Linklaters

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UK Corporate Update.

Lord Davies sets new target of 33% women on boards by 2020

Lord Davies has published his final report on improving the gender balance on UK boards. His plea, made in 2011, that women should hold 25% of FTSE 100 board positions by 2015 has been met. However, the report finds that there is work to be done in increasing the number of women holding executive and senior leadership positions. Lord Davies has also set a new target of 33% female board representation across the FTSE 350 by 2020.

Key findings

Key points of the report include that:

> At 1 October 2015, there are no male-only boards in the FTSE 100 and women hold 26.1% of board positions in those companies, compared to 12.5% in February 2011. Within the FTSE 250, women hold 19.6% of board positions, but there remain 15 male-only boards.

> While the steering group does not believe quotas are warranted, European countries with quota regimes are likely to meet their target figures in the next few years and the UK will fall behind, both in Europe and internationally, if it does not progress beyond 26% female representation.

> Work by the executive search community to develop its standard voluntary code of conduct and the enhanced code of conduct has been a key driver of progress on gender diversity in the boardroom.

> The steering group feels that the investor community as a whole has yet to gather momentum, with the results of a recent survey showing that the majority of surveyed investors believe the investor community has responded only moderately well to the drive for female board representation.

> Work needs to be done to increase the number of women holding executive positions (currently 9.6% within the FTSE 100).

> Nomination committees and search firms should cast their net beyond the corporate sector and professional services firms when searching for potential candidates for board appointments.

Recommendations

The report makes five recommendations to maintain and encourage greater momentum going forward:

> That the voluntary, business-led approach to improving female board representation be continued for another five years.

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- Setting a target for female board representation in the FTSE 350 of 33% within five years, increasing the progression of women to the roles of chair, senior independent director and executive director, and asking all FTSE listed companies to address gender imbalance on their boards.
- That FTSE 350 companies extend work on gender balance to their executive committees and in the most senior leadership positions.
- That a new steering group be established under a new chair, comprising business and subject matter experts.
- That the new steering group should review the above recommendations and, after consultation, publish more detailed comments at the start of 2016.

Click here for Lord Davies' final report.

FRC seeks views on board succession planning

The Financial Reporting Council is seeking to identify good practice in relation to succession planning. It has published a discussion paper which focuses on the role of the nomination committee, board evaluation and the importance of identifying a pipeline of candidates both inside and outside the company for executive and non-executive director roles. It also considers diversity and the role of institutional investors.

Nomination committee

The nomination committee is seen by some as the 'poor cousin' of other committees, meeting less frequently and with poorer quality disclosure. There is also a perceived need for the nomination committee to be evaluated more robustly, particularly with regard to succession planning. The FRC is therefore seeking views on ways to clarify the nomination committee's responsibilities in the Corporate Governance Code and on steps that could be taken to improve its standing. The FRC suggests that:

- greater use should be made of the committee to make recommendations to the board on succession planning
- the committee should plan for unforeseen as well as foreseen departures of directors, e.g. for sudden emergencies where a director cannot continue working through illness or because of regulatory investigation
- the committee should consider senior management team as well as board appointments and have a broader oversight of talent management.

The nomination process

The FRC responds to the suggestion by the Parliamentary Commission on Banking Standards that individuals who might provide constructive challenge were sifted out by the nomination process. The FRC has found no evidence of this but invites comments. It also wants to hear about the experience of publicly advertising for non-executive positions.

Evaluation

The discussion paper invites comments on practical steps to ensure boards integrate succession planning within the annual evaluation exercise and on how to achieve more transparency in the reporting of changes to the succession planning process that result from the evaluation. It asks whether retrospective disclosure might deal with concerns about revealing sensitive findings.

Pipeline

The FRC suggests that boards need to become more familiar with individuals (both internal and external candidates) in the pipeline for director positions. The CEO, chairman, nomination committee and company secretary could also play a role in managing the process.

It seeks feedback on a number of questions, including:

> the ways in which companies review internal talent and the development practices used support of succession planning

> the ways in which companies could establish an external pipeline, e.g. tracking external candidates for NED positions

> the ways to ensure that board members become more familiar with the role of internal candidates and their skills and attributes.

Diversity

The FRC considers that the major benefit of diversity is avoiding group think. It seeks feedback on:

> the ways in which a succession plan could incorporate and deliver diversity objectives

> whether current UK Corporate Governance Code provisions relating to non-executive independence, particularly the nine year rule, encourage diversity and progressive refreshment.

It also asks for examples of human resources and nomination committees working closely with executive search firms to identify more diverse candidates.

Institutional investors

The FRC notes that institutional investors want to discuss succession planning, generally in order to be confident that the board has an effective overall plan and that this is reviewed, updated and acted upon. As with board evaluations, there are confidentiality issues and the FRC seeks views how information might be shared between companies and investors.

Next steps

The FRC invites comments by 29 January 2016. A feedback statement will follow.

The discussion paper can be found here.

BIS consults on regulations to limit length of audit engagements

The Department for Business, Innovation and Skills is consulting on draft regulations to implement the EU Audit Directive (Directive 2014/56/EU) in the UK and its implementation options under the EU Audit Regulation (Regulation 537/2014).

Which entities will be subject to the EU Audit Regulation?

The Audit Regulation applies to “public interest entities” or “PIEs”. BIS will not take up the Member State option to extend the definition of public interest entities, meaning that the Regulation will apply only to entities with securities admitted to trading on a regulated market, banks, building societies, and insurers.

Length of audit engagements

Of particular interest are the proposals on the length of audit engagements to be set out in amendments to Sections 487 and 491 of the Companies Act 2006 and in a new Section 489A CA 2006:

> The maximum duration of an audit engagement should be 10 successive accounting years beginning on the date the auditor takes office for the first time. The auditor should still be reappointed annually during that 10 years.

> A public interest entity should be permitted to extend the maximum duration of the audit engagement by a further 10 years on the basis of a tender process for any accounting year up to and including that following the conclusion of the 10 year maximum duration. The tender process should be conducted in accordance with Article 16(3) of the Regulation and overseen by the audit committee.

> No provision is being made to enable the maximum duration to be extended by the use of joint audit appointments.

> If the auditor has been reappointed following one or more tender processes, the maximum duration of a continuous audit engagement (including joint audits) should be 20 years in total.

The Government has decided not to require PIEs to disclose the timing of their next audit tender as proposed by its discussion document in December 2014. Instead, the FRC is proposing to amend C3.8 of the UK Corporate Governance Code to require a disclosure in the audit committee report giving advance notice of retendering plans.

Other provisions

The draft regulations also:

> designate the Financial Reporting Council as competent authority to conduct audit inspections, investigations and disciplinary cases in relation to PIEs and to oversee the work of the recognised supervisory bodies for other audits;

> give authority to the FRC to introduce changes in ethical and technical standards for auditors; and

> make ineffective any agreement with a third party that restricts an audit client's choice of auditor.

The closing date for responses is 9 December 2015. The Government will then finalise the regulations with the intention that they will apply for financial years beginning on or after 17 June 2016. The Audit Regulation will take effect automatically on 16 June 2016, which is also the deadline for implementation of the Audit Directive.

The consultation can be found here. The draft regulations can be found here.

ESMA statement on quality of disclosures in financial statements

The European Securities and Markets Authority is calling for an improvement in the quality of disclosures in financial statements. It highlights the following principles:

> *Being specific*: Issuers should focus on "entity-specific" disclosures and avoid boilerplate language;

> *Providing relevant information in an easily accessible way*: relevant information for these purposes is information that is necessary to

understand the issuer's financial performance and position and that could influence an investor's economic decisions;

> *Thinking about materiality*: issuers should review disclosures in financial statements that are no longer relevant, remove elements that are no longer required and consider deleting immaterial information;

> *Promoting readability*: The most relevant information should not be obscured by a large amount of less relevant information. Cross references should be used where possible and the layout of financial statements modified to improve conciseness and clarity;

> *Ensuring consistency*: Information provided in financial statements and accompanying documents (such as the management report) should be consistent.

ESMA is encouraging all parties involved in preparing financial statements to contribute to improving the quality of disclosures. Auditors should encourage issuers to focus on materiality and entity-specific information and European national enforcers should promote best practice and reflect on their enforcement practices in light of the statement.

ESMA's statement can be found here.

Impact of new market abuse regulation on UK rules

The EU Market Abuse Regulation, which will apply from next July, is forcing the Financial Conduct Authority to delete or convert into guidance the parts of its Handbook that deal with market abuse, disclosure of inside information and share dealings.

The FCA is consulting on these changes and also on two aspects of MAR where the FCA has a choice as to the approach to take in the UK. These are: the threshold for disclosure of dealings by a person discharging managerial responsibility and whether issuers must provide an explanation automatically every time they delay disclosure of inside information or only on request.

Further proposals in the consultation include

> the Disclosure Rules in DTR 1-3 would largely be deleted, and only some of the current guidance would remain,

> the deletion of the Model Code on dealings by directors and senior managers, since there are provisions prohibiting dealings by PDMRs in closed periods in MAR, although the FCA proposes requiring premium listed companies to have appropriate systems on giving PDMRs clearance to deal, and

> changes to the status and content of the Code of Market Conduct.

A full briefing is available on the Linklaters Knowledge Portal

Click here for the FCA consultation paper 15/35, published on 5 November. The consultation closes on 4 February 2016.

Transparency Directive changes take effect soon

The FCA has published the final rule changes necessary to implement the amended EU Transparency Directive. These changes will take effect on 26 November 2015.

The changes impact financial reporting, notification of changes in major shareholdings and the sanctioning powers of competent authorities and include, in particular:

> a company's annual financial report and the half-yearly report must be publicly available for at least ten years;

> the period for issuers to publish their half-yearly reports has been extended from two months to three months after the end of the half-year period; and

> the power of competent authorities to impose higher fines.

Some of the changes from the amended Directive are already in force in the UK, having been implemented early. These include the abolition of interim management statements last year and the requirement to disclose certain payments made by companies in the extractive and logging sectors which applies for financial years commencing on or after 1 January 2015 (see UK Corporate update 27 August 2014).

HM Treasury has also been responsible for the implementation of the amended Directive and published Regulations in October setting out the changes to be made to the Financial Services and Markets Act 2000 (see UK Corporate Update 15 October 2015).

A briefing on the implementation of the amended Directive will be published shortly.

Schemes of arrangement and stamp duty: change in HMRC practice

HM Revenue & Customs has issued new guidance, changing its view and practice regarding how stamp duty is paid on transfer schemes of arrangement.

In March of this year the Companies Act was amended to ban takeovers from being effected by cancellation scheme. The ban was introduced in order to prevent cancellation schemes being used to avoid the payment of stamp duty on takeovers. Companies effecting takeovers now have to use a transfer scheme (or a contractual offer) on which stamp duty is payable.

HMRC practice since March has been to stamp the court order approving the scheme, which has delayed the date on which such schemes become effective. In response to representation from Linklaters and other law firms, HMRC has now accepted that it is the stock transfer form and not the court order which needs to be stamped when the scheme provides for a separate stock transfer form (which is normal practice).

This means that it will be possible to make the scheme effective shortly after the court sanction hearing or scheme record date (if later), rather than having to wait for stamping by HMRC.

HMRC will issue a letter to confirm this.

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