Spending Review Submission by the Chartered Governance Institute UK & Ireland

February 2025

Executive Summary

- Champion responsible governance as vital to effective organisations and as a driver of long-term sustainability.
- Champion the importance of qualified governance professionals
- Deliver new statutory powers for the Financial Reporting Council and complete the legal underpinning for its transition to ARGA.
- Broaden the range of responses to manage unacceptable behaviour by directors.
- Set a clear timetable for secondary legislation to deliver transformation of Companies House.
- Bring forward reform of all-employee share plans to increase participation.
- Reduce fraud risk for business by closing loopholes through smart regulation.

1. About The Chartered Governance Institute UK & Ireland

The Chartered Governance Institute UK and Ireland (the Institute) represents the views of 14,500 senior governance professionals working across all sectors of the UK economy, with particularly strong representation from FTSE companies. This submission is based on our members' direct experience of the challenges and implications of political and economic decisions.

The Institute is the professional body for governance and the qualifying and membership body for governance professionals across all sectors. Our purpose under the Royal Charter is to lead *'effective governance and efficient administration of commerce, industry and public affairs'* working with government, regulators and policy makers to champion high standards of governance and providing qualifications, training, and guidance.

We are the professional body that qualifies Chartered Secretaries and Chartered Governance Professionals, which includes company secretaries. As a lifelong learning partner, the Institute helps governance professionals to achieve their professional goals, providing recognition, community and the voice of its membership. We promote the contribution of good governance to economic and societal value as we believe better governance drives better decision making across all organisations.

ProShare - the voice of employee share ownership since 1992 and which was established by HM Government and a group of FTSE 100 to promote wider share ownership - is part of the Institute.

2. Responsible Governance

Government should champion responsible governance as vital to effective organisations and as a driver of long-term sustainability. The Institute believes that trained governance professionals, along with properly qualified directors with the required skill set, help to underpin this sustainability as responsible governance practices promote open, transparent decision-making. Additionally, it supports the efficient use of funding, particularly important when financial resources are limited.

The Institute believes that responsible governance and stewardship can help businesses to focus on competitiveness and attract greater investment, creating the optimum conditions for value creation over the long term. The UK economy is bolstered by clearly valuing the benefits of oversight and regulation which support sustainable value creation and UK values. It Is vital that the Government actively champions the benefits of governance for business to maintain and grow investment in UK companies and businesses through increased investor confidence.

We would like the Government to deliver a commission on governance that would demonstrate support for the UK's corporate governance tradition. Governance should enhance the competitiveness, agility and resilience of organisations, balancing the desire for the delivery of societal change and protecting reputation with the desire to be competitive. The commission could explore how this could be delivered, including the merits of the introduction of regulatory tests such as:

- That regulation is effective and efficient implementation costs should be assessed.
- That governance should help to promote/acknowledge our culture and values. (business is not separate from society) (Companies Act S172).
- That governance should be proportionate to support sustainable business growth from business inception to established listed companies.

3. Economic Crime

The Institute welcomes the commitments made in the Budget 2024 enabling HMRC to improve compliance and the investments that will help HMRC to modernise and improve its productivity.

We applaud the commitment to a transparent and accountable business environment and acting to reduce economic crime and look forward to working with the Government to ensure this is delivered.

Reducing tax avoidance and evasion is vital and the Institute would welcome greater transparency so that criminals can no longer hide their activities behind trusts, shell companies, or in our offshore tax havens. Government should focus on eliminating loopholes exploited by bad actors through smart regulation and enforcement.

The government should complete the necessary legislation to develop the Financial Reporting Council into the Audit, Reporting and Governance Authority (ARGA) and provide the new regulator with a range of responses to manage unacceptable behaviour by any of the directors of a company which matches the seriousness of the oversight or misconduct, similar to the current range of responses available for financial officers. This would apportion responsibility more evenly across financial actors on the board and encourage higher standards of corporate accountability.

Additionally, Government should:

- Monitor whether the powers and finance afforded to Companies House are sufficient to deliver accurate and reliable data on who owns and manages companies.
- Prioritise implementation of the Economic Crime Plan 2.
- Set out a clear timetable for the extensive secondary legislation and complex system changes that need to take place within Companies House.
- Allow all those registered for Identity & Verification (ID&V) at Companies House under the ECCT Act to be treated as identified for all AML purposes.

4. Audit Reform

The Corporate Governance and Audit Reform bill presents an exciting opportunity to deliver where previous administrations have dithered and delayed. There is a potential for enhanced enforcement mechanisms to be established as the FRC transforms into the Audit, Reporting, and Governance Authority (ARGA).

Given the importance of shareholder stewardship in the UK corporate governance structure, there should be more rigorous oversight from the regulator in situations where shareholders are not engaging as expected. The changing dynamic of the investor model means that although some shareholders and investment managers continue to see themselves as owners of a company with associated stewardship responsibilities, others see themselves primarily as investors, interested only in income and asset growth. Where shareholders who are signatories to the Stewardship Code decline to engage, or do not do so effectively, we believe that companies should be expected to report this to ARGA.

The FRC's Annual Audit Quality Inspection Results for Tier 2 & 3 firms 2023/24 showed only 21% of audits were good or required limited improvements. This perception creates a lack of confidence in the ability of smaller auditors to deliver high quality audits of large and / or complex organisations and must be tested by an independent body. This would be a more effective solution to the capacity and resilience problem than the proposed remedies, which might well reduce audit quality.

UK Audits have a poor record of alerting investors about corporate failure. A recent analysis of the audit reports of the largest 250 publicly traded companies that collapsed between 2010 and 2022 revealed that auditors failed to identify a problem (known as “material uncertainty related to going concern”) with 75% of major corporate failures. (reward-for-failure.pdf)

It would be reasonable to conclude that investor scepticism about the veracity of financial reports is one of the causes behind the decline of the UK equity markets. High-profile corporate collapses - including Carillion, Thomas Cook and BHS – have highlighted significant deficiencies in audit practice and standards where the issue is, more often than not, one of judgement, and these deficiencies remain.

We would like Government to bring forward a statutory regime which includes the following changes to company law:

- An expansion of the scope of regulation to include all large private companies (using the formula 750:750).
- S271 of Companies Act 2006 (employment of a professionally qualified company secretary) should be extended to apply to all large private companies.
- Restricting use of the term ‘company secretary’ to those with a recognised professional qualification
- Reiterate Government support for the UK’s corporate governance tradition as a guarantee of the rights of retail shareholders and minority investors, and the protection of stakeholder interests.

New powers for the FRC / ARGA

- The power to direct changes to the entire contents of the annual report and accounts, rather than having to seek a court order.
- The power to investigate and sanction directors (including directors of large private companies) for breaches of their corporate reporting and audit-related duties and responsibilities.
- Establish new, enforceable principles of corporate auditing as these are vital to improve audit quality.

5. Reform of All-Employee Share Ownership schemes

For more than 40 years employees have been able to make savings and investments through workplace salaries, via these all-employee share plans. But as the nature of work changes, some features of these plans are becoming outdated and are putting off prospective participants.

There are two all-employee plans - the Share Incentive Plan (SIP) and the Save As You Earn (SAYE). Both schemes are seeing participation rates decline:

- The number of firms offering an SAYE has been on a downward trajectory – halving over the last two decades (1110 firms in 2001, down to 550 firms in 2023).
- The number of companies offering staff a SIP fell from 860 in 2022 to 830 in 2023.
- Based on ProShare’s annual survey an estimated 550,000 employees currently invest in a SAYE (down from 711,000 in 2018)

- The overall tax relief (NIC and IT) applicable to both SIP and SAYE has been falling – an indication that fewer employees are investing (£550m in 2023 vs £840m in 2014).

A number of simple reforms would make these plans easier to manage, more attractive to workers (especially younger people) and crucially open them up to more participants. We encourage the government to consider the following proposals:

1. Reduce the SIP holding period from 5 to 2 years for all SIPs

- This would make them far simpler to understand, communicate, and administer, and would increase employee participation without impacting productivity.
- More than 40 companies have written to the Treasury, calling on them to introduce this reform including Admiral, Aviva, easyJet, National Grid, Pearson, Vodafone and Wickes.

2. Optional 'free' company contribution

- As an optional feature, companies could 'auto-enrol' employees into the SAYE by making a free monthly 'Company Contribution' towards employees' savings.
- For example, firms could make a net payment to each employee's SAYE of, say, £10 after tax and NIC deductions, giving every employee an opportunity to participate and benefit from any rise in the share price, encouraging staff to save, and build financial resilience.

3. 'Whole-workforce' approach - allowing gig economy / zero hours workers to participate

- Circa 5m people are in informal contracts, working on zero-hours or in the 'gig economy'.
- Firms would like the flexibility to include them in share plans, but current rules prevent this.
- The financial, productivity and wellbeing benefits of offering employee share plans more broadly within companies' workforces would be considerable, for the employer, for the workforce, and for the UK economy as a whole.

CONTACT

For further information please contact David Mortimer, Head of External Affairs on *dmortimer@cgi.org.uk*