

2018 AGM and reporting season: what to expect

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This briefing summarises developments for companies to consider when preparing for their 2018 annual general meetings and compiling the narrative aspects of their annual reports and accounts. It is aimed principally at premium listed companies. It may also be useful for AIM companies who choose voluntarily to comply with the UK Corporate Governance Code and/or any other aspects of legal or regulatory requirements applying to listed companies.

On the AGM front, the key development concerns the newly published views of the UK Investment Association and US-based Institutional Shareholder Services on virtual-only and hybrid AGMs.

On the narrative reporting front, the key development impacting this season's annual reports, as we have highlighted previously, is the additional disclosures required from certain large companies by the new non-financial reporting regime.

We also look at future developments for those who want or need to prepare for them, or be early adopters. In particular, we consider the proposed new reporting requirements that the Government plans to introduce and also the proposed new UK Corporate Governance Code which could require board changes for some companies.

The briefing ends with an appendix of key 2017 publications and links which may be useful to companies both for the 2018 AGM and reporting season and also more generally.

2018 AGM ISSUES

2018 AGM ISSUES

- Virtual-only and hybrid shareholder meetings
- Changes to articles of association
- Pre-emption disapplication resolutions
- IA Public Register
- Miscellaneous

Virtual-only and hybrid shareholder meetings

Guidance has recently been issued by both the UK Investment Association and by Institutional Investor Services, the US provider of corporate governance services, on "virtual-only" shareholder meetings (ie where there is no physical meeting) and "hybrid" shareholder meetings (i.e. where shareholders can choose to participate either at a traditional physical meeting or on-line after downloading software and/or through certain recent versions of specified web browsers).

The Investment Association (IA). In December 2017, the IA issued a [position statement](#) on virtual-only AGMs, stating that it does not believe them to be in the best interests of all shareholders and that they should not be used by investee companies as their use could be detrimental to board accountability. Key points in the IA's position statement include the following.

IA position statement on virtual-only shareholder meetings

- IA members will not support amendments to articles of association in relation to electronic AGMs if they allow for virtual-only AGMs.
- The IA, via its Institutional Voting Information Service, will red-top any company that will have the ability to hold virtual-only meetings following any amendments to articles of association.
- IA members expect any amendments to articles of association to confirm that a physical meeting will be held alongside any electronic meeting element (a "hybrid" meeting).

In its rationale for its position, the IA notes that investors believe that the public nature of the AGM and full attendance by the board is important to allow them to bring matters to the attention of the board and that removing this will impair their ability to hold boards to account on behalf of their clients. The IA also notes that in virtual-only meetings it is harder for participants to identify the views of fellow participants and register their own agreement or disagreement. Also, virtual-only meetings risk giving the impression that the company is attempting to filter questions or participation. Whilst stating that technology such as webcasting to complement the physical meeting could be beneficial, the IA notes that investors believe that technology should only be used in parallel with the physical meeting.

Institutional Shareholder Services (ISS). ISS, as part of its [policy updates](#) and [voting guidelines](#) for the 2018 season, has added a new recommendation on virtual-only and hybrid shareholder meetings. In describing its rationale, ISS notes that opinion is divided and that concerns include the possibility that virtual-only meetings may hinder meaningful exchanges between management and shareholders and enable management to avoid uncomfortable questions.

ISS key recommendations on virtual/hybrid shareholder meetings

- ISS will generally recommend voting for proposals that allow for the convening of hybrid meetings if it is clear that it is not the intention to hold virtual-only meetings.
- ISS will generally recommend voting against proposals that allow for the convening of virtual-only meetings.

Practical points on hybrid AGMs. Even ruling out, for now, virtual-only AGMs, a number of points should be noted before companies consider holding hybrid meetings.

- **Articles of association** will still need to be reviewed, and likely amended, before holding an AGM in this way.
- **The planning process** should still be started early with significant extra lead time allowed for preparation, testing and rehearsals and with the involvement of advisers including in particular the company's registrars.

Although different considerations will apply for different companies, relevant factors on whether to hold hybrid meetings might include:

- **Costs and time.** Is there awareness of the additional legal, IT and other costs and management time commitment that a physical meeting plus an electronic add-on is likely to entail?
- **Attendance.** Are there shareholders who do not currently attend, who would attend electronically, hence making it worthwhile?
- **Questions.** Are there commonly many questions and or comments and can current technology effectively facilitate and manage these? Having a virtual element to a meeting, with non-face to face communications, may make the chair feel less in control of the virtual element where attendees' inhibitions might be let loose, facilitating disruption, with the meeting being more unpredictable.
- **Uncertainty.** The virtual element, being an IT one, involves the usual IT risks: risk of failure or hacking. More significantly, there may be uncertainty as to whether failure of all or part of the IT element would render void the whole meeting i.e. including the physical element and whether it would be necessary to reconvene the meeting at a later date. It may not even be apparent at the time of the meeting to the chair that the IT element of the meeting has failed or whether failure is due to the shareholder's IT or the company's or simply a hostile group falsely claiming technology failure. To have a virtual meeting there is a requirement for the shareholder to be able to (a) hear the proceedings; (b) speak in some way; (c) have access to documents available for inspection at the meeting; and (d) vote. Any of these elements could fail and if one contrasts this with the gremlins that sometimes lurk on a simple conference call, the risks are evident.
- **Articles of Association.** As mentioned, in order to have a virtual element, it will be necessary to alter articles. Various solutions to the risks of IT failure are in practice attempted within articles but currently there is no clear consensus as to the best market practice to achieve this. Companies may be

best advised to delay amending articles until the position is more settled.

- **Reaction.** We understand a rising number of shareholder meetings in the US are virtual-only meetings, as opposed to only one so far in the UK. However, there have been recent press reports noting (in addition to the views of ISS) the views of US groups against virtual-only meetings as well as the filing of resolutions at ConocoPhillips and Comcast calling for a return to physical meetings.
- **Easier fix.** Companies could bear in mind that a much easier option – requiring no legal changes, no such risks and minimal operational disruption to the company (and one which several companies have already adopted) - is to allow a webcast of the meeting to take place and be available to shareholders. This will not constitute part of the meeting and shareholders viewing the webcast will not be able to vote but will nonetheless be able to see and hear what is going on. Several companies currently stream a live webcast on their website, which is publicly available to internet users and is sometimes available to view online after the AGM. Companies doing so usually include a warning in their Notice of AGM that the proceedings will be filmed and that they reserve the copyright in this material.

Changes to articles of association

Somewhat more companies amended their articles of association in 2017 than in 2016. The most common change, again, was to increase the cap on non-executive director fees. Other changes include: introducing the ability to make shareholders receive their dividends by bank transfer only (although some companies have taken this power, very few are actually doing this) (for detail see our [2016 AGM season briefing](#)); changes to reflect the accepted practice of annual director re-elections; changes to borrowing powers; changes as regards untraced shareholders; and a few companies that made changes for electronic AGMs (before publication of the IA and ISS guidance noted above).

As we mentioned last year, a particular area for companies to consider concerns new accounting rules in IFRS 16, requiring

operating leases to be included as assets and liabilities on balance sheets. These rules are required to be adopted by companies for accounting periods beginning on or after 1 January 2019. As part of their conversations with their auditors about the effects of IFRS 16, companies should consider whether IFRS 16 may require (if operating leases are material for a company) (a) amendment of its borrowing limits in its articles of association; and (b) amendment of performance targets in share incentive schemes (because IFRS 16 will substitute depreciation and interest for rental payments). IFRS 15 (revenue recognition) may also require changes eg to performance targets, as it can reduce profits. Both IFRS 15 and 16 may also impact distributable reserves.

Pre-emption disapplication resolutions

In May 2017, the Pre-Emption Group published its [annual monitoring report](#) on implementation of its 2015 statement of principles for disapplying pre-emption rights and its 2016 template resolutions for use by companies seeking to disapply pre-emption rights by up to 5 per cent generally and up to a further 5 per cent for an acquisition or specified capital investment. The report states that the statement and resolutions have generally been adhered to although notes examples of poor consultation and disclosure. The group has issued an Appendix of Best Practice in Engagement and Disclosure to help companies.

Best practice in engagement and disclosure – some key points
<ul style="list-style-type: none"> Companies should only seek the additional five per cent disapplication authority when appropriate for their circumstances.
<ul style="list-style-type: none"> Where possible, companies should signal an intention to undertake a non-pre-emptive issue at the earliest opportunity and establish dialogue with shareholders.
<ul style="list-style-type: none"> Consultation about a proposed issue should be specific and unequivocal and with a wide range of shareholders.
<ul style="list-style-type: none"> The additional five per cent disapplication must only be for an acquisition or specified capital investment as described in the statement. Issues for other reasons are not consistent with the statement (including cash box placings).

Additionally, in a [press release in July 2017](#), the Pre-Emption Group confirmed that notwithstanding the new 20 per cent exemption from having to produce a prospectus which was introduced by the Prospectus Regulation, the IA and the Pensions and Lifetime Savings Association continue to support the current ten per cent overall limit on pre-emption disapplications effected by way of two separate five per cent resolutions and no change to this is expected.

IA Public Register

IA Public Register
<ul style="list-style-type: none"> The IA Public Register was launched in December 2017 and will be updated on an on-going basis.
<ul style="list-style-type: none"> It is an aggregated list of publicly available information regarding meetings of companies in the FTSE All-Share Index which have received significant shareholder opposition votes (of 20 per cent or more) to proposed resolutions or who have withdrawn a resolution prior to the shareholder vote.
<ul style="list-style-type: none"> The register will feature the name of the company, a description of the resolution, the result of the vote, a link to the AGM results announcement (including any E.2.2 statement) and a link to any further statement made by the company on actions taken since the vote.

The register aims to increase transparency, accountability and scrutiny of listed companies by shareholders, the media and the wider public. Analysis of this first set of data reveals, amongst other things, that:

- Over one fifth (22 per cent) of FTSE All-Share companies feature on the register.
- Pay-related resolutions feature most (38 per cent).
- The second most frequent type of resolution on the register is the re-election of directors (32 per cent).
- Just under one third of companies on the register have published a response on how they are addressing shareholder concerns in response to an IA letter sent in October 2017.

A related point on remuneration resolutions is worth remembering here. If a vote on the directors' remuneration report was not passed at a company's last AGM, and at that AGM no remuneration policy vote was put to the vote, then a remuneration policy must be put to the vote at this AGM (if it is not dealt with at an earlier general meeting) (section 439A(2)).

Miscellaneous

Auditor resolutions. As regards the resolution to appoint/re-appoint auditors, companies should continue to consider their compliance with the Competition and Markets Authority [Statutory Audit Services for Large Companies Order 2014](#) (requiring tendering of the audit contract at least every ten years and certain disclosures in the annual report) (the Order) and the Companies Act 2006 as amended by the EU audit reforms (requiring removal of the auditor at least every 20 years assuming a tender has taken place by the ten year point, but with complex transitional provisions). If either or both apply, it may mean companies need to prepare for and tender the audit contract before the next or a subsequent AGM.

In addition, whether or not a new auditor is to be voted on, due to changes to the Companies Act 2006 (section 485A), specified disclosures must be made in, for example, the explanatory notes to the resolution.

On the resolution to approve the remuneration of auditors, in recent years we have seen many, but not all, resolutions move away from authorising directors to set remuneration of auditors, to instead authorising the audit committee to set it. (The Order states that only the audit committee may negotiate and agree the audit fee and the FRC, in its Guidance on Audit Committees, states that the audit committee should approve auditors' remuneration.)

Shareholder requisitioned resolutions. In 2017, we are aware of only two shareholder-requisitioned AGM resolutions. Shareholders requisitioned a resolution at Royal Dutch Shell plc's AGM concerning setting and publishing targets for greenhouse gas emissions. Also, at BHP Billiton plc, due to shareholders in Australian BHP Billiton Limited (the two companies being in a dual listed company

structure) having requisitioned two resolutions, BHP Billiton plc added the resolutions to its already published AGM notice by way of a supplemental notice. Both resolutions failed.

2018 NARRATIVE REPORTING ISSUES

2018 narrative reporting issues

- Non-financial reporting
- Diversity reporting
- FRC publications
- IA publications
- Other UK and US voting guidelines
- Miscellaneous reporting requirements

Non-financial reporting

In our [2017 AGM season briefing](#), we wrote in detail about the [EU Directive on Disclosure of Non-financial and Diversity Information \(2014/95/EU\)](#) (the Directive) and its implementation by (i) [the Companies, Partnerships and Groups \(Accounts and Non-Financial Reporting\) Regulations 2016](#) (the regulations) and (ii) changes to the Disclosure Guidance and Transparency Rules (DTRs) (see next article for DTRs aspects). We have also written in our 2017 Quoted Company Newsletters about FRC publications issued to assist companies with reporting in these areas, namely a [Factsheet](#) in July and [Frequently Asked Questions](#) (FAQS) in December.

The regulations amend the Companies Act 2006 by adding new sections 414CA and B requiring disclosures by way of the non-financial information statement (NFIS), effective for certain listed groups (therefore not AIM companies, unless they are banks or insurance companies) with more than 500 employees) for financial years beginning on or after 1 January 2017. Although the NFIS has a significant overlap with the existing strategic report disclosure requirements for quoted companies, there are key differences and relevant companies should review their existing disclosures and add in any new disclosures.

We set out below a brief summary of key points (for more detail generally see our [September](#) and [December](#) 2017 newsletters).

Non-financial reporting key points – general and FRC FAQs
<ul style="list-style-type: none"> • What companies are covered by the Regulations? The FAQs contain a useful flowchart to assist companies with the interplay between pre-existing section 414C (7) (the existing "enhanced strategic report" requirements for quoted companies) and new section 414CB on the non-financial information statement. It confirms, for example, that for non-parent companies with 500 or fewer employees, there is no change in their reporting, but that for all traded companies (eg listed companies) and also for banking and insurance companies (whether traded or not) with over 500 employees, the regulations apply.
<ul style="list-style-type: none"> • What are the new requirements. The FAQs mention the need to include "to the extent necessary for an understanding of the company's development, performance and position and the impact of its activity" information on: environmental matters (including impact); employees: social matters; respect for human rights; and anti-corruption and bribery matters. <p>This must include, in relation to the above areas, descriptions of: policies and their outcomes; due diligence processes; and principal risks in connection with the above matters. Additionally, where proportionate, there should be a description of its business relationships, products and services which are likely to cause adverse impacts and how the company manages the principal risks.</p>
<ul style="list-style-type: none"> • For existing quoted companies, what are the new disclosures? The most significant new disclosures are described as those on: the impact of the company's activities (ie the effect it has externally); anti-bribery and anti-corruption matters; principal risks; business relationships, products and services which are likely to cause adverse impacts; and due diligence.
<ul style="list-style-type: none"> • Materiality. Disclosures are only required if material, which the FRC see as a proxy for "to the extent necessary for an understanding of the company's development, performance, position and the impact of its activity".

Diversity reporting

Diversity reporting under the DTRs. As mentioned, the Directive also deals with reporting on diversity. These elements of the Directive have been implemented by way of new DTRs 7.2.8A and B, which will require for relevant issuers, broadly large listed companies, similar information on diversity matters to those already covered by provision B.2.4 of the UK Corporate Governance Code, but again with a few differences that mean companies in scope should check that their diversity reporting in their 2017 accounts complies, bearing in mind in particular that the DTRs are mandatory and not comply or explain.

DTRs 7.2.8A and B – key requirements to be described
<ul style="list-style-type: none"> • The diversity policy applied as regards for instance age, gender or educational and professional backgrounds. (This is wider than B.2.4 of the UK Corporate Governance Code in that it goes beyond gender.)
<ul style="list-style-type: none"> • If there is no policy, an explanation as to why not.
<ul style="list-style-type: none"> • The policy's objectives. (Unlike B.2.4, this assumes there are objectives.)
<ul style="list-style-type: none"> • How the policy has been implemented. (This is also wider than B.2.4.)
<ul style="list-style-type: none"> • Results in the reporting period.

For more detail on the DTRs, see our [September 2017 newsletter](#).

Reporting on diversity on boards – Hampton/Alexander supplementary report.

In our 2017 AGM season briefing, we wrote about the issue by the Hampton-Alexander Review of its FTSE Women Leaders report with its recommendations for diversity targets across boards and across executive committees and their direct reports. In November 2017, the Review published a [supplementary report](#) on improving gender balance in FTSE leadership. For more on the progress in meeting the targets, see our [December 2017 Quoted Company Newsletter](#).

Most companies now submit to the Review their data on achievement of the targets and many also note diversity achievements in their annual

reports. Given the now mandatory diversity reporting required by the DTRs, as mentioned above, this is likely to increase.

A change that the Review steering group has decided to make is to extend the target of 33 per cent women across executive committees and their direct reports to FTSE 250 companies (as well as FTSE 100 companies). Such companies will want to consider whether to adopt and report on the newly applicable target.

Reporting on ethnic diversity: the Parker Review Committee final report. We also noted in our 2017 AGM briefing that the Parker Review Committee had published a consultation version of its report on the ethnic diversity of UK boards. In October 2017, the [final report](#) was published.

Ethnic diversity reporting – key points
<ul style="list-style-type: none"> Increasing the ethnic diversity of boards to have at least one director of colour by 2021 for FTSE 100 companies and by 2024 for FTSE 250 companies.
<ul style="list-style-type: none"> Developing and promoting candidates of colour in the pipeline of board candidates.
<ul style="list-style-type: none"> Enhancing transparency and disclosure. For example, the description of the board's policy on diversity in its annual report should include the company's efforts to increase ethnic diversity in its business and on its board and companies that do not meet the board composition targets by the suggested dates should explain why not.

FRC publications

Summary of key developments for 2017/2018 annual reports. In October 2017, the FRC wrote its annual summary of key developments for annual reports in its [end-of-year letter to audit committee chairs and finance directors](#). It covers aspects of annual reporting where companies should improve and highlights changes to reporting requirements.

At the same time, it published its [annual review of corporate reporting](#) covering much the same ground as the end of year letter, but in more detail. On narrative reporting, some key points from both documents, are set out opposite.

FRC key points for annual reports
<ul style="list-style-type: none"> Strategic reports. These remain subject to much FRC challenge. Companies are encouraged to improve where there is a lack of disclosure or a lack of balance and also to explain the relationships and linkages between different disclosures, for example, between key performance indicators and remuneration policies.
<ul style="list-style-type: none"> Drivers of value and long-term success. Companies should be transparent about their key sources of value, how they are managed and how value is likely to be generated. They should also consider broader drivers of value that contribute to the long-term success including those not recognised in the financial statements such as a highly-trained workforce and stakeholder engagement.
<ul style="list-style-type: none"> Performance reporting. The FRC commonly identifies reports where not all key aspects of performance have been considered. Companies should explain changes to key performance indicators and make clear, company-specific disclosures.
<ul style="list-style-type: none"> Brexit disclosures. Whilst a consistent theme is of continuing uncertainties and it being too early to measure longer-term effects, companies are starting to identify in more detail the likely risks. Companies should disclose their latest analysis of how their assessment of the potential impact on their business has developed over the year.
<ul style="list-style-type: none"> Risk reporting and viability statements. Investors are calling for differentiation in time periods for viability statements used by different companies and sectors bearing in mind the broad range of factors that should be taken into account and not just the company's medium-term business plan. See the FRC Lab report (noted overleaf) for more detail.
<ul style="list-style-type: none"> Dividend disclosures. 48 per cent of FTSE 100 companies and 30 per cent of FTSE 250 companies are now reporting information either on the level of distributable reserves or that distributable reserves are sufficient or significant. This area continues to attract investor focus and the FRC urges companies to adopt the recommendations in the October 2017 FRC Lab study on dividends (mentioned overleaf), in particular reporting on capacity to pay dividends, including how distributions might flow to the top company and the extent of any restrictions.

FRC Lab reports. In 2017, the FRC Lab issued project reports on the following areas:

- **Risk and viability reporting.** Amongst other things, this report highlights the importance of principal risk reporting which: is specific to the company; is clearly linked to its business model; shows any change in risk year on year; and gives some indication of the potential impact of risks occurring. On viability statement reporting, the report highlights for example that investors are looking for companies to: explain their long-term prospects more clearly; to consider their prospects over the longer term relative to their specific business; and to give information on the stress and scenario testing that has been done on the company's resilience to risk.
- **Disclosure of dividends – policy and practice.** This [report](#) examines how companies have responded to the Lab's 2016 report on disclosure of dividends including how dividend disclosure have improved, examples of developing practice and opportunities to take things further.
- **Audit committee reporting.** This [report](#) by the FRC's audit and assurance Lab (AA Lab) looks at external reporting by audit committees. It considers how investors' confidence in audit is enhanced by, and audit quality promoted through, reporting by audit committees in the annual report and it also updates views of good practice on audit committee reporting. The report covers most of the aspects that audit committees deal with including: appointment; tendering; independence and effectiveness of the external auditor; reporting on significant issues; and internal control and risk management.
- **Digital future of corporate reporting.** This [report](#) relates to financial reporting, rather than narrative reporting, and looks at how corporate reporting can be improved using technology, specifically the use of "eXtensible Business Reporting Language" (XBRL) tagging of financial statements which will make them more accessible and

machine-comparable for use by investors as they make their investment decisions.

Investment Association publications

IA principles of executive remuneration. In November 2017, the IA published its annual update of its [principles of executive remuneration](#) (the principles) ahead of the 2018 AGM season. Changes from the previous version are not substantial and include: the insertion of new guidance on relocation benefits; updating the section on annual bonuses, including on disclosing bonus targets and deferring bonus payments; and reorganisation of the section on long-term incentive schemes, to give a clearer picture of members' attitudes to specific scheme types.

The [accompanying letter](#) to remuneration committee chairs of FTSE 350 companies highlights certain items of focus for the IA's members in 2018.

IA key items of focus
<ul style="list-style-type: none"> • Levels of remuneration. This covers, for example, restraint on variable pay increases, justification of levels of pay taking account of the wider social context, pay ratio disclosures and pensions disparity.
<ul style="list-style-type: none"> • Remuneration structures. This includes noting the need for flexible structures appropriate to the business and also the concern that in some cases new remuneration structures are only proposed when the current ones are not paying out to executives.
<ul style="list-style-type: none"> • Shareholder consultation. This notes that the consultation process can be improved in some cases and that where resolutions have been withdrawn before AGMs, companies should conduct a full analysis of shareholder feedback and consult further before re-submitting their remuneration policies.
<ul style="list-style-type: none"> • Pay for performance. This includes that greater transparency will be expected on financial targets as well as on personal and strategic performance targets to show the link between pay and performance which investors will closely scrutinise.

Investment Association guidance on long-term reporting. In May 2017, the IA published new [guidance on long-term reporting](#). It is intended to complement the Companies Act 2006 strategic reporting regime and the FRC's Guidance on the Strategic Report. The guidance is for companies with a premium listing, but companies with a standard listing or AIM or High Growth Segment companies are encouraged to adopt it. It sets out detailed recommendations in the key areas noted below.

IA guidance on long-term reporting
• Business model and long-term reporting
• Productivity
• Capital management
• Material environmental and social risks
• Human capital and culture

The Institutional Voting Information Service, the corporate governance research arm of the IA, will start monitoring implementation of the guidance for annual reports for year-ends on or after 30 September 2017, and will outline to IA members those companies that continue to adopt short-term reporting models.

Other UK and US guidelines

The Pensions and Lifetime Savings Association (PLSA). In [Hidden Talent: what do companies' annual reports tell us about their workforce](#), the PLSA and Lancaster University examine corporate reporting on employment models and working practices across the FTSE 100. The report looks at the following areas as key for investors as regards the workforce: composition; stability; skills and capabilities; and engagement levels.

It concludes that there are substantial variations in the quality of reporting on the workforce and that the onus is on companies to provide better information and on investors to ask for it. It encourages both to engage with recent initiatives for better reporting such as the [PLSA stewardship toolkit for pension funds – understanding the worth of the workforce](#) issued in 2016 and the IA long-term reporting guidance (mentioned above).

In January 2018, the PLSA issued its updated [Corporate Governance Policy and Voting](#)

[Guidelines](#) which aim to promote the long-term success of the companies in which the PLSA's members invest and ensure that boards and management of such companies are held accountable to shareholders, such as pension funds.

PLSA governance policy and voting guidelines 2018 – key changes

- **New section on sustainability.** Amongst other things, the new section suggests shareholders should not support re-election of the chair where, after attempts by shareholders to engage, companies fail to provide a detailed risk assessment on, and response regarding, the effect of climate change on their business and fail to incorporate appropriate expertise on the board. The new section also suggests that shareholders should consider voting against the annual report or the re-election of the chair where they believe that key stakeholder relationships are being neglected.
- **Audit and audit committees.** Changes include: the need for members of the audit committee to be independent not only of executives but also of the auditor; considering a vote against the audit committee chair and auditor where an auditor has been in place for more than 20 years; mention of the need for professional scepticism by auditors; and that companies should spend no more than 50 per cent of the audit fee on non-audit services (or a material monetary sum - £500,000) absent an explanation of exceptional circumstances.
- **Employment model and working practices.** A strengthening of the guidelines here so that failure to provide a fair and balanced explanation of the composition, stability, skills and capabilities and engagement levels of the workforce would render a vote against the annual report to be appropriate.

Institutional Shareholder Services (ISS). ISS, the influential US provider of corporate governance services has issued its [policy updates](#) and [voting guidelines](#) for the 2018 season. As mentioned in the AGM section earlier, the key change is its new guidance on virtual-only and hybrid AGMs.

Another area of change worth pointing out is "overboarding" (the holding of too many other

positions). Here, ISS has simplified its wording on the positions it considers acceptable for a director to hold (but still recommending that more than five mandates at listed companies will be considered overboarded). It has also changed its wording as regards a chairman who is "overboarded" and when it would recommend targeting the chair position itself.

Other changes on audit and remuneration committees, threshold levels for long-term incentive plans and share issuances without pre-emption are described as clarificatory.

Glass Lewis. Glass Lewis, another US provider of governance services, has also issued its [2018 proxy guidelines](#). Areas of update that it highlights in its Summary of Changes for the 2018 UK Policy Guidelines include the following.

- Board diversity and skills.
- Remuneration.
- Company responses to shareholder dissent of more than 20 per cent.

Glass Lewis has not added anything on virtual-only AGMs to its UK guidelines. In its updated US guidelines it states that whilst in 2018 it will not make recommendations solely on the basis of a company holding a virtual-only AGMs, it has concerns about the ability of shareholders to meaningfully communicate with management. Therefore, in its 2019 US guidelines it will generally recommend voting against "members of the governance committee" of a board where the company holds a virtual-only AGM **and** does not provide robust disclosure in the Proxy Statement assuring shareholders that they will be given the same rights and opportunities to participate as they would at an in-person meeting. Glass Lewis therefore seems more open to virtual-only AGMs in the US, but it remains to be seen what, if anything, it might decide to say in its UK guidelines in the future.

Miscellaneous reporting requirements

This section briefly looks at miscellaneous reporting requirements which, whilst not for inclusion in the annual report, merit a mention.

Reporting on business payment practices and performance – now in force. We have covered this new requirement for large companies to report twice a year on payment practices and performance in various client briefings since 2016.

[The Reporting on Payment Practices and Performance Regulations 2017 \(SI 2017/395\)](#) and the [LLP equivalent regulations \(SI 2017/425\)](#) each came into force on 6 April 2017 and apply for each relevant company in a group (broadly all companies unless medium sized or smaller under the Companies Act 2006) with financial years beginning on or after that date. The regulations are supported by [Guidance to reporting on payment practices and performance](#) issued by the Department of Business, Energy and Industrial Strategy.

The first entities have now reported under the new regime. Their reports are accessible on the [Government website](#).

December year-end entities will have a first reporting period of 1 January 2018 to 30 June 2018 and will need to file their first report on or before 30 July 2018. For more on the regime, see our [March](#) and [December](#) 2017 Quoted Company Newsletters.

Gender pay reporting. The [regulations](#) on mandatory gender pay gap reporting came into effect on 6 April 2017 for each company in a group which employs 250 or more employees. Non-statutory [guidance](#) on the regulations is available to assist employers. The deadline for publishing the first set of data is 4 April 2018 and a number of employers have already begun to upload their gender pay gap data onto the Government [website](#) as well as Companies' own websites. The information must be confirmed as accurate by a director.

There has been some criticism that several companies have reported an identical mean and median figure, which is statistically unlikely and that some companies did not link to a supporting statement.

Please see our [briefing](#) on the top five issues for employers as well as an updated version of our more detailed [briefing](#) on the regulations.

FUTURE DEVELOPMENTS

Future developments
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New secondary legislation on reporting

In our September 2017 Quoted Company Newsletter, we covered the [Government response to its Green Paper on corporate governance reform](#).

Amongst other things, the response notes that the Government plans to introduce secondary legislation for more corporate reporting on a number of areas. See the table below for the areas to be covered.

Proposed secondary legislation
<ul style="list-style-type: none"> • Section 172 reporting. That all companies of a significant size (public and private) explain how their directors comply with the requirements of section 172 of the Companies Act 2006 to have regard to employee and other interests.
<ul style="list-style-type: none"> • Pay ratio reporting. That quoted companies report annually in their remuneration report on the ratio of CEO pay to the average pay of their UK workforce, explaining any year-on-year changes and how the ratio relates to pay and conditions across the wider workforce.
<ul style="list-style-type: none"> • Reporting on share-based incentives schemes. That quoted companies provide clearer explanations in their remuneration policies of the range of potential outcomes from complex share-based incentive schemes.
<ul style="list-style-type: none"> • Corporate governance for large private companies. That companies of a certain size disclose their corporate governance arrangements in their directors' reports and on their websites including whether they follow a formal code.

As regards timing, the response notes that the intention is to put the draft secondary legislation before Parliament before the end of March 2018, with the changes being brought into force by June 2018 and to apply for reporting years beginning on or after that date.

Proposed new Corporate Governance Code

In our December 2017 client briefing, we wrote about the [FRC consultation on the UK corporate governance code](#) (the Code). The consultation runs until 28 February 2018.

Key areas being consulted on are set out below.

Proposed Code – key areas of change
• Stakeholder, especially workforce, engagement
• Culture
• Succession planning and diversity
• Independence
• Remuneration
• Application to smaller listed companies

If the changes to the proposed Code go ahead in their current form it will likely lead to a number of changes to corporate governance reporting in annual reports. For example, disclosures on how a company applies the updated Principles of the Code, on how it has engaged with its workforce and other stakeholders, on actions it takes following significant votes against resolutions and on the work of its nomination committee.

As regards the various changes on independence including the need for the chairman to be independent and also the new application to smaller listed companies, these could require board changes in some smaller and larger companies.

The FRC's current intention is to publish a final version of the new Code by early Summer 2018, to apply to accounting periods beginning on or after 1 January 2019. For more on this, please see our [December 2017 client briefing](#).

Updated guidance on the strategic report.

We noted in our September and December 2017 Quoted Company Newsletters [the FRC consultation on its Guidance on the Strategic Report](#). The proposed amendments to the guidance reflect the increasing focus on the need for businesses to consider their impact on society and wider stakeholders and to report more on the sustainability of their business over the longer term. In particular, the amendments aim to update the guidance to:

- Reflect changes to the strategic report requirements made by the non-financial reporting regulations (mentioned earlier).
- Enhance the linkage between section 172 of the Companies Act 2006 and reporting in the strategic report.
- Make targeted improvements to reflect recent developments in corporate reporting.

Comments on the consultation were requested by 24 October 2017. Subsequently, in December 2017, the FRC issued a [press release](#) stating that it will wait to publish the final guidance until after the Government has published its proposed secondary legislation on reporting on section 172 of the Companies Act 2006 (mentioned above).

For more, see our [September](#) and [December](#) 2017 newsletters.

Miscellaneous European developments

[Directive 2017/828 amending the Shareholder Rights Directive \(2007/36/EC\) as regards encouragement of long-term shareholder engagement](#).

We have been writing about this as a proposed directive for many years. In May 2017, the Directive was published in the Official Journal of the EU. Member States have until 10 June 2019 to implement it.

A key relevant area of the Directive relates to shareholder voting on pay which is already covered in the Companies Act 2006. Another area, that of shareholder identification, is already catered for in the Act's provisions on information about interests in a company's shares. Other areas of the Directive do not impact on AGMs or narrative reporting in the annual report (eg provisions on related party transactions and provisions as to transparency by institutional investors, asset managers and proxy advisers).

Given Brexit, whether or not the UK will choose to implement any aspects of the Directive that are not already catered for remains to be seen.

The proposed Directive on gender balance among non-executive directors of listed companies.

Equally, we have noted this proposed directive for some years. It remains a proposal (centred around a goal of 40 per cent representation of the under-represented sex among non-executive directors of listed companies) albeit one that has stalled for quite some time due to the preference of several Member States for national measures.

The UK corporate governance environment

Some key 2017 publications

Below is a table of key 2017 publications and links to them, which may be useful to companies both for the 2018 AGM and reporting season and also more generally.

Title	Date
Financial Reporting Council (FRC) and Lab	
A sharper UK Corporate Governance Code to achieve long-term success and trust in business	December 2017
Frequently asked questions about non-financial reporting	December 2017
Strategic report guidance to follow government legislation	December 2017
Audit and Assurance Lab Project: audit committee reporting	December 2017
Lab Report: digital future of corporate reporting	December 2017
Lab Project Report: risk and viability reporting	November 2017
Annual review of corporate reporting 2016/2017	October 2017
Summary of key developments for 2017/2018 annual reports	October 2017
Lab Implementation Study: disclosure of dividends, policy and practice	October 2017
Consultation on draft amendments to guidance on the strategic report	August 2017
Non-financial reporting factsheet	July 2017
Development in corporate governance and stewardship 2016 (We understand no 2017 report will be published)	January 2017
The Department of Business, Energy and Industrial Strategy (BEIS)	
Government response to its Green Paper on corporate governance reform	August 2017
The Investment Association (IA)	
Position statement on virtual-only AGMs	December 2017
Public Register	December 2017
Principles of remuneration and accompanying letter	November 2017
The Pensions and Lifetime Savings Association (PLSA)	
Corporate Governance Policy and Voting Guidelines 2018	January 2018
Hidden talent: what do companies' annual reports tell us about their workforce	January 2018
Pre-Emption Group	
No change to pre-emption thresholds for Prospectus Regulation	July 2017
Monitoring report May 2017	May 2017
Institutional Shareholder Services	
UK and Ireland Proxy Voting Guidelines	January 2018
Glass Lewis	
2018 proxy season guidelines UK	January 2018
Diversity related	
Hampton/Alexander review – FTSE women leaders – supplementary report	November 2017
Parker review committee final report on the ethnic diversity of UK boards	October 2017

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