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**Response to *Corporate Governance Code Consultation***

[Submitted via email to: [codereview@frc.org.uk](mailto:codereview@frc.org.uk)]

Dear Mr Styles,

Chartered Accountants Ireland ('the Institute') welcomes the opportunity to respond to the Financial Reporting Council (FRC) *UK Corporate Governance Code* (the 'Code') Consultation. The Institute has over 31,000 members, with many performing a range of governance roles including as directors and leading the provision of compliance, risk and corporate reporting for companies applying the Code. The Institute is both a Recognised Supervisory Body ('RSB') and a Recognised Qualifying Body ('RQB') under UK company law. As an RSB, the Institute performs certain audit regulatory functions in respect of those of its member firms that are statutory auditors, including those that audit companies applying the Code. The Institute licenses approximately 700 audit firms that are eligible to conduct statutory audits in the UK and Ireland.

Our response to the questions set out in the consultation document is attached as an appendix to this letter. However, we would also like to highlight two additional general comments:

1. By limiting the proposed revisions to the Code to "the legislative and governance reforms the Government proposes" in the White Paper '*Restoring trust in audit and corporate governance*', we believe there is a missed opportunity for a broader focus on improving the principles-based approach to corporate governance that the Code has championed for over thirty years.

In addition to reinforcing compliance with statutory obligations, there is an opportunity to reflect on the principles and values that were lacking in respect of the corporate failures that led to the reforms, and to address these in the Code. We provide the following examples for consideration:

- Principle B refers to acting with integrity, promoting the desired culture and ensuring workforce policies and practices that are consistent with the company's values. We believe that the Code

could go further by calling for companies to clearly communicate and enforce their values and promote ethical conduct, for example with a code of ethics.

- Principle G (Section 2) could be enhanced so that non-executive directors, including the chair, are aware of information asymmetry and ensure they have sufficient understanding of the company, its operations and culture to effectively challenge and support management.
- Principle N (Section 4) could be improved by ensuring that the board of directors (the 'board') establish and maintain an effective values system in the company that supports a healthy culture and promotes ethical conduct.

2. It is apparent from reviewing Section 4 of the Code and the legislative requirements for audit committees that the role and responsibilities of the audit committee are increasing. Audit committees play a crucial role in promoting strong corporate governance, through their involvement in risk oversight, internal controls, corporate reporting (financial and ESG), and audit. Introducing narrative reporting will further increase these responsibilities and we believe the scope of this should be limited to corporate reporting in the annual report. Likewise, the Code should maintain emphasis on financial controls and extend only to controls related to corporate reporting in the annual report. Also, the board is ultimately responsible for reporting and the Code should not mandate narrative reporting, by default, part of the role of the audit committee.

As other assurance requirements for companies emerge, for example supply-chain due diligence, we can expect the competency and skills of the audit committee to be further called upon by the board. To avoid overburdening the audit committee, or any one board committee, we believe it is important that the board is not restricted by legislation or the Code in relation to its ability to delegate roles and responsibilities as it sees fit in accordance with its fiduciary duties.

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Yours sincerely

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Chartered Accountants Ireland

## Appendix – Chartered Accountants Ireland’s response to Consultation questions

### Section 1: Board Leadership and Company Purpose

#### Q1 - Do you agree that the changes to Principle D in Section 1 of the Code will deliver more outcomes-based reporting?

- a) We welcome efforts to discourage boilerplate wording and to encourage clear and concise disclosure that provides sufficient explanation on the reasons for any departure from the Code’s provisions, including providing sufficient insight on how the board has otherwise adhered to the overall principles of the Code.
- b) Reporting on the Code has successfully operated on a ‘comply or explain’ basis to date, and any detailed reporting under the Code has been to disclose it complies with the Code except for any departure from the Code’s provisions, which must be explained, or a specific disclosure required by one of the Code’s provisions. It is not clear what other ‘governance activity’ the board will be reporting on under the Code. While other obligations to disclose certain governance practices exist, e.g., from company law or sustainability reporting standards, these are often prescriptive and include requirements of their own. The principle, however, would be much clearer and relevant if the ‘governance activity’ was only in relation to explanations on any departure from the Code’s provisions or in relation to any disclosure required by the Code.
- c) The introduction of ‘outcomes-based reporting’ will provide many challenges unless ‘outcomes’ is defined. A definition will ensure that a consistent, interpretable, and repeatable standard of disclosure is achieved. This applies also to Provision 3, where the ‘outcomes’ from engagement with major stakeholders can be vague, e.g., is it obtaining a greater awareness and understanding of the views of these stakeholders, or is it more specific, relating to specific actions taken by the board and the results of those actions?

#### Q2 - Do you think the board should report on the company’s climate ambitions and transition planning, in the context of its strategy, as well as the surrounding governance?

- a) Yes. Climate ambitions and transition planning have become a critical part of business purpose, strategy, and values. The disclosure requirements for these are best addressed by established sustainability reporting standards and requirements, including the Task Force on Climate-Related Financial Disclosures (TCFD). It is appropriate that the Code refers to the board’s consideration of all material sustainability and ESG matters.

#### Q3 - Do you have any comments on the other changes proposed to Section 1?

- a) We welcome the additional emphasis on culture in Provision 2. There is a concern that requiring a board to “report on how effectively the desired culture has been embedded” is very broad and will lead to boilerplate

statements unless there is accompanying additional guidance. While the board will rightly have to choose the most appropriate methodology for assessing how effectively desired culture has been embedded, and how this is reported, these should be disclosed to provide context and understanding for the user.

- b) Further guidance from the FRC should illustrate how 'embedding culture' can be reported, in addition to clarification and confirmation that reporting on "how effectively desired culture is embedded" is different to "reporting on the culture that exists" in the organisation. The former can reference values and behaviours promotion, policies, procedures, controls, training, evidence of leading by example, etc. The latter is more challenging, as organisational culture is constantly in flux, and any measurement is at best indicative of a culture that may exist at a point in time.
- c) We welcome retention of the emphasis on 'workforce' in Provision 5, but strongly recommend including a definition of 'workforce' within the Code. A definition is currently included in the FRC's *Guidance on Board Effectiveness*; it would provide for better understanding and promote greater consistency if included within the Code.
- d) In general, we believe it is important to always keep in mind the balance of costs and benefits of any reporting requirements introduced by the Code, including the audit and assurance implications. Increasing complexity and reporting requirements are adding significant costs and have an impact on all areas of an organisation. Reporting is not only a matter for the finance function; due to the increase in reporting operational, environmental, and other data, it is now the remit of the entire organisation. We encourage and support an approach whereby the Code embeds existing reporting obligations rather than increasing their number.

## Section 2: Division of responsibilities

### **Q4 - Do you agree with the proposed change to Code Principle K (in Section 3 of the Code), which makes the issue of significant external commitments an explicit part of board performance reviews?**

- a) Yes. If a board is to perform at a high level it needs to ensure several factors are in place, including that board members have sufficient time to devote to it. Board performance review is the right tool to ensure that this is the case and to examine significant external commitments of each board member.

### **Q5 - Do you agree with the proposed change to Code Provision 15, which is designed to encourage greater transparency on directors' commitments to other organisations?**

- a) In the absence of a definition there will be an inconsistent interpretation of what is a 'significant appointment' or 'commitment'. Furthermore, there are many factors that should be considered when

determining the likely demands on directors' time and the number of appointments held does not always reflect this. We believe it is better to consider this issue from two perspectives:

*1. Focus on overall process rather than a single factor:*

- Director appointments are a matter of public record and can be ascertained via a corporate search facility. Director appointments are only one factor to consider when determining whether a director has sufficient time to allocate to the board. There may be demands on time from other commitments, professional or otherwise, and the level of an individual's familiarity or competency with a particular board matter will also be a determinant of the time they need to allocate to that matter.
- Disclosure should instead focus on an explanation of the board's process for ensuring directors are allocating sufficient time to fulfil their responsibilities. This may include assessment as part of the annual board performance review, and governance processes such as appointments, annual review of the board's skills matrix, contractual arrangements with directors, including clauses dealing with time commitment, and the board considering time commitments when reviewing an approval request for any additional director external appointment.

*2. Conflict of Interest:*

- There is a duty on directors to avoid conflicts of interest, and this may be extended to considering whether a director has competing demands for time that they should be properly allocating to fulfilling their responsibilities on the board.

### **Section 3: Composition, succession and evaluation**

**Q6 - Do you consider that the proposals outlined effectively strengthen and support existing regulations in this area, without introducing duplication?**

- a) Except for matters addressed in response to Question 7 of this consultation, we agree that the Code adequately addresses diversity and inclusion and it is appropriate not to duplicate mandatory and voluntary requirements outside of the Code.

**Q7 - Do you support the changes to Principle I moving away from a list of diversity characteristics to the proposed approach which aims to capture wider characteristics of diversity?**

- a) We agree with the need to strengthen the Code in this area and support the amendment to add 'inclusion'. We also agree with extending the consideration of diversity beyond gender and ethnicity, but we are not convinced this is achieved by including consideration of 'protected and non-protected' characteristics. Consideration of these characteristics is not a 'comply or explain' matter. It is unlawful to discriminate against any protected

characteristic under the Equalities Act 2010. Unprotected characteristics are not clearly defined, but when juxtaposed with 'protected characteristics' the reference should simply read 'all characteristics'.

- b) We support the intention of the amendment, but we believe the new wording is too limiting. We propose repurposing the replaced wording of Principle J, merging it with new suggested wording to read as follows: "They should promote equal opportunity, and diversity and inclusion of all characteristics (for example, gender, race, and socioeconomic situation), including cognitive and personal strengths."
- c) For consistency, we also propose amending the wording in Principle K to add "are inclusive" to "...how effectively members are inclusive and work together".
- d) We propose including, as part of Principle J, "consideration should also be given to degree of alignment with the company's purpose, values and culture, and achieving an appropriate balance of key stakeholder perspectives". We believe this is fitting in the context of diversity and inclusion and in alignment with Principles B and C of the Code.

**Q8 - Do you support the changes to Provision 24, and do they offer a transparent approach to reporting on succession planning and senior appointments?**

- a) Except for the three points below, we support the changes to Provision 24. They are practical and make sense for inclusion in the nomination committee report. There is an inextricable link between strategy and ensuring the correct resources are identified and in place to support its implementation, and disclosure provides relevant insight for stakeholders.
- b) On the point relating to succession planning, this is a complex and sensitive subject. We agree the succession planning process should be explained at a high level, but the provision should allow for boards to exclude any level of detail that refers to confidential matters or involves commercially sensitive information.
- c) On the point relating to board performance reviews, we are concerned with the requirement to disclose 'outcomes and actions' as it may also be interpreted to include matters relating to any individual director's performance review. We would welcome a clearer distinction limiting the disclosure of outcomes and actions to overall findings arising from the board performance review only.
- d) Also on this point, for consistency "evaluators" should be replaced with "reviewers", given the amendment to replace "board evaluation" with "board performance review".

**Q9 - Do you support the proposed adoption of the CGI recommendations as set out [on page 13 of the consultation document], and are there particular areas you would like to see covered in guidance in addition to those set out by CGI?**

- a) Please refer to our response to Question 8 for comments in relation to Provision 24 and performance reviews. We recommend clarifying within Provision 22 that board performance reviews can be carried out internally or

externally; however, the chair should commission a regular externally facilitated board performance review. Otherwise, we support the outlined proposals to adopt certain CGI recommendations.

- b) We welcome the commitment to issue guidance on how listed companies can report against Provisions 22 and 24 of the Code. We would also welcome guidance from the FRC on matters included in the *Principles of Good Practice* developed by CGI covering the selection of the reviewer and how the review is conducted and reported on. Furthermore, the CGI Review included a recommendation on defining independent board performance review. We agree that the independent board performance review should not be seen as an assurance function; however, the FRC is well positioned to offer guidance to boards on the level of independence required for a reviewer to be considered 'independent'.

## Section 4: Audit, risk and internal control

### Q10 - Do you agree that all Code companies should prepare an Audit and Assurance Policy, on a 'comply or explain' basis?

- a) We note that the "Draft Companies (Strategic Report and Directors' Report) (Amendment) Regulations 2023" propose that all companies "with a high level of employees and turnover" (750 or more employees and £750 million or more turnover) be required to prepare an Audit and Assurance Policy.
- b) We understand the Code is principles-based and therefore should not seek to duplicate or provide alternative interpretations of matters required by law. We supported the introduction of a requirement for an Audit and Assurance Policy in our response to the Department of Business, Energy, and Industrial Strategy White Paper, "Restoring trust in audit and corporate governance". While we would prefer to see the law limiting the requirement to prepare an Audit and Assurance Policy (a reasonably onerous process) to premium listed companies, we do not expect to see the Code extending this requirement further.
- c) On the basis that the Audit and Assurance Policy will be required by law, this leaves no scope for a 'comply or explain' approach for companies incorporated in the UK. However premium listed international companies would have the option to explain, as they are not obliged to comply by law. We have a concern that this may lead to two-tier reporting for domestic versus foreign-listed issuers.
- d) We support the view that engaging with shareholders and other stakeholders is an effective way to communicate and improve the company's approach to the Audit and Assurance Policy. Stakeholder engagement is well established by listed companies and, practicing good stewardship, stakeholders will drive the engagement according to their priorities. While audit committees may directly engage with stakeholders on specific items, introducing a formal requirement may undermine an existing effective process the company has for stakeholder

engagement, including the board's authority and responsibility to delegate appropriately. We would welcome guidance from the FRC on stakeholder engagement by the audit committee.

**Q11 – Do you agree that amending Provisions 25 and 26 and referring Code companies to the Minimum Standard for Audit Committees is an effective way of removing duplication?**

- a) We agree that the proposal is an effective way of removing duplication for companies with a premium listing on the London Stock Exchange, and which are included within the FTSE 350 index.
- b) However, as acknowledged by the FRC, there will be some non-FTSE 350 companies that will be brought into the scope of the Minimum Standard for Audit Committees because of this proposal. We propose an alternative approach for non-FTSE 350 companies: adding a provision that applies on a comply or explain basis for non-FTSE 350 companies not applying the Minimum Standard for Audit Committees and which includes the aspects of Provisions 26 and 27 that were removed to avoid duplication. This option facilitates non-FTSE 350 companies to state that they comply with the Code without having to provide an explanation that they are not complying with a standard as they are not included in its original scope.

**Q12 – Do you agree that the remit of audit committees should be expanded to include narrative reporting, including sustainability reporting, and where appropriate ESG metrics, where such matters are not reserved for the board?**

- a) We agree with the expansion of the audit committee's remit in relation to sustainability reporting, especially in respect of disclosures and assurance. However, we believe the inclusion of the term 'narrative reporting' is only appropriate to the extent that it relates to narrative included in the annual report and this should be clarified accordingly.
- b) We agree that audit committees play a crucial role in promoting strong corporate governance through their involvement in risk oversight, internal controls, corporate reporting and audit. However, we support the inclusion of a caveat, i.e. "where these matters have not been reserved for the board", as it is important to acknowledge that the board remains ultimately responsible for sustainability governance and the quality of sustainability reporting, and this role should not be a default allocation to the audit committee.
- c) Effective governance requires a collaborative approach to risk management and internal controls and as acknowledged by the FRC, "companies are building experience in different ways". While the audit committee is an important mechanism for monitoring and communicating with the board on the quality of assurance of sustainability reporting and related internal controls, board committees with responsibility for risk, remuneration and nominations will also have key responsibilities to ensure effective oversight of sustainability requirements in the company. It is therefore important that the Code is not overly prescriptive in relation to all aspects of 'narrative reporting' or to assume the audit committee is always "best positioned to oversee ESG"



controls and processes per paragraph 50 of the consultation document. Boards need to have the flexibility to delegate matters to committees as they see fit on a case-by-case basis.

**Q13 – Do you agree that the proposed amendments to the Code strike the right balance in terms of strengthening risk management and internal controls systems in a proportionate way?**

- a) The pending guidance referred to in the Code will be essential to providing a better understanding of the Code’s requirements and demonstrating the scalability (and proportionality) of Provisions 29 and 30. For example, the FRC’s working definition of ‘material weakness’ will provide a guideline for what organisations will include in the annual report. However, in this example clarification should be provided whether there is duplication in Provision 30 to require disclosure of “material weaknesses or failures”, when the working definition of material weakness includes a “failure in the design or operation of the risk management and internal control framework”.
- b) In addition to defining key terms, there is a need for supporting guidance to clarify minimum procedures that directors should perform to ensure a “robust assessment” is performed, including the type of assurance and what framework it should be based on when making the required declaration.
- c) Except for our concern included in our response to Question 15 (below) regarding lack of definition for ‘reporting’, we agree that the proposed Principle N and Provisions 29 and 30 achieve the right balance and serve the public interest with transparent reporting of the establishment and ongoing maintenance of risk management and internal control systems, both integral parts of governance. The comply or explain basis will afford organisations the necessary adaptability to explain any aspect of the provisions with which they have not complied.
- d) There is a concern regarding the effectiveness of the proposed amendments and that they will result in further boilerplate reporting, as how organisations monitor and review effectiveness of these systems is very similar in approach (e.g., board and committee oversight, internal audit function, executive responsibilities, dedicated compliance and risk functions, competent and qualified personnel, etc.). In addition, without defined parameters for which deficiencies constitute a material weakness, boards will differ in how they determine what should be

reported, and there is a risk that either 'no' or 'some generic weaknesses' will be reported, including generic plans to address over a short or medium timeframe.

**Q14 – Should the board’s declaration be based on continuous monitoring throughout the reporting period up to the date of the annual report, or should it be based on the date of the balance sheet?**

- a) We believe the board’s declaration should be based on continuous monitoring throughout the reporting period up to the date of the balance sheet. This fits within an organisation’s existing annual reporting cycle and other ‘annual report’ narrative reporting relating to a defined ‘reporting period’.
- b) Regarding reporting material weaknesses and control effectiveness, we believe this would only be relevant and most useful to a user if the material weakness existed at the balance sheet date. The ‘at balance sheet date’ attestation provides scope for organisations to report before approving the annual report whether the material weakness has since been remediated.

**Q15 - Where controls are referenced in the Code, should 'financial' be changed to 'reporting' to capture controls on narrative as well as financial reporting, or should reporting be limited to controls over financial reporting?**

- a) Without an objective definition of what ‘reporting’ includes, e.g., reporting in the annual report, reference to financial controls should remain unchanged. ‘Reporting’ is a broader term, and it takes place at every level of an organisation and can include internal and external reporting. The meaning of ‘financial controls’ and what they entail are commonly understood, especially in the context of audit committee responsibilities.

**Q16 - To what extent should the guidance set out examples of methodologies or frameworks for the review of the effectiveness of risk management and internal controls systems?**

- a) The guidance should set out a menu of methodologies and/or internal control frameworks that organisations reporting under the Code could apply. It should be clear that the menu is non-exhaustive and accompanied by guidance on how an organisation can select the methodology/framework (from the menu or elsewhere) or design one most suited to their size and scale. For example, COSO may be an appropriate framework for the largest FTSE 100 companies, whereas an alternative methodology/framework would be more suitable for smaller companies applying the Code.
- b) Care should be taken to ensure the guidance is not prescriptive. It can be helpful to include examples explaining how different organisations with different circumstances and characteristics, (e.g., industry, size, complexity,

geographical location, etc.) might design, operate, and monitor their risk management and internal control systems.

- c) The guidance should describe how an effective system of risk management and internal control differs from an ineffective one, providing examples of material weaknesses.

**Q17 - Do you have any proposals regarding the definitional issues, e.g. what constitutes an effective risk management and internal controls system or a material weakness?**

- a) The proposed definitions for ‘material weakness’ and ‘deficiency’ are broader than the existing and more commonly understood definitions used by the Public Company Accounting Oversight Board (PCAOB), Committee of Sponsoring Organizations of the Treadway Commission (COSO) and the International Standards on Auditing (ISA). The same definitions should be used in the Code for consistency and clarity, and the focus should remain on matters reported in the annual report, e.g., financial and company law reporting, sustainability reporting, and any other narrative reporting included in the annual report.
- b) As mentioned in our response to Question 13 certain terms require clarification, such as ‘failure’ in the context of Provision 30, ‘material weaknesses or failures’ versus a ‘failure’ in the context of the proposed definition for ‘material weakness’, “failure in the design or operation of the risk management and internal control framework”.
- c) The Code refers to a “reasonably concluding” (Provision 30) and a “reasonable possibility” in the proposed definition for ‘material weakness’. There is judgement involved in determining what is reasonable and it is dependent on many factors, including availability and access to relevant information, competency, experience, and skillsets. Having a ‘reasonable basis’ is a familiar concept for auditors and the FRC introduced the ‘Third Party Test’ as a proven way to assess objectivity and reasonableness in the Ethical Standard applying to auditors. This achieved a more consistent understanding of reasonableness and ensured a more robust consideration of the concept. The Code should include a similar consideration.
- d) As per our response to Question 15 (above), without an objective definition of what ‘reporting’ includes, e.g., reporting in the annual report, reference to financial controls should remain unchanged. Reporting is a broader term, and it takes place at every level of an organisation and can include internal and external reporting. Financial controls are commonly understood, especially in the context of the audit committee responsibilities.

**Q18 - Are there any other areas in relation to risk management and internal controls which you would like to see covered in guidance?**

- a) In addition to our points raised in responses to Questions 15 to 17, we believe the guidance should include an approach to reconciling disparity between the board reporting on risk management and internal control deficiencies and the material weaknesses reported by the auditors.

**Q19 - Do you agree that current Provision 30, which requires companies to state whether they are adopting a going concern basis of accounting, should be retained to keep this reporting together with reporting on prospects in the next Provision, and to achieve consistency across the Code for all companies (not just PIEs)?**

- a) Yes, we agree with retaining this provision.

**Q20 - Do you agree that all Code companies should continue to report on their future prospects?**

- a) It is sensible to avoid duplication between the Code and legislation, but while UK law will prescribe the requirements for a resilience statement, the Code should retain the principles-based provision for organisations to report on their future prospects. While reporting on future prospects can present challenges (especially in times of macroeconomic, social or political uncertainty, or polycrisis), the amended provision is appropriate and beneficial to shareholders and other users of the annual report.
- b) While Provision 31 defines a time period of at least twelve months from the date of approval of the financial statements in relation to going concern attestations from the board, Provision 32 is silent on the minimum period to be assessed in relation to the viability statement. While it is appropriate for each organisation to set a period more relevant to their circumstances (bearing in mind their strategy, markets in which they operate, product or service maturity, etc.) directors will welcome guidance on how a minimum period should be determined.

**Q21 – Do you agree that the proposed revisions to the Code provide sufficient flexibility for non-PIE Code companies to report on their future prospects?**

- a) As per our response to Question 20, reporting on future prospects can present challenges, and while the amended provision is appropriate, there is a risk of losing some of the benefit to shareholders and other users of the annual report arising from current reporting on future prospects based on the way the proposals are set

out. Further guidance from the FRC on setting an appropriate minimum period to consider future prospects and viability would be welcome.

- b) The fact that an organisation can approach the Code on a ‘comply or explain’ basis ensures proportionality and provides some flexibility.

## **Section 5: Remuneration**

### **Q22 - Do the proposed revisions strengthen the links between remuneration policy and corporate performance?**

- a) Yes. The emphasis on transparency and link to long-term sustainable success, including ESG objectives, is important.

### **Q23 - Do you agree that the proposed reporting changes around malus and clawback will result in an improvement in transparency?**

- a) The consultation papers refer to proposed guidance on the suggested format of reporting companies use of their malus and clawback provisions in the last five years. Guidance in this area will be necessary and should include circumstances where non-disclosure or confidentiality agreements may impact the ability to report certain details.

### **Q24 - Do you agree with the proposed changes to Provisions 40 and 41?**

- a) We agree with the basis for removing current Provision 40; however, Provision 33 does not fully address all the criteria listed and we believe the content has benefit and should be included in guidance. While the content of the current Provision 40 is often used as a template for reporting, it has been a reliable guide for remuneration committees in determining executive director remuneration policy and remuneration. It would be unfortunate to lose other practical benefits arising from applying the provision because of boilerplate reporting.
- b) We agree with the proposed Provision 43.

### **Q25 - Should the reference to pay gaps and pay ratios be removed, or strengthened?**

- a) The legal gender pay-gap reporting requirements address this area adequately and there is no need for duplication in the Code. Provision 34 could emphasise the matter as part of determining an appropriate remuneration policy by including after “ensure outcomes are proportionate”, “equitable (including being considerate of any pay gaps and ratios)”.

**Q26 - Are there any areas of the Code which you consider require amendment or additional guidance, in support of the Government's White Paper on artificial intelligence?**

- a) Artificial intelligence (AI) is proving to be transformative. With a range of significant new tools launched every day, AI is changing the way we work, and how organisations are managed and controlled. The UK Government's white paper recommends that "governance measures should be in place to ensure effective oversight of the supply and use of AI systems, with clear lines of accountability established across the AI life cycle." The Code's Principles are appropriately high level and sufficiently broad to focus on mechanisms including purpose, values, strategy, policies, processes, information, and resources. AI tools may be deployed by an organisation within any of these mechanisms. However, the overall principles of the Code remain relevant and applicable. Examples of how AI can impact these mechanisms, and some considerations for FRC guidance in this area, include:
- i. Purpose – market forces, and emerging threats and opportunities presenting because of AI may challenge the purpose of the organisation and its long-term objectives.
  - ii. Values – The International Ethics Standards Board for Accountants (IESBA) has revised the *Code of Ethics for Professional Accountants* to reflect the impact of technology, including AI, on behaviours and decision-making processes in the accounting profession. AI will similarly have an impact on organisational values and culture, and good governance mechanisms will be required to manage and control this. Ensuring competency and an awareness of bias in the output from AI will be an important responsibility for anyone making decisions based on information it provides.
  - iii. Strategy – Strengths, weaknesses, opportunities and threats are all likely to arise as a result of AI and organisations will need to adapt or devise their strategies accordingly.
  - iv. Policies – Other than considering organisational policies on the use of AI, some existing risk management and internal control policies may require amendment. AI is also likely to impact areas such as an organisation's Audit and Assurance Policy, including the use of AI tools as part of assurance procedures.
  - v. Processes – Organisations, including the board, can expect AI to impact many processes, and the Principle H of the Code is sufficiently broad to address this consideration.
  - vi. Information – Transparency will be an important objective regarding the use of AI, including obtaining required permissions for the use of data, how the data will be used, the analysis performed, the level of validation, the level of reliance on output information and its significance/weight in decision-making.
- b) AI is a technological tool, and as such it will require effective risk management and internal controls around its deployment, use and the level of reliance on its output. Depending on an organisation's level of exposure to AI, the board will require some level of competency in AI and/or access to expertise to fully comprehend its impact and potential for the long-term success of the company. As the FRC continues to review corporate governance reporting and note, through stakeholder engagement, the evolving use of AI, there will be opportunities to consider the effectiveness of the principles and provisions of the Code and whether revisions are necessary.