The City of London Law Society

4 College Hill
London EC4R 2RB

Tel +44 (0)20 7329 2173
Fax +44 (0)20 7329 2190
DX 98936 – Cheapside 2

mail@citysolicitors.org.uk

www.citysolicitors.org.uk

CORPORATE GOVERNANCE REFORM

Response of the City of London Law Society Company Law Committee to the Green Paper

The CLLS represents approximately 17,000 City lawyers through individual and corporate membership, including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multijurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees.

Overview

We welcome this opportunity to participate in the public debate on the way forward for corporate governance in the UK. The Green Paper rightly recognises that our existing framework of company law and corporate governance standards is generally respected but we acknowledge that it raises legitimate questions about whether updating is needed. Before dealing with the specific questions in the Green Paper we offer the following observations on the wider issues raised:

- good governance depends on the calibre and motivation of the individuals who are appointed to the board. The importance of having a robust process for recruiting the right people, with appropriate diversity of backgrounds, skills and experience cannot be overstated.

- the statutory duty of directors is centred on shareholder interests. This is underlined in the terms of Section 172, which makes "success of the company for the benefit of its members" the objective of directors[1]. Unless this objective is changed, the primacy of shareholder interests will remain the guiding principle underlining corporate governance in UK companies. Change of this kind would be a bold step and would require careful consideration and further consultation. In particular, the following questions would need to be addressed:

[1] Except in the case of insolvency or threatened insolvency when the interests of creditors become relevant (CA 2006 Section 172(3))

- the effect of such a change on the willingness of investors to contribute capital and trade in the shares of companies where shareholder interests are not the primary consideration. While there are examples of companies which have chosen to follow such an approach to a greater or lesser extent it would be important to be satisfied that forcing such a change on all UK companies would not diminish the attractiveness of the UK as a place to invest or to establish a company

- the question of enforcement of directors' duties would have to be considered. Under the existing framework enforcement is a matter for the company (acting through its board) or its shareholders. Unless that is changed any change in the terms of the statutory duty may not have the desired effect. However, to make an independent authority responsible for enforcement would have significant implications for board decision making, as would any real or perceived increase in the exposure of directors to potential litigation

- boards may legitimately ask for guidance on how competing interests should be balanced if none is given primacy over the others

- a change in the statutory duty on its own may not be sufficient to reduce materially the influence of shareholder interests on board decision making. UK company law and the rules governing listed companies give shareholders a more central role in governance than in other jurisdictions (examples include: director appointment and removal; pre-emption rights on new issues of equity; shareholder approval of Class 1 transactions; the prohibition on poison pills). Without wider changes to the framework within which they operate, boards will only feel properly empowered to take decisions that will benefit the development of the company in the long term if shareholders actively support them in doing so. Section 172 already gives boards a basis to defend their decisions that take into account wider stakeholder interests against claims from shareholders that their (potentially short term) interests are adversely affected.

- it is important to be clear whether the objective of reform is to influence businesses in the UK or to change the way that UK companies operate. The two are not the same. Many UK businesses are operated by companies incorporated outside the UK. Perhaps more importantly, many more could be organised in that way, if their shareholders thought it more attractive to do so. Some issues, such as treatment of employees and protecting the interests of members of UK pension schemes, will be better addressed in the wider context of business generally and not as a corporate governance issue, in order that all UK employees and pensioners who are affected are protected appropriately (we are not expressing a view that employees need additional protections or that UK pensions regulation requires reform).

- when discussing the way boards should take into account non-shareholder stakeholders it is important to be clear whether the concern is limited to UK stakeholders or a global view should be taken. Most large companies operate in more than one country, through subsidiaries (which may be incorporated in the UK or other countries) and/or branches operating outside the UK. The Green Paper appears to be focussed on UK stakeholders but for companies operating internationally it may not be acceptable to limit attention to stakeholders in the UK.

A way forward

We suggest that at this stage reform could include the following:

- changes to the Corporate Governance Code requiring companies to explain their values and the objectives of the company, and how those take into account wider stakeholder interests (including explaining which stakeholder groups are considered to be relevant). Companies could also be required to explain what steps they have taken to obtain views from stakeholders to inform decisions made by the board.

- the FRC could be given enforcement powers to ensure that non-financial disclosures meet the required standard; the scope of any such powers would require careful consideration, including whether they would be limited to statutory requirements or would include the enhanced disclosures required by the Corporate Governance Code.

- for privately held companies, a voluntary code expressed as high level principles, on a comply or explain basis (with an appropriate size threshold), with a requirement to report on whether the code has been adopted and if so, providing explanations of any non-compliance.

A limited package of reform of this kind would give companies in the UK the opportunity to take appropriate action to rebuild public trust. It would be relatively simple to implement and would build on (and not undermine) the strong foundations of the existing corporate governance structure in the UK, which many internationally regard as the gold standard. Reform of this kind, based on disclosure and leaving companies to make their own decisions regarding implementation, reduces the risk of unintended harmful consequences and should ensure that the UK remains competitive in the market for international capital.

EXECUTIVE PAY

Question 1. Do shareholders need stronger powers to improve their ability to hold companies to account on executive pay and performance? If so, which of the options mentioned in the Green Paper would you support? Are there other options that should be considered?

We do not express a view on whether shareholders need stronger powers but we do suggest caution before changing a relatively new regime that is among the most robust in the world and already gives considerable powers to shareholders. We are entering the third year since the regime came in and companies are having to renew their pay policies for the first time. While it may be thought that the new regime has not yet led to a sufficient change in behaviour, we think there is a strong case for waiting to see whether the other reforms that may be adopted, together with the continuing shareholder pressure on boards, will bring about the change that is needed.

Our comments on the options are set out below:

Option (i): Make all or some elements of the executive pay package subject to a binding vote. This could be the full remuneration report or refer only to variable pay elements of the pay award (such as the annual bonus, the Long-Term Incentive Plan and any proposed increase in basic salary). It could be applied annually to all companies or only to companies that have encountered significant shareholder opposition to the remuneration report.

We see major difficulties with a mandatory vote on executive pay, which would mean that executive directors would be expected to accept that all or part of their remuneration will depend on shareholders' willingness to approve, retrospectively, the amount to be paid. The implications of this include:

- executives would have to trust shareholders to use this power responsibly.
- the increased risk for the executive may lead to demands for increased rewards.
- it will be more difficult to attract the best people to take on challenging leadership roles in UK companies when they have alternatives in companies operating under more benign regimes.
- the need to secure the vote on pay may add to the pressure on executives to take short term "shareholder-pleasing" decisions.
- the process for the RemCo to determine the amount of remuneration of the executives (exercising their discretion for that purpose) will become complex and may either involve a potentially lengthy dialogue with principal shareholders to gain their agreement to the amount proposed (do shareholders have appetite and resources sufficient for this?) or a "take it or leave it" approach which gives shareholders a simple choice of whether or not to approve a proposal made by the RemCo (which is unattractive as explained below).
- given the potentially serious consequences for the company if shareholders do not pass the resolution (we assume that a decision not to pay the CEO would usually lead to their immediate departure) it may be that shareholders will feel forced into supporting the proposal (even if they think the quantum is excessive). By doing so shareholders may be seen as taking responsibility for the decision, deflecting criticism from the board.
- if the ability to provide a reliable remuneration structure is too heavily compromised, companies may be encouraged to establish outside the UK.

Option (ii) Introduce stronger consequences for the company losing its annual advisory vote on the remuneration report

While attractive because it defers the problems that arise from a mandatory vote in every case, the proposal to require a supermajority (we assume this would be a special resolution) after one advisory vote is defeated suffers from two problems:

- the failure to approve a remuneration policy potentially has a very significant effect on the company (it is unable to pay any of its directors), which should not be triggered by a relatively small minority.

- as explained above, having the ability to trigger significant adverse consequences is a dangerous weapon for shareholders to deploy, and they may be reluctant to do so.

Option (iii) Require or encourage all company pay policies to (a) set an upper threshold for total annual pay (from all elements of remuneration), and (b) ensure a binding vote at the AGM where actual executive pay in that year exceeds the threshold

Requiring a binding cap on total annual pay as part of the remuneration policy will reduce flexibility for the RemCo to respond appropriately to changes in circumstances, where the company's best interests are not best served by a requirement to wait for a shareholder vote.

The second element of the proposal is unnecessary because the effect of a binding cap would be to require the overpayment to be held in trust for the company and any directors who approve a payment in excess of the cap to indemnify the company for the amount of the excess[2].

Option (iv) Require the existing binding vote on the executive pay policy to be held more frequently than every three years, but no more than annually, or allow shareholders to bring forward a binding vote on the new policy earlier than the mandatory three-year deadline

The requirement for pay policies to be renewed every three years was adopted in response to pressure from shareholders who did not want to have to undertake the process of approving policies more frequently. There is no restriction on policies being approved annually and nothing to prevent shareholders proposing a new policy, replacing one previously approved. Once approved the new policy would become binding. We suggest that no change is required, therefore and if shareholders now wish companies to move to annual pay policy votes they have power to compel them to do so.

Option (v) Strengthen the Corporate Governance Code to provide greater specificity on how companies should engage with shareholders on pay, including where there is significant opposition to a remuneration report

We are not aware that there is any confusion on the part of companies as to how to engage with shareholders. We understand that many companies, in particular smaller companies, experience difficulties obtaining sufficient attention from their shareholders for an effective dialogue to take place. Any increase in the expectations on companies should be accompanied by strengthening the Stewardship Code to emphasise the importance of investors allocating sufficient resources to respond to the reasonable demands of companies to engage with them on these questions.

[2] CA 2006, section 226E

We note that paragraph 1.28 of the Green Paper suggests that the changes to the Corporate Governance Code may also include engagement with employees. We have provided our comments on the question of engagement with employees below (Question 3, Option (i)).

Question 2. Does more need to be done to encourage institutional and retail investors to make full use of their existing and any new voting powers on pay? Do you support any of the options mentioned? Are there other ideas that should be considered?

The evidence referred to in the Green Paper is far from conclusive that there is a problem with a lack of shareholder participation. The fact that the majority of pay policies are approved may be a result of effective engagement between companies and shareholders and not evidence that such engagement is not occurring.

Option (i): Mandatory disclosure of fund managers' voting records at AGMs and the extent to which they have made use of proxy voting

We do not have a view but observe that the proposal to make disclosure of voting mandatory raises questions regarding the scope of the requirement (to which investors will the requirement apply) and the nature of the sanction that would be applied for failure to provide the information. We expect that fund managers would find it burdensome to publish more detail of the rationale for their voting decisions and no useful purpose would be served by additional boilerplate disclosures.

Option (ii): Establish a senior "shareholder" committee to engage with executive remuneration arrangements

The concept of a "senior shareholder committee" is one that has been discussed before and not adopted. There are a number of problems that would have to be addressed, the principal being:

- selecting certain shareholders and giving them special rights is inconsistent with the fundamental principle that all shareholders should be treated equally
- to define which shareholders would be represented on the committee and how they would be selected (would this be based only on size of holding or would the type of investor be relevant?)
- whether the members of the committee would be expected to consult other shareholders (which would duplicate the engagement efforts of the company) or only provide their own views (in which case they cannot claim to be representative of shareholders generally)
- to determine whether the members of the committee would owe enforceable duties to the company equivalent to the duties owed by directors and, if not, whether there would be any legal constraint on their freedom to vote in their own interests.

Existing mechanisms for organising collective engagement between shareholders and companies (for example the Investor Forum) are focussed on strategic issues, which does not seem to include remuneration[3]. Shareholders who are supportive of the board and may see no value in collective engagement would effectively be forced to participate in order to ensure there was a balanced view on the committee. There is a danger that a shareholder committee would provide a platform for an activist shareholder with its own agenda to wield disproportionate power.

Option (iii): Consider ways to facilitate or encourage individual retail shareholders to exercise their rights to vote on pay and other corporate decisions

We think that amending the Companies Act to <u>require</u> entities who hold shares on behalf of individual investors (we think this should refer to custodians or nominees rather than brokers) to offer opt-in to voting and information rights should be considered as a last resort as it would impose a cost on the underlying holders, whether or not they were interested in exercising their rights. The first step should be better education of investors, so that the availability of the option to opt-in to voting and information rights could become a factor in the choice of broker (to be balanced against other factors such as the additional cost of making those rights available).

Question 3. Do steps need to be taken to improve the effectiveness of remuneration committees, and their advisers, in particular to encourage them to engage more effectively with shareholder and employee views before developing pay policies? Do you support any of the options set out in the Green Paper? Are there any other options you want to suggest?

Option (i): Require the remuneration committee to consult shareholders and the wider company workforce in advance of preparing its pay policy

We question the need for an obligation to consult shareholders. The requirement to obtain approval creates a powerful incentive for such consultation to take place and we doubt that imposing an obligation will lead to any different level of engagement.

We express no view on whether remuneration decisions will better promote the success of companies if they are reached after consultation with employees but we note that the Remuneration Policy is already required to include a statement on how the pay and employment conditions of non-director employees were taken into account in setting the policy for directors' remuneration[4].

If it is considered desirable to require consultation with shareholders and/or with employees we recommend that it be through the Corporate Governance Code, bolstered by the dissemination of examples of what is regarded as best practice and additional disclosure of the steps taken.

Before adopting a legal obligation it would be necessary to address questions of scope (which shareholders or employees would have to be consulted) mechanism (formal or informal) and enforcement (who would enforce and what sanctions would be applied). Proceeding by way of

---

[3] None of the engagements reported by the Investor Forum in its 2015/2016 Review related to remuneration.

[4] Paragraph 38 of Schedule 8 of the Large and Medium-Sized Companies and Groups (Accounts & Reports) Regulations 2008 (SI2008/410)

the Corporate Governance Code will allow a more flexible approach better tailored to the circumstances of the individual company.

Option (ii): Require the chairs of remuneration committees to have served for at least 12 months on a remuneration committee before taking up the role

While we agree it makes sense for a director to have experience of serving on a remuneration committee before taking on a chairmanship role, we are not convinced it is necessary to mandate a 12 month period on the committee that is to be chaired.[5] Doing so might preclude the recruitment of an experienced director to replace a chairman, even where that is the right course in the particular circumstances.

Question 4. Should a new pay ratio reporting requirement be introduced? If so, what form of reporting would be most useful? How can misleading interpretations and inappropriate comparisons (for example, between companies in different sectors) be avoided? Would other measures be more effective? Please give reasons for your answer.

We make no comment on whether pay ratios are useful but we would observe that the lengthy (290+ pages) and complex SEC guidance in this area demonstrates that the challenges presented by pay ratio reporting should not be underestimated. We believe that the time and effort involved in producing a ratio and carrying out any meaningful comparison of different ratios should be properly considered as a part of the cost benefit analysis before any changes are made in this area. We also note that the SEC's Acting Chairman, Michael S. Piwowar, has proposed reconsideration of their pay ratio rule and has invited further consultation to identify "unexpected challenges" faced by companies preparing to comply with the pay ratio disclosure rule and whether relief is needed.

Question 5. Should the existing, qualified requirements to disclose the performance targets that trigger annual bonus payments be strengthened? How could this be done without compromising commercial confidentiality? Do you support any of the options outlined in the Green Paper? Do you have any other suggestions?

We think the commercial confidentiality exception is justified so long as it is properly applied. We suggest that guidance from the FRC would be helpful in encouraging a more rigorous approach to the application of the exception with a consequent improvement in the quality of disclosure of targets. Where the exception is applied subsequent disclosure of the targets would provide useful transparency but we would not be in favour of setting a definitive deadline for that disclosure. We suggest that disclosure should be included in the first remuneration report to be published after the information ceases to be commercially confidential.

Question 6. How could long-term incentive plans be better aligned with the long-term interests of quoted companies and shareholders? Should holding periods be increased

---

5 Which was the recommendation of The Investment Association Executive Remuneration Working Group referred to in the Green Paper.

from a minimum of three to a minimum of five years for share options awarded to executives? Please give reasons for your answers.

No comment.

STRENGTHENING THE EMPLOYEE, CUSTOMER AND WIDER STAKEHOLDER VOICE

Question 7. How can the way in which the interests of employees, customers and wider stakeholders are taken into account at board level in large UK companies be strengthened? Are there any existing examples of good practice that you would like to draw to our attention? Which, if any, of the options (or combination of options) described in the Green Paper would you support? Please explain your reasons.

The introductory comments in section 2 of the Green Paper explain that many companies reap "enormous benefit" from "wider engagement around their business activities" and point to "economic benefits to be derived from bringing external perspectives to bear and in properly understanding and maintaining healthy relationships with interested groups". We do not disagree. The corollary is that there should be no need to make significant changes to the framework of corporate governance to force boards to do what they will understand is in the best interests of the company which they are managing. On this basis, what is needed is better explanation by boards of how these wider interests have been taken into account, as suggested in paragraph 2.2.

The relationships of companies with their non-shareholder stakeholders are governed by their own legal frameworks appropriate to the particular nature of the relationship and we suggest that the corporate governance system is not the most effective way to ensure those relationships operate effectively. Those relationships are also very diverse in their natures. They may be purely transactional, where there are many alternatives counterparties and the relationship with each is transitory. They may be closely interconnected, with a relationship of trust on both sides. They may be equal or there may be a significant disparity in bargaining power. They may be local or international. And it is likely that those relationships are dynamic, changing over time, particularly as technology changes the environment in which they exist. The complexity of the issues leads us to believe that, above all, any changes to corporate governance must provide flexibility for companies to respond according to their own circumstances.

We strongly support the importance of maintaining the unitary board system.

Option (i): Create stakeholder advisory panels

We recognise that stakeholder advisory panels may have a part to play for some companies as a means for the directors to obtain views from relevant stakeholder groups. However we think flexibility is important and companies should be allowed to establish mechanisms that suit their own circumstances. This flexibility should extend to the number of groups to be established, the composition of those groups and the matters on which their views are sought. Consultation with stakeholders groups is unlikely to be appropriate for some kinds of decisions. For example, decisions which have to be taken in a relatively short time frame or where confidentiality is particularly important may not be suitable. On the other hand, questions of values and strategy would be better suited to this kind of consultation.

Option (ii): Designate existing non-executive directors to ensure that the voices of key interested groups, especially that of employees, is being heard at board level

Allocating responsibility for supervising the collection of views from relevant stakeholder groups and reporting those views to the board to one or more designated non-executive directors may be the right approach for some companies but we see little benefit in a prescriptive approach. We agree with the comments in the Green Paper that make it clear that the company executives who are closest to its key non-shareholder stakeholders (employees, customers, its supply chain) must be involved in this process. For that reason we see the role of the nominated director as being to supervise a process actually undertaken by others. We also note the caution expressed in paragraph 2.25. It should be clear to all concerned that the director(s) involved was not their representative on the board but merely a conduit for their views and to ensure that an appropriate process was undertaken.

Option (iii): Appoint individual stakeholder representatives to company boards

We agree with the observations in paragraphs 2.26 to 2.29 and support the decision not to propose mandating direct appointment of representatives of specific interest groups to company boards.

Option (iv): Strengthening reporting requirements related to stakeholder engagement

We believe that strengthening the reporting requirement is the approach most likely to achieve real change in relation to stakeholder engagement. We would envisage disclosures starting with an explanation of the board's view of which non-shareholder constituencies are relevant and then describing how it has gone about ascertaining the effect of decisions it takes on those constituencies to ensure that in fulfilling the directors' duties under section 172 they have had regard to all relevant considerations. Coupled with a robust but proportionate enforcement regime this will require boards to take a considered decision on how wider stakeholder considerations should inform their pursuit of the success of the company in the interests of its shareholders. We also suggest that increased guidance (from the FRC or BEIS) on what section 172 requires would be helpful.

If additional disclosure requirements are imposed in this area consideration should be given to allowing that disclosure on the company's website either in addition to, or instead of, in the Annual Report. This would make the disclosure more accessible to the general public and so be more likely to increase levels of public trust.

We do not support the proposal described in paragraph 2.34, which suggests special accountability for a designated non-executive director. We think the conclusions of the board on these matters should be the responsibility of the whole board and not just one individual. We also suggest that it should be a matter for the company (in consultation with its stakeholder panel, if it has one) to determine whether a separate report from the stakeholder panel is appropriate.

Question 8. Which type of company do you think should be the focus for any steps to strengthen the stakeholder voice? Should there be an employee number or other size threshold?

We suggest that the starting point should be premium listed companies (which are subject to the Corporate Governance Code) and voluntary adherence to the same standards by companies whose shares are traded on other public markets. We do not think within this category a size threshold should be applied. We would expect any changes to the Corporate Governance Code adopted to implement reform to be adopted by all companies in this category (on a comply or explain basis). The application of these principles to privately held (i.e., non-publicly traded) companies is discussed in response to Question 10.

Question 9. How should reform be taken forward? Should a legislative, code-based or voluntary approach be used to drive change? Please explain your reasons, including any evidence on likely costs and benefits.

We suggest that reform should initially be by a code-based or voluntary approach, turning to legislation if that proves inadequate to drive better behaviour. We think in any event the scope for legislative reform should be limited to additional disclosure obligations.

CORPORATE GOVERNANCE IN LARGE, PRIVATELY-HELD BUSINESSES

Question 10. What is your view of the case for strengthening the corporate governance framework for the UK's largest, privately-held businesses? What do you see as the benefits for doing so? What are the risks to be considered? Are there any existing examples of good practice in privately-held businesses that you would like to draw to our attention?

Many large UK privately owned companies recognise the importance of good governance. They do this because it is in their interests to do so. To some extent they may be driven to do so by the ethical standards of the owner/founder, irrespective of any tangible business benefit. However, it seems to us important that they choose to do so and they are entitled as a matter of the law to choose not to do so. This view sees companies as an emanation of the individuals who are their owners and as they are free to decide to act unethically but legally in their personal lives, so should the companies they own. A more pragmatic argument is that privately held companies are inherently more mobile than those that are publicly held, having flexibility to choose whether to incorporate, and if so, in what form and in what jurisdiction to do so.

We agree with the proposition that society today has expectations about the way in which businesses should behave. Those expectations are not limited to UK incorporated companies but include all businesses carrying on business here, wherever incorporated (or even if not incorporated at all). The Modern Slavery Act is a good example of the way our society's expectations can be applied to all substantial businesses operating in the UK.

However, the proposition set out in paragraph 3.3 that "society has a legitimate expectation that companies will be run responsibly in return for the privilege of limited liability" (emphasis added) is a recent construct. Limited liability companies arose to satisfy a need for investors who did not seek active involvement in a business to contribute their capital without taking on unlimited liability. Limited companies had existed for many years before there was any suggestion that carrying on business through a corporate form of itself implies responsibilities to society.

Question 11. If you think that the corporate governance framework should be strengthened for the largest privately-held businesses, which businesses should be in scope? Where should any size threshold be set?

To the extent this is a question of corporate governance, we suggest the threshold needs to be set at a level of materiality that justifies the additional costs of compliance. That will be affected by the nature of the requirement. If the requirement is based on a voluntary code, a relatively low threshold, such as that for large companies for the purposes of the Companies Act reporting framework, would be appropriate. If, as discussed in our response to Question 13, the objective is addressed by reference to businesses rather than companies, the thresholds under the Modern Slavery Act would be suitable. We see merit in the simplicity of using one of the existing metrics used to apply different reporting requirements.

Question 12. If you think that strengthening is needed how should this be achieved? Should legislation be used or would a voluntary approach be preferable? How could compliance be monitored?

Option (i): Applying enhanced standards of corporate governance more widely

We think the approach outlined in paragraphs 3.12 to 3.16 would be worth exploring, noting in particular that any code must be suitable for the companies concerned (such that it does not lead to extensive explanations) and that adoption of a code should be voluntary. It might be worthwhile to consider whether a “kitemark” scheme could be used to encourage companies to adopt the code.

Question 13. Should non-financial reporting requirements in the future be applied on the basis of a size threshold rather than based on the legal form of a business?

Option (ii): Applying reporting standards more consistently

To the extent the objective is to encourage better behaviour by businesses operating in the UK, it makes more sense to apply non-financial reporting requirements based on business size and not legal form. This approach produces a level playing field for businesses operating in the UK and removes the advantage of incorporating abroad or using a different corporate form to avoid the application of the requirements. At the same time, however, it will be important to avoid making the UK a less attractive jurisdiction for establishing a business. We suggest that the Modern Slavery Act may provide a useful model, as it allows flexibility for businesses to decide on actions they think appropriate for their business, taking into account what matters to their important stakeholders and to report accordingly. Although not prescriptive we believe that the requirement for reporting under the Modern Slavery Act has influenced positively the behaviour of businesses.

OTHER ISSUES

Question 14. Is the current corporate governance framework in the UK providing the right combination of high standards and low burdens? Apart from the issues addressed specifically in this Green Paper can you suggest any other improvements to the framework?

We have outlined above (under "The Way Forward") a possible approach to the next phase of development of corporate governance for UK companies. We think that proposal would build on the existing framework and minimise the risk of unintended negative consequences. It would avoid adversely affecting the competitiveness of UK companies or the attractiveness of UK companies to investors. Increased transparency will encourage UK companies to demonstrate the behaviour that will deserve the trust of the public. Additional enforcement, if necessary, should be focussed on the quality of disclosures.

Some have suggested that we need a mechanism to allow stakeholders other than shareholders to obtain a remedy when their interests are not adequately taken into account in decisions by directors[6]. We do not think the time is right for the creation of a regulator or other mechanism for this purpose. As we have explained in our introductory comments, such a mechanism is unlikely to deliver the change that is sought without a change in the terms of the statutory duty and even then may serve little purpose without fundamental changes in the relationships of boards with their shareholders. Changes of this kind could have profound effects on the effectiveness of boards, the willingness of talented individuals to accept directorships and the attractiveness of UK companies to investors. The proponents of this radical change suggest that taking stakeholder views into account makes companies more successful. If that is the case, a regime that encourages boards to do so, without the straightjacket of additional regulation, is likely to lead to voluntary (and therefore more effective) adoption of best practice.

Contact details:

Please contact **William Underhill** (william.underhill@slaughterandmay.com; 0207 090 3060) if you have any questions on our submissions.

[6] See for example the public letter sent by the International Corporate Governance Network, the Institute of Directors, ICSA/the Governance Institute and the TUC to the Prime Minister dated 24 January 2017