

ICSA: The Governance Institute
Saffron House
6–10 Kirby Street
London
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12th June 2019

Dear Sirs,

Response to the consultation on the effectiveness of independent board evaluation

Thank you for your email inviting us to respond to your consultation document: “Review of the effectiveness of independent board evaluation in the UK listed sector”.

EquityCommunications Ltd, is an independent company which has been helping listed companies and other organisations to undertake efficient, personal and worthwhile externally facilitated Board evaluations since 2002. Our extensive experience is sector and market wide. We have worked with UK listed companies from the FTSE30 to AIM quoted, Pension Boards, Building Society, European and Far East listed companies and UK not-for-profit organisations.

QUESTIONS:

THE PURPOSE OF BOARD EVALUATION

1. Do you agree that the purpose of independent board evaluation is to help boards continue to improve their performance and to demonstrate to shareholders and others that they are committed to doing so? If not, what do you consider the purpose should be?

Yes.

However, beyond this stated purpose, we believe our role is to give client board members some external indication of their corporate Board performance vis-à-vis other companies. Relatively few fulltime executives have a NED role with other companies. Portfolio NEDs rarely sit on more than 3 Boards at any one time. An independent evaluator will ‘see’ considerably more boards over the course of a year and as such we are ideally placed as part of an evaluation to put an individual client board performance review into a very much wider context.

OVERVIEW OF SUGGESTED ACTIONS

2. Will the changes made to the UK Corporate Governance Code in 2018 be sufficient on their own to improve the standard of board evaluation and reporting by listed companies, or would additional actions be helpful?

It is still too early to judge whether the changes made to the Code in 2018 have yet had the desired results.

3. If further action is desirable, do you support the proposed package of a code for board reviewers and principles and disclosure guidance for listed companies? If so, should they be mandatory or voluntary? Are there any parts of the package you consider to be unnecessary or inappropriate?

We support the proposed package of a Code for Board reviewers which should be mandatory.

However we disagree that listed companies should be subjected to further mandatory requirements in this area. The exception might be that reporting disclosure guidance at Appendix E should be extended and companies required to comply with reporting against these guidelines. See also reply to Q18.

4. Are there other actions that should be taken to improve independent board evaluation in the listed sector as well as or instead of these suggested measures? If so, please specify.

The main issue for an independent evaluator is that we lack any real form of sanction. We have no practical solution to offer to overcome this flaw in our service offering – other than to observe that if the proposals advanced in Qs18 – 20 below are implemented this will go some way to balancing the current lack of sanctions.

5. Should shareholders have more direct influence on the appointment of the independent board evaluator? If so, what form should this take?

It is difficult to see how this might be achieved in practice; indeed the Department for Business, Energy and Industrial Strategy has given no indication as to its thinking behind this point. Perhaps there might be a role for institutional shareholders to question the appointment of the same evaluator on more than 3 consecutive projects? Beyond this, the practicalities of involving shareholders (even if they wanted to be involved) would probably outweigh any advantages of companies following and reporting on a 'best practice' approach outlined in this consultation document.

6. Should the code and principles be applied to other sectors as well?

There is no reason for them not to be; as independent evaluators we always endeavour to bring the highest possible standards to all projects whether in the UK listed company environment, private companies, overseas organisations or the UK not for profit sector.

ACTIONS FOR SERVICE PROVIDERS

7. Do you agree with the proposed definition of 'independent board evaluation'?

Yes.

8. Do you agree that a disclosure approach to understanding a signatory's competence and capacity is appropriate? Should the code identify specific processes that must form part of evaluations carried out by signatories?

Yes; however proposals to identify specific processes which must form part of an evaluation are inappropriate and are in direct contradiction of the FRC's Guidance on Board Effectiveness (2018) which states: "... evaluation should be bespoke in its formulation and delivery ..."

Specifying what should form part of an evaluation is far too granular and prescriptive an approach to preparing what should be a flexible and responsive procedure individually tailored to the exact needs of a client.

9. Should the code should set out minimum standards in relation to the independence and integrity of the reviewer? If so, are the suggested standards the right ones?

Yes.

10. Do the code of practice and the principles for listed companies deal adequately with potential conflicts of interest?

Yes.

11. Are there any other issues that should be addressed in the code?

Should a potential user of their services request to do so, Signatories to the Code should facilitate appropriate contact with recent clients. By enabling the potential user to make their own selection from a list, a Signatory should assist them to seek an independent reference into their levels of service and satisfaction.

12. Is there a need for oversight and/or accreditation, or should service providers be able to self-certify that they are meeting the standards set out in the code of practice?

A process of self-certification is akin to an internal evaluation; one is essentially marking one's own homework. If external evaluators argue that independent review is a superior approach to establishing best practice standards, how can we argue against an external oversight or accreditation for our own Code of Practice? There should be some sort of Oversight Body.

13. If there is a need for a formal oversight body, which of these functions should be included in its remit – accreditation, monitoring of compliance, dealing with complaints, reviewing and revising the code?

The Oversight Body should be charged with accreditation, monitoring of compliance together with reviewing and revising the Code.

Dealing with complaints can be time consuming and costly and will only serve to increase the overhead of running an Oversight Body. Complaints should be a commercial matter between a service provider and the client company involved. However, the Oversight Body should be able to withdraw accreditation from a service provider on prima-face evidence of 'bringing the Code into disrepute'.

14. Do you have any suggestions for how oversight arrangements might operate in practice (including who might undertake them and how they might be funded)?

It is unclear from this Consultation document whether it is intended that a Signatory to the Code should represent a *corporate* or an *individual* registration.

From an individual perspective, the 'areas of capability' listed on page 36 of the Consultation document are drawn so widely so as to exclude no-one; this shortcoming alone substantially devalues the entire scheme. We urge the Steering Group to revisit their thinking in this area and considerably restrict the extremely wide definitions suggested here.

Both individuals and corporate entities should be required to apply to be considered for inclusion as a Signatory to the Code.

Corporate applications should be accompanied by a comprehensive list of clients for whom the applicant company has worked in the last (say) 4 years. The Oversight Body should seek the views of a random selection these end-users as to the applicants' suitability to be invited to become a Signatory to the Code. This might most easily be achieved by devising a modest confidential questionnaire for a Company Secretary to complete and return to the Oversight Body. The questionnaire should invite commentary on service levels; ability to interact with board members; quality of report; validity of recommendations etc.

A simple scoring system should be devised against which the end-user could give (an admittedly subjective) score against each question. A minimum score threshold (80%?) should be set which if achieved would allow the Oversight Body to extend an invitation to become a Signatory to the Code. The attractiveness of this proposal is that if as an applicant, your own clients cannot give an excellent

anonymous score of their experience of an applicant's abilities and service levels, should the Oversight Body really allow access to becoming a Signatory to the Code?

Individual applicants should be required to support their request by providing appropriate evidence for their inclusion as a Signatory to the Code - and this might include personal testimonials from corporate clients.

The running of an oversight body will inevitably incur costs. Fees should be set at a level to offset reasonable costs - perhaps reflecting the level of professional registration costs elsewhere.

ACTIONS FOR LISTED COMPANIES

15. Is there a need for some good practice principles aimed at listed companies conducting externally facilitated board valuations? If there is a need for such principles, do you agree that adoption by companies should be voluntary?

It is probably true to say that the adoption of independent external board evaluations by FTSE350 companies was largely driven by the compulsion element of the 'comply or explain' regimen of the UK Corporate Governance Code. However, most companies in this cohort would now continue the practice without the obligation; the 'principles' as drafted in Appendix D are essentially 'preaching to the converted' and 'teaching your grandmother'.

What are being proposed as 'principles' could perhaps be better drafted as 'Advisory Guidelines'. They should be considerably expanded and targeted at explaining to companies and other organisations who are not subject to any compulsion to undertake Board evaluations the potential benefits of doing so on a regular and independent basis.

16. Do the draft principles cover all the relevant aspects of the relationship between the company and external reviewer? Are they reasonable and appropriate? Do they go far enough?

See reply to Q15.

17. Should the principles include a requirement that companies should only engage board reviewers that have signed up to the code of practice for reviewers?

Not as a "principle". Instead, this should be a disclosure requirement only and should be added to a revised Appendix E 'Disclosure Guidance' content. See reply to Q18 below.

18. Is there a need for guidance on how companies should report on board evaluations in order to comply with the provisions of the UK Corporate Governance Code?

The variation in the quality of reporting by companies on the outcome of their Board evaluations would suggest guidance would be extremely helpful.

The disclosure guidance as drafted in Appendix E should be extended to cover how the reporting company approached selection, identified the scope and handled the disclosure, i.e. all the points in Appendix D of the "principles of good practice for listed companies", and companies required to comply with reporting against these guidelines.

This would obviate the need to have companies specifically 'adopt' a set of principles. See also disclosure suggestion in Q20.

It must be recognised that if the draft guidance is followed in full it would considerably extend this section of the annual report.

19. Does the draft guidance cover all the relevant issues of interest to investors and other users of annual reports? Are the expectations it places on companies appropriate?

If amended as suggested in Q18 above. Yes.

20. Should the independent reviewer be expected to certify that the disclosures made by the company are accurate? If so, what form should this take?

Yes.

A simple declaration following the Board evaluation review report in the company Annual Report which states: "This report on the externally facilitated board evaluation process has been approved by <<name of evaluating company>> who were also invited to present their findings to a meeting of the full Board".

It should be made clear to companies that falsely including this statement would allow the independent board evaluator to report this breach to the FRC for appropriate action.

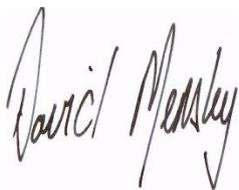
Finally, paragraph 29 on page 11 makes it clear that as part of the process of preparing this consultation document the Steering Group held discussions with Board reviewers.

EquityCommunications Ltd wrote to the ICSA at the end of August 2018 when the ICSA announced it would be accepting the BEIS invitation to convene a group. We offered to contribute to this exercise, drawing attention to our long involvement in providing independent Board evaluation services to Listed and other companies.

We would like to record our disappointment that despite our proactive offer of involvement, the ICSA failed to respond to our approach.

We look forward to confirmation of receipt of this response to your consultation process.

Yours faithfully,



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