The City of London Law Society

The Law Society

Law Society and City of London Law Society comments to the Companies (Miscellaneous Reporting) Regulations 2018 - Q&A (BEIS)

September 2018

Preface

These comments are provided by the Company Law Committee of The Law Society of England & Wales ('the Society') and members of the City of London Law Society (CLLS). The Society is the professional body for solicitors in England and Wales, representing over 170,000 registered legal practitioners. The Society represents the profession to parliament, government and regulatory bodies and has a public interest in the reform of the law. 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 specialists committees.

Comments on The Companies (Miscellaneous Reporting) Regulations 2018
Frequently Asked Questions

1 SECTION B. SCOPE

Inclusion of a table showing the application of the various new requirements is helpful, but we note that there are a few areas where the suggested application is incorrect or confusing as set out below:

1.1 Row (i) [Regulation 4]

We feel it would be helpful to clarify the treatment in group situations, including referring to the exclusions from being treated as medium-sized under section 467(1)(c) and 467(2) of the Companies Act 2006. For example, although the Section 172(1) statement is considered on an individual company basis, a company that is part of an ineligible group because say there is a traded company within the group will have to prepare a statement even if it meets the criteria listed in the table for being medium-sized.

1.2 Row (ii) [Regulation 13]

It would be helpful to note that where the company is a parent company it is the number of employees in the group and not just the company itself that is used (per new paragraph 11A(4)).

1.3 Row (iii) [Regulation 13]

It is not correct to suggest that this test is identical to that at Row (i), as the criteria are the specific quantitative criteria set out in the new paragraph 11C. The test for application in paragraph 11C is entirely based on the size criteria, whereas the test referred to in row (i) is, as explained in paragraph 1.1 above, by reference to whether the company qualifies as a medium-sized company under sections 465 to 467 of the Companies Act 2006, which imposes other

tests; including whether the company is a member of an ineligible group. Therefore, companies that are required to include a section 172 statement in their strategic report may nevertheless not be required to include a statement in their directors' report about suppliers, customers etc.

It would also be helpful to note that (in contrast to row (ii)) the employee threshold of 250 employees refers only to employees of the relevant company and not, if it is a parent company, to the number of employees in the group; there is no equivalent to the new paragraph 11A(4) within paragraph 11C.

1.4 **Row (iv) [Regulation 14]**

The statement that companies already required to report on their corporate governance arrangements are not within scope is misleading. The exemption only applies to companies required to publish a DTR7 statement and not for example to companies traded on AIM, which must from 28 September 2018 apply a recognised corporate governance code and publish a statement explaining this under the revised AIM Rule 26.

2 SECTION D: REPORTING ON MATTERS IN SECTION 172(1) OF THE COMPANIES ACT 2006

2.1 Question 1

2.1.1 To avoid confusion, we suggest acknowledging that AIM traded companies are also required to make their annual reports available on a website under AIM Rule 26, with reference to the second paragraph of the answer to Q1.

2.1.2 It would be helpful to make specific reference to the carve out from having to report on matters which are commercially sensitive in respect of the information required to be included within the directors' report pursuant to Regulation 13, as this will be a key consideration for companies considering the reporting requirements. It should be made clear that the carve out does not apply to the Section 172(1) statement to be included within the strategic report; there are no equivalent provisions under Regulation 4.

2.2 Question 2

[*No comment*.]

2.3 Question 3

[*No comment*.]

2.4 Question 4

[*No comment*.]

2.5 Question 5

[*No comment*.]

2.6 Question 6

It is not correct to state that the UK Corporate Governance Code "requires" companies to have in place a director appointed from the workforce, formal workforce advisory panel or a designated non-executive director. The UK Corporate Governance Code, at Provision 5, states that one or a combination of those methods should be used, but that alternatively the board may explain what other alternative methods are in place.

2.7 Question 7

[*No comment*.]

2.8 **Question 8**

[*No comment*.]

2.9 **Question 9**

The final two sentences should be removed as they are unhelpful and represent a misleading interpretation of directors' duties.

The legal framework for directors' duties rests on the primacy of shareholder interests. Directors have a duty to promote the success of the company for the benefit of its shareholder(s), which in the case of a subsidiary is its parent company. Directors of a subsidiary must promote the interests of its parent company (as shareholder) whilst the company continues to be solvent (i.e. prior to any insolvent situation under which the duties of the directors are instead owed first to its creditors).

Furthermore, a parent company can for example formally direct the directors of a subsidiary undertaking to take, or refrain from taking, certain actions and remove and replace the directors if they act contrary to its wishes.

2.10 **Question 10**

The reference in the final sentence to "*cross-references to group statements and policies*" suggests that it includes the group "Section 172(1) Statement" of the relevant member of the group, rather than just specific policies (e.g. whistleblowing policy). If that is the intention, the answer should be made more clear accordingly.

2.11 **Question 11**

[*No comment*.]

2.12 **Question 12**

[*No comment*.]

3 SECTION E. REPORTING ON CORPORATE GOVERNANCE ARRANGEMENTS IN LARGE PRIVATE AND UNLISTED PUBLIC COMPANIES

3.1 Question 1

The requirement under paragraph 26(1)(c) is to state "*if the company departed from any corporate governance code reported under sub-paragraph (a), the respects in which it did so, and its reasons for so departing*". We feel that the statement that "*If the company has departed from any aspect of the code it must set out the respects in which it did so*…" could be interpreted as a more onerous requirement than that set out in the regulations, and does not align well with the concept of a code of principles, provisions and related guidance; for example, departure from an aspect of guidance does not necessarily mean a departure from the relevant principle.

We feel that the answer should be better aligned with the regulations as follows:

"*If the company has departed from ~~any aspect of~~ the code it must set out the respects in which it did so*…"

It could alternatively be amended to refer to departing from any aspect of the principles of the code, rather than any aspect of the code, but we feel that may not be sufficiently flexible to provide for different code structures, and as noted does not align with the primary requirement in the regulations.

3.2 Question 2

This answer should refer to the ability to include the statement within the strategic report under section 414C(11) of the Companies Act 2006.

3.3 Question 3

[*No comment*.]

3.4 Question 4

[*No comment*.]

3.5 Question 5

[*No comment*.]

3.6 Question 6

It will be helpful to update the answer to this question.

3.7 **Question 7**

[*No comment*.]

3.8 **Question 8**

The second paragraph is misleading in the context of parent-subsidiary relationships in a similar way to the answer to Question 9 of Section D (on which, see our comments above). As we note in our comments above, directors of subsidiaries have a duty to promote the success of the company for the benefit of the parent undertaking.

We do not feel that there is any need to retain the paragraph in amended form, as the remaining two paragraphs are sufficient to explain that the requirement does apply to subsidiaries and that reporting amongst group companies will be dependent upon the relevant companies' circumstances.

3.9 **Question 9**

We have no comments on this question, but feel an additional question in relation to AIM traded companies may be helpful, to confirm that even though they are required to similarly publish their compliance against a code under the revised AIM Rule 26 they will still be subject to these requirements where they meet the qualifying criteria.

3.10 **Question 10**

[*No comment*.]

3.11 **Additional Questions**

We suggest that the following additional questions should be covered in Section E:

3.11.1 **Corporate governance statement as separately identifiable statement and how to make it available on a website**

We feel that it would be helpful to make clear that the answers to Questions 7 and 8 in Section D (in respect of the section 172(1) statement) apply equally to the corporate governance statement; we assume that the same approach should apply to both statements. This could be done by repeating the questions in similar form in Section E.

3.11.2 **Application of thresholds within groups**

We feel that guidance should be provided to clarify that the thresholds the qualifying conditions, in contrast to Regulation 13 for reporting on engagement with employees, are calculated by reference to the company and not the wider group.

We would suggest that questions along the following lines could be added:

"*Q*. What if a company operates as a Group? In calculating the threshold of more than 2,000 employees, do you count the employees in the parent company, at a subsidiary level or across the group as a whole?*

Companies should determine the number of global employees at an individual level for each relevant company. So, for example: (i) if each individual company within the Group has 2,000 or fewer employees, but the Group in aggregate has more than 2,000 employees globally (spread across different companies in the Group), no reporting will be necessary; and (ii) if one subsidiary in the group has more than 2,000 employees and all other group companies have 2,000 or fewer employees, only that one subsidiary, and not the parent company nor any other subsidiary, will have to report. This is a different test, applied differently, from the test for the pay ratio reporting requirement, where the threshold of 250 UK employees is applied across the Group as a whole for parent companies (see question 6 in Section F)."

"*Q*. Similarly, in calculating the turnover and balance sheet thresholds where a company operates within a Group, do you look across the Group as a whole or only at individual companies?*

The turnover and balance sheet thresholds should be determined at an individual company level only. No aggregation across a Group is required for these thresholds."

4 SECTION F. EXECUTIVE PAY – PAY RATIO REPORTING

4.1 Question 1

[*No comment*.]

4.2 Question 2

[*No comment*.]

4.3 Question 3

[*No comment*.]

4.4 Question 4

[*No comment*.]

4.5 Question 5

[*No comment*.]

4.6 Question 6

[*No comment*.]

4.7 Question 7

[*No comment*.]

4.8 Question 8

[*No comment*.]

4.9 Question 9

[*No comment*.]

4.10 Question 10

[*No comment*.]

4.11 Question 11

[*No comment*.]

4.12 Question 12

[*No comment*.]

4.13 Question 13

[*No comment*.]

4.14 **Question 14**

[*No comment*.]

4.15 **Question 15**

[*No comment*.]

4.16 **Question 16**

[*No comment*.]

4.17 **Question 17**

It would be helpful if the answer referred to the prescribed statement mandated by the regulations under paragraph 19C(6)(b) in respect of years where the reporting requirement did not apply.

4.18 **Question 18**

[*No comment*.]

4.19 **Question 19**

[*No comment*.]

4.20 **Question 20**

[*No comment*.]

4.21 **Question 21**

[*No comment*.]

4.22 **Question 22**

This answer should be corrected to refer to “employees” rather than “workforce”. “Workforce” is not a term defined in law or regulation, and for example the FRC’s Guidance states that in the context of the UK Corporate Governance Code it is not meant to align with legal definitions of workforce, employee, worker or similar. Both the current and amended reporting requirements use the term “employee” (including paragraph 38 of Schedule 8 of the Accounting Regulations as currently in force), and so this document should use the same term to avoid confusion.

5 SECTION G. EXECUTIVE PAY – SHARE PRICE IMPACT REPORTING

5.1 Question 1

[*No comment*.]

5.2 Question 2

It would be helpful to refer to the term "quoted company" as well as the explanation of that term, for example:

"*Those companies that prepare directors' remuneration reports, being "quoted companies", i.e. all UK incorporated*…"

5.3 Question 3

[*No comment*.]

5.4 Question 4

[*No comment*.]

5.5 Question 5

[*No comment*.]