

One Minute Memo®



UK Corporate Governance Reform - More Regulation, But Not as Bad as Feared!

By Robert Hanley

Last week the UK Government published its formal response paper on UK corporate governance reform, describing the proposals as “world-leading.” The proposals follow an earlier green paper published by the Government in November 2016 that aimed to identify changes to the UK corporate governance regime to create “an economy that works for everyone.” The unions and sections of the media have expressed disappointment and suggested the reforms do not go far enough. Unions were seeking a cap on CEO pay, employee representatives on boards and binding shareholder votes on pay (amongst other measures), but these have been ruled out, much to the relief of the business community. The proposals suggested by the Government include the following:

- **Pay ratios** - Quoted companies will be required to report annually on the ratio of their CEOs’ pay to the average UK workforce pay, together with an explanation of any change in that ratio from year to year and how the ratio relates to pay and conditions across the wider workforce.
- **Shareholder opposition to executive pay** - The Government has requested that the UK Investment Association establish a register of listed companies which encounter significant (20% or more) shareholder opposition to executive pay proposals and for the register to record what those companies do in response to such opposition, such as issuing a public response or subjecting the executive pay proposals to a shareholder vote. The Investment Association is expected to establish its register before the end of 2017.
- **Enhanced stakeholder engagement** - Section 172 of the UK *Companies Act 2006* obliges company directors to consider the interests of employees, customers, suppliers and other stakeholders. The Government now proposes that public and private companies of “significant size” must explain how their directors have complied with section 172. It is not yet clear what “significant size” means, but commentators believe it refers to those companies with greater than 1,000 employees.
- **Employee board representation** - The Government has asked the Financial Reporting Council (FRC) to revise the UK Corporate Governance Code to require companies to choose one of three models (suggested in the 2016 green paper) for involving employees in board decisions. The three models are: to designate a non-executive director to represent employees; to create a formal employee advisory council that the board would be required to consult; and, to appoint a director from the workforce. The Government has not proposed employee representation on remuneration committees.

- **Governance of large private companies** - The Government has asked the FRC to work with various industry bodies (including the Institute of Directors, the Confederation of British Industry and the British Venture Capital Association) to develop a voluntary set of corporate governance principles for private companies with more than 2,000 employees. Separately, all such companies will also be required to disclose their corporate governance arrangements in their directors' reports and on their website and to indicate whether they follow a formal code.

The Government intends to take forward its proposals by June 2018 and for the new requirements to apply to company reporting years commencing on or after that date. The changes are intended to be delivered not through primary legislation, but by changes to the UK Corporate Governance Code and other regulator-led reforms. The FRC has indicated that changes to the Code will be the subject of a consultation later in 2017.

The real impact of the proposed changes to the corporate governance regime is yet to be seen, but it seems unlikely that the "world-leading" reforms will deliver fully on the Government's promise to create "an economy that works for everyone."

If you have any questions or would like further information, please contact [Robert Hanley](#) in our London office at rhanley@seyfarth.com, or any member of our [International Corporate & Commercial practice](#).

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