifically disclose who the board has consulted where significant votes are cast against a resolution. Often one gets excuses that “they have consulted major shareholders” when few shareholders seem to have been asked.

Section 1 – Provision 14. There should be a specific limit on the number of roles that non-executive directors have. Four is a reasonable limit bearing in mind the obligations and time requirements of such positions.

Section 2 – Provision 15. The exclusion of consideration for independence from those with “close family ties, or any of the company’s advisors, directors or senior employees” should be extended to include those with close business ties.

Section 4 – Provision 24, and Section 1. Provision 24 requires the “committee as a whole shall have competence relevant to the sector in which the company operates” but only one member requires “recent and relevant financial experience”. This is much too weak for a major public company in several respects. At least one Committee member should have a recognised financial qualification in addition.

I also suggest that similar principles be applied to the board as a whole in Section 1. At present we get too many board members who have no experience of the sector in which a company operates – I suggest it needs to be at least 50% of the board members.

Conclusion

I hope my answers to your questions are helpful. You are welcome to contact me for further information if required.

Yours sincerely

Roger W. Lawson
Managing Director