

# Response of the Institute of Business Ethics to the Financial Reporting Council consultation on proposed revisions to the UK Corporate Governance Code

## Introduction

The Institute of Business Ethics was established in 1986 to champion the highest standards of ethical behaviour in business. We are a registered charity with a wide and solid network of supporters who contribute with their individual and corporate donations.

For the past four decades, the IBE has advised leading organisations of all sizes, including those listed in the FTSE 100 and 250, on how to strengthen their ethical culture by sharing knowledge and good practice. Working closely with boards and executive leaders, the IBE:

- Advises senior business leaders and those with responsibility for developing and embedding corporate ethics policies
- Supports the development of these policies through networking events, research, benchmarking guidance and training
- Works with universities and young people to support the next generation of business leaders

The IBE welcomes the opportunity to contribute to this consultation and we hope our comments are helpful.

## General comments

The IBE broadly supports the proposed changes to the UK Corporate Governance Code currently being consulted on. They add robustness and clarity to the Code, prioritising impact and capitalising on the flexibility of a principles-based code.

The IBE would recommend including ethical risks as one of the areas that the boards will need to consider when establishing and maintaining the risk management and internal control framework.

Currently there is little guidance available to the boards on how they should promote and monitor business culture. Under the UK Corporate Governance Code, the board of a listed company is required to 'establish the company's purpose, values and strategy, and satisfy itself that these and its culture are all aligned. All directors must act with integrity, lead by example and promote the desired culture'.

The importance of establishing an ethical culture is now widely recognised across organisations in the private, public and third sectors.

Aiming to help boards to 'promote the desired culture', in early 2023 the IBE convened a steering group comprising a majority of non-executive board members of major businesses, alongside a senior business ethics practitioner and a company secretary to develop guidance for boards on how to promote an ethical business culture within their organisations. During the summer, we consulted on

the draft guidance, and plan to publish a final version this autumn. The IBE would welcome reference to its new board guidance, which we believe will prove an invaluable resource to businesses seeking to establish an ethical culture, either in the Code or in its supporting guidance.

Please see below our responses to the questions in the consultation document where we have a contribution to make.

## **Answers to the consultation questions**

### **Section 1**

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

We share the desire to achieve outcomes-based reporting and think it is a positive ambition. The IBE would also welcome more guidance for companies on what is expected. In our experience businesses find it challenging to decide which metrics to track to measure culture, including the ethical aspects of culture, and there are limited public examples available, especially given the particular complexity of ethical performance reporting.

#### **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?**

The IBE agrees that reporting should include that related to climate change mitigation – namely, carbon emissions reductions throughout the value chain towards a target aligned with the global ambitions of reaching net zero by 2050. We think that the expectation of companies reporting on progress towards their climate targets as part of their ESG strategy and efforts would be consistent with the desire to promote more outcomes-based reporting.

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

Principle B talks about a *desired culture* and *workforce policies and practice*. We would suggest reinforcing the message by making an explicit reference to ethics in business, for example: *The board should establish the company's purpose, values and strategy, and satisfy itself that these and its culture are all aligned. All directors must act with integrity, lead by example and promote ~~the desired~~ \* an ethical culture \*. The board should ensure that workforce policies and practices, \* including any Code of Ethics \*, are consistent with the company's values and support its long-term sustainable success.* We also suggest that, wherever appropriate throughout the document, explicit reference is made to *ethical culture, integrity, and values*.

## Section 2

**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?**

Yes, the IBE supports this change.

**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?**

Yes, the IBE supports this change.

## Section 3

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

Yes, the IBE supports these changes which, while avoiding duplication, do introduce a broad understanding of diversity and inclusion.

**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?**

Yes, the IBE supports these changes. They align with the IBE's [The Ethics of Diversity report](#) in which the authors discuss the need to broaden diversity strategies and look beyond specific protected characteristics in favour of diversity of thought, which will inevitably benefit from diversity in all its forms and dimensions.

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

While the IBE fully supports gender balance and welcomes the fact that boards are asked to report on this, we find that referring to it specifically might conflict with the message on a broad understanding of diversity and inclusion endorsed in Principle I. We assume this may be deliberate to be consistent with existing regulation, but suggest that the wording is changed to include broader aspects of diversity, as in Principle I, for clarity and consistency purposes. We support all other changes to Provision 24.

**Q9: Do you support the proposed adoption of the CGI recommendations as set out above, and are there particular areas you would like to see covered in guidance in addition to those set out by CGI?**

Yes, the IBE supports the adoption of the CGI recommendations.

## Section 4

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

Yes, the IBE supports this.

**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?**

Yes, the IBE supports this.

**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?**

Yes, the IBE supports this.

\*\*\* The IBE has no further comments to make on the remaining questions in Section 4. \*\*\*

## Section 5

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

The IBE view is that it would be appropriate for executive remuneration to reflect the achievement of an ethical culture, driven by the company's purpose and values. A significant finding of the [IBE's 2023 Annual Survey on British Public's Attitudes Towards Business](#), was that over two-thirds of the public believe that it is very important/important for a chief executive's pay to reflect the ethical performance of their company.

We therefore suggest amending Principle P and make it explicit for ethical performance to be a factor considered in remuneration policies. We suggest rewording it so it reads as follows: *Remuneration outcomes should be clearly aligned to company performance, purpose and values, inclusive of the successful establishment and practice of an ethical culture, and the delivery of the company's long-term strategy along with environmental, social and governance objectives.*

\*\*\* The IBE has no further comments to make on the remaining questions in Section 5. \*\*\*

**Other matters for consideration**

**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?**

The use of AI opens numerous opportunities to businesses and poses great challenges and risks that must be considered and addressed. At the IBE we are currently working with our supporters and wider network to better understand how companies are using AI, with the aim of developing a principles-based guidance on the ethical use of AI tools.

We expect this debate to develop quickly over coming months. As an initial starting point, organisations creating or making use of AI tools and systems should set principles that govern their use and report on them as part of their risk and internal controls systems.

**The Institute of Business Ethics**

**8<sup>th</sup> September 2023**

