

Capital Markets Policy Team
Financial Conduct Authority
12 Endeavour Square
London E20 1JN

By email: cp21-24@fca.org.uk

20 October 2021

Dear Policy Team

**Diversity and inclusion on company boards and executive committees
Consultation Paper CP21/24 - response to consultation**

We welcome the opportunity to respond to the Financial Conduct Authority (FCA)'s consultation on diversity and inclusion on company boards and executive committees.

The Chartered Governance Institute is the professional body for governance and the qualifying and membership body for governance professionals across all sectors. Its purpose under Royal Charter is to lead 'effective governance and efficient administration of commerce, industry and public affairs' working with regulators and policy makers to champion high standards of governance and providing qualifications, training and guidance. As a lifelong learning partner, the Institute helps governance professionals to achieve their professional goals, providing recognition, community and the voice of its membership.

One of nine divisions of the global Chartered Governance Institute, which was established 130 years ago, The Chartered Governance Institute UK & Ireland represents members working and studying in the UK and Ireland and in many other countries and regions including the Caribbean, parts of Africa and the Middle East.

As the professional body that qualifies Chartered Secretaries and Chartered Governance Professionals, which includes company secretaries, our members have a uniquely privileged role in companies' governance arrangements including the work of boards and nomination committees in the oversight of equity, diversity and inclusion on company boards, executive committees and throughout the company. Our members are therefore well placed to understand the issues raised by this consultation document.

The Institute has engaged with the Davies, Hampton-Alexander and Parker reviews at the time and has actively supported the work of these, in particular the Hampton Alexander Review, ever since, assisting BEIS with gathering data from companies.



In preparing our response we have consulted, amongst others, with members of our Company Secretaries Forum, a group of company secretaries from more than 30 large UK listed companies from the FTSE 100 and FTSE 250. However, the views expressed in this response are not necessarily those of any individual members of this group, nor of the companies they represent.

Our responses to the questions raised in the consultation are set out below. Where appropriate we have explained the reasons behind our responses and we have set out our views on the relative merits of the potential options set out in the consultation as we see them.

General comments

We believe that diversity, broadly defined, including experience and viewpoint, makes for better boards and leadership teams.

We recognise the FCA's conclusion that, as noted in the consultation document, "overall, the empirical evidence for the impact of diverse workforces and boards on financial performance is inconclusive", although there does seem to be some evidence of correlation between board gender diversity and improved risk management and corporate governance outcomes. The consultation document also refers to the FCA's finding that "increased gender diversity in the boardroom positively influences board monitoring functions, such as attendance, quality of discussions, and monitoring effectiveness including better oversight of a firm's disclosures and reports" and cites "studies that link board gender diversity with lower performance volatility and fewer cases of fraud and misconduct."

But beyond academic evidence, it seems to us quite simply that achieving a position in which the best possible candidates for board and leadership roles will be drawn from all available and qualified talent is not just common sense but is also the right thing to do.

Consequently, nomination committees and boards need to improve their approach to diversity. Although the pace of women being appointed to FTSE 350 boards has increased – up to 40% of new appointments according to Institute research in 2020, there is still a significant difference between the female share of executive directorships (14.2% in the FTSE 100 and 11% in the FTSE 250) compared with non-executive directorships (42.2% in the FTSE 100 and 39.1% in the FTSE 250). This is the real issue; the need to develop and strengthen the pipeline of women and other under-represented groups ready to move into executive directorships. It is our contention that some of solutions that have been proposed, such as increasing the number of seats on boards for under-represented groups do not go far enough to tackle this core issue, although it is worth emphasising that many corporate boards will be in the range 8-12 individuals and so a one person change – in either direction – can have a disproportionate impact on the percentage of any minority on the board.

However, diversity of experience and viewpoint is not just about gender. It's also about ethnicity, sexual orientation, educational background, age and stage of career as well as any number of other factors. Even then, true diversity depends on the personal characteristics of the individual concerned. Managing board diversity is a critical part of the role of the Chair, with the support of the nomination committee and the Company Secretary.



Key issues for company secretaries and their boards to consider are:

- How representative is the board of the business it leads, of its markets and customer base, and of the society or societies in which it operates?
- Is the challenge that boards simply want people in their own likeness or are recruitment firms just proposing candidates who fit this bill? What are the views of investors? Are they supportive of diversity?

We believe that one part of the solution is a recognition that company secretaries provide a suitably skilled and experienced board-ready pipeline. They have a very privileged and advantageous position from which to observe boards in action and, in many cases, more boardroom experience than many of the directors with whom they work.

As a professional body, we are certainly seeing much greater diversity in the profession than ten or twenty years ago. At the time of writing, 42 FTSE 100 companies have a female company secretary, and we are seeing increasing numbers of women and people from ethnic minorities joining the profession.

Feedback from our members includes:

- Diversity of board membership is a means to an end not an end in itself. One of our members gave us an example of a board, lauded at the time for its high standards of governance, that was diverse enough to score very well against the metrics for gender and ethnicity but which suffered from 'group-think' because "nearly all the horses were from the same stable".
- Potentially discriminating against directors and executives from over represented groups may ensure the delivery of the targets being sought but in the long term is damaging to creating inclusive organisations
- Diversity should be considered from a succession planning perspective. We need people in earlier stages of their careers and those with diverse characteristics in the executive pipeline as they will provide a broader perspective. Until now, the focus has been exclusively on women and on NEDs when actually a larger problem is the limited diversity of the executive pipeline.
- HR development could be improved in some companies. There may be lessons to be learned from the military selection processes where people are given considerable responsibility at an earlier stage of their career. With the development of age-discrimination legislation and the need for people to work for longer to get to a pension, we should consider whether we are reducing the opportunity for people to become directors at an earlier stage of their careers?
- Whilst boards are being urged to encourage more diversity, there is a problem around what constitutes an individual being board ready. How do you encourage a board to accept readily people who are not what they might traditionally consider as board-ready? For example, experience on a FTSE board should not be seen as mandatory as this acts only to reduce the potential talent pool, but too many organisations – including Government – include board experience as an essential criterion.
- For all these reasons, the induction and training of new directors will need particular attention if new directors are not to be set up to fail.

With these thoughts in mind, we support the aims that the FCA has set out in this consultation document. However, we have some doubts as to the efficacy of certain of the solutions proposed.



Fundamental to these doubts is a recognition that this reflects a much larger social issue than can be addressed simply by companies reporting data. Companies have a part to play – an important part – and a responsibility to help drive social change, but cannot do this on their own. Much of the responsibility for action to increase the number of women and people from diverse backgrounds in executive positions on boards and, indeed, generally to increase diversity of all kinds at every level within organisations, does not rest with companies alone.

The Institute has consistently suggested a range of steps that should be taken at Government level to increase diversity in the executive pipeline which we believe are relevant to this consultation:

- Encouragement for women and those from diverse backgrounds to consider the broadest range of careers, starting in schools. Such activity should be co-ordinated with the business community, which can help and is, indeed, keen to do so as maximising the use of the available talent pool in the UK makes great business sense.
- More initiatives to support parental leave, including shared parental leave, and childcare, which we consider to be at the heart of addressing the imbalance between men and women at senior levels in business. Supporting women to return to work and progress in their career after having children is a much wider social issue than can be addressed simply by companies reporting more data.
- Better support for carers, in order that, in particular, older working women and those from certain cultures are able to fulfil their career potential. For a variety of societal reasons, care for the elderly tends to fall more heavily on women than on men.

Initiatives to showcase diverse business leaders, for example BAME or LGBTQ where there is a dearth of role models, can also be helpful.

The ONS statistics for gender and ethnicity split in the UK are widely available. But for a variety of historic reasons, it seems widely accepted that the same percentages of individuals are not, currently, suitable to be senior executives and board members at public companies. Targets such as those proposed in the consultation are a good means of fostering improvement, but there remains a tension between seeking apparent diversity representation over skill and where the balance should lie. Companies are caught between wanting to maximise the use of the available qualified talent pool in the UK and, at the same time, wanting to maximise the quality of the board. These two aims should not be mutually exclusive but, in our current socio-economic environment, they can be and whilst we understand that the FCA's proposals are currently on a 'comply or explain' basis, we are concerned that this may not always be the case. In the FCA's discussion paper on diversity and inclusion in the financial sector – working together to drive change (DP21/12), it is clear that the FCA wishes to see significant and rapid change on diversity and inclusion and that the progress made so far falls short of its expectations. The statement in paragraph 1.4 of that document that "Ultimately, where firms fail to meet our minimum expectations, we will be prepared to use our regulatory powers, and take action where appropriate" suggests that a degree of compulsion is planned which we do not believe to be appropriate.

This concern is exacerbated by our members' experience of the influence of proxy advisers such that even a very clear explanation of non-application of a recommended target can still lead to negative feedback and/or voting.



Many companies would also take the view that simply because some investors – often a vocal minority – would like a piece of information reported is not reason enough in itself for a regulator to mandate, or even recommend, the public reporting of that information. They would question whether these proposals are relevant to the FCA’s objectives of market integrity or consumer protection. They might also hold the view that the FCA is in danger of under-estimating the risk that the continued growth of regulatory requirements has on the competitiveness and attractiveness of the UK market.

Finally, we are concerned about the potential for confusion in the market between the respective roles of the FCA and the Financial Reporting Council (FRC), especially as the latter transitions to its new guise as the Audit, Reporting and Governance Authority (ARGA). This ‘demarcation’ issue should be a key point to be agreed between the FCA and ARGA.

Our members see a clear distinction between the making of rules – for example the Listing Rules – with which all listed companies must comply and the establishment of ‘comply or explain’ principles which fit better in the UK Corporate Governance Code. In our view, having more than one regulator responsible for setting reporting requirements risks those requirements becoming confusing and, more importantly, less effective than they might be if subject to a single, integrated approach. We therefore suggest that the FCA limit the Listing Rule requirement to one that companies must report on those issues covered by the UK Corporate Governance Code, with the FRC or ARGA setting those criteria and assessing the quality of explanations.

Answers to specific questions

Q1: Do you agree with the proposed comply or explain disclosure requirement on board diversity targets relating to gender and ethnicity?

On balance yes, although for the reasons outlined above, we strongly recommend that, were this requirement to be introduced, it should be made absolutely clear that a good explanation for not meeting the targets constitutes compliance. For this reason, we believe the reporting requirement would be better suited to being introduced by the FRC through the UK Corporate Governance Code than by the FCA through the Listing Rules.

Q2: Do you agree with the proposed disclosure obligation to set out numerical data on the gender and ethnic diversity on a company’s board and its most senior level of executive management?

As per our response to question 1 above, we agree with this proposal but with significant caveats. The proposed template approach will help to ensure consistency of reporting, but that may not be appropriate for all companies.

Q3: Do you agree with the proposed scope of who would be required to report under the new Listing Rules proposals, and those we have excluded (e.g. issuers of listed debt)? If you disagree, please explain why.

We see no reason why such organisations should be excluded from the reporting requirement albeit that their data may reflect their different circumstances. However, we have no fundamental objection to the exclusions.



Q4: Do you agree with our proposal to include overseas and smaller issuers in the new Listing Rules proposals? If not, please explain whether you would propose further flexibility within the rules, or would exclude such companies from scope?

Yes. Again, we see no reason why such organisations should be excluded from the reporting requirement, albeit that their data may reflect their different circumstances and it is appropriate that foreign companies listed on the London market should be held to the same disclosure and governance standards as UK registered companies if the integrity of the London market is to be maintained.

Q5: Do you agree with proposed targets on gender and ethnic diversity representation at board-level of companies? Should we consider any additional or different targets?

Generally, yes, although as noted above, we believe these are more suited to the UK Corporate Governance Code than to the Listing Rules and the targets themselves should be regularly reviewed against the wider socio-economic factors at play and available qualified talent in the United Kingdom.

We do, however, have concerns about the proposal that “At least one of the senior board positions (Chair, CEO, SID or CFO) is held by a woman (including individuals self-identifying as a woman).” The current low level of female executive directors (14.2% in the FTSE 100 and 11% in the FTSE 250) suggests that this will be a particularly high bar for companies to achieve and one that may not yet be justified by the quality of candidates. If this proposal is to be carried forward, we would suggest that the positions concerned be broadened to include the chairs of the main board committees.

Q6: Do you agree with the format and extent of numerical data reporting proposed in the tables in Annex 2? If not, please explain any changes you would suggest or where further clarity is needed.

Generally, yes. The format and extent of numerical data reporting proposed in the tables in Annex 2 seems proportionate, although clear definition of terms like ‘executive management’ would be helpful to ensure consistency and comparability of reporting. We are pleased to see the inclusion of “Not specified/prefer not to say” as we have some anecdotal evidence from our members that some directors, particularly those of mixed ethnicity, would be very sensitive to such reporting.

One query raised by some companies with an international perspective is the terminology used in the tables. Whilst we understand the logic of deriving these from the ONS categories, these are rather Anglo-centric for use by companies with an international workforce and it may be appropriate to allow some flexibility in terms of the categories used. For example, there was a concern about the use of the term ‘British’ in the tables and a feeling that ‘Other Ethnic Group’ suggests some level of hierarchy – for example that Arabic or middle eastern might be perceived as less important than the specified categories.

Technically, inserting an additional line to report an additional category might be seen as non-compliance but, for example, for companies with a significant American workforce, a category of ‘Hispanic’ might also be appropriate.



Q7: Should we consider requiring similar numerical data reporting for the level below the executive management team of in-scope listed companies and / or seek data on representation by sexual orientation? If so, we welcome any drafting suggestions and views on any impact this may have for the CBA and scope of our proposals.

In principle, yes although again we do not believe that the FCA is the appropriate regulator to require such reporting.

Creating a pipeline of diverse talent should be a priority for companies and regulators alike and we see many benefits to the collection of data on ethnicity and sexual orientation by companies – not least in ensuring that diversity policies are truly effective in practice. We therefore believe that the extension of reporting level below the executive management team of in-scope listed companies may – indeed should - be an aspiration over time.

However, feedback from our members is that many companies do not routinely keep ethnicity or sexual orientation data and consequently its collection may be quite onerous, particularly for companies operating in multiple jurisdictions where it is not always legally permissible to gather such data or, indeed, legal or even safe for employees to give it. There are, we understand, more than 70 countries in the world where homosexuality is illegal. Whilst some companies were justifiably proud of the way in which their policies on diversity and inclusion had been received by staff, for example, one of our members reporting their most active LGBT network being in Poland, where they have been told that “work is the only place where I can be myself”, others have felt it necessary on legal advice to be circumspect in some jurisdictions. Another member reported that although their company was delighted to be a supporter of Pride, they had not shared any communications about that support in those countries in which they operate where homosexuality remains illegal.

Furthermore, some of our members are concerned that the collection of this data might be widely seen as intrusive and unlikely to produce accurate data. Whilst the ONS collects such statistics, there is a considerable difference between an anonymous report to the UK Government, for example in the decennial census, and a report to one’s employer, especially in certain global jurisdictions. Even the census statistics are widely held to under-report data on sexual orientation and, for many individuals, this is a strictly private matter. Reporting on sexual orientation may not, therefore, be an appropriate extension in the short term although voluntary reporting, where practicable, should be encouraged.

Again, the principle of ‘comply or explain’ and the principle that low levels of reporting should not be seen as a cause for criticism are both important here.

Q8: Do you agree with proposed amendment to DTR 7.2.8AR to add to the examples of diversity aspects included in DTR 7.2.8AR which issuers could disclose in their reporting on their diversity policy, and to extend consideration to key board committees? If not, please explain why.

On balance, no. Although we see little harm in the proposed change itself, neither do we see any benefit – companies already know that they are not precluded from including such diversity aspects in their reporting and the small size of most boards makes extension to key board committees seem unnecessary. Our concern about the change is the risk that it will be seized on by some single-issue pressure groups to force companies to disclose this data, whether appropriate or not, thereby creating unnecessary and onerous work, either to disclose the data or to explain their reasons for not doing so.



Q9: Do you agree with our proposed new guidance provision DTR7.2.8CG encouraging in-scope issuers to consider providing numerical data to further inform reporting on the results of their diversity policies? If not, please explain why.

No, for the same reasons as given in our response to question 8 above.

Q10: Do you agree with the proposed implementation timing? If not, please explain why and indicate what alternative timeframe you consider appropriate

No. By the time that this consultation has concluded, and the FCA is in a position to make changes to the listing rules, we will be very close to the proposed commencement date – indeed the ‘next steps’ section of the consultation refers to the FCA’s “aim to make final rules and publish a Policy Statement before the end of 2021.” The proposed implementation timing is, therefore, too soon.

In our periodic Boardroom Bellwether surveys, we have asked FTSE 350 companies for their views on a number of topical governance issues. One that we have asked about in our most recent surveys is around the complexity of reporting on the ethnic pay gap and more than half of respondents to our latest survey indicated that they believe this will be difficult or very difficult. This is a slightly different issue from the reporting proposed here but anecdotal feedback was that one of the main reasons for this anticipated difficulty is the lack of data that many companies hold about their employee ethnicity – indeed for some international companies, we are told that it is actually illegal for them to collect and hold such data. This issue will also apply to reporting. While we appreciate that any reporting is on a ‘comply or explain’ basis, it does still seem a very short window for companies to source such data, especially as board and senior executive succession planning is a process that usually extends over a period of years rather than months.

Consequently, we believe that any new Listing Rule requirement should apply no earlier than to accounting periods starting on or after 1 January 2023, so that reporting will start to appear in annual financial reports published for that year in spring 2024. Of course, companies that are able to disclose this data, on a voluntary basis, before then will undoubtedly do so.

Q11: Do you agree with our phased approach to improve our use of data over time? Should we consider other approaches? If so, please suggest these.

We have no strong views in response to this question. We are concerned, however, by the implication that the FCA may seek to consider further action in this area which, as we indicated above, we believe should rest within the purview of the FRC or ARGAs.

If you would like to discuss any of the above comments in further detail, please contact me.

Yours faithfully

Peter Swabey

Policy & Research Director

The Chartered Governance Institute UK & Ireland

020 7612 7014

pswabey@cgi.org.uk

