

## **Response of the Equality and Human Rights Commission to the Consultation:**

### **Consultation details**

Title:	Consultation Document: Gender Diversity on Boards
Source of consultation:	Financial Reporting Council
Date:	Closing date 29 <sup>th</sup> July 2011

### **For more information please contact**

Name of EHRC contact providing response and their office address:	
John Sharman, Policy Manager, Arndale House, Arndale Centre, Manchester M4 3AQ	
Telephone number:	0161 829 8568
Mobile number:	
Email address:	John.sharman@equalityhumanrights.com

## **Financial Reporting Council (FRC) Consultation: Gender diversity on Boards**

### **1. Background: The Equality and Human Rights Commission**

The Commission is a statutory body established under the Equality Act 2006, which took over the responsibilities of Commission for Racial Equality, Disability Rights Commission and Equal Opportunities Commission. It is the independent advocate for equality and human rights in Britain. It aims to reduce inequality, eliminate discrimination, strengthen good relations between people, and promote and protect human rights. The Commission enforces equality legislation on age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex, sexual orientation, and encourages compliance with the Human Rights Act. It also gives advice and guidance to businesses, the voluntary and public sectors, and to individuals.

### **2. Introduction to our Response**

Lord Davies' review of Women on Boards and accompanying recommendations are welcomed by the Commission which has consistently highlighted and expressed its concern about the slow progress of women to the highest levels in the UK corporate world.

The Commission in its 'Sex and Power'<sup>1</sup> series, the Cranfield University female FTSE Board<sup>2</sup> and the 'Women Matters', Mc Kinsey & Co<sup>3</sup> reports have all charted this lack of progress and called for action to bring about much needed change. Lord Davies makes reference to the EHRC (2008) 'Sex and Power' report which suggested that at the current rate of change it would take more than 70 years to achieve gender- balanced boardrooms in the UK's listed companies. Progress is acknowledged to be slow and by 2010 only 12.5 % of directors were women in FTSE 100 companies and just 7.8% in FTSE 250 companies.

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<sup>1</sup> Equality and Human Rights Commission (2008) *Sex and Power*, Manchester EHRC.

<sup>2</sup> Cranfield School of Management (2010) *The Female FTSE Board report 2010* 'Vinnicombe, Sealy, Graham and Doldor, Cranfield University 2010.

<sup>3</sup> McKinsey and Company, 2007 "Women Matter; gender diversity, a corporate performance driver".

The business case for increased diversity in the Board room and at the executive level is substantiated and unequivocal.<sup>4</sup> The Davies' recommendations provide a framework for practical action which we largely endorse and believe we can add value to as the UK equality regulator.

The Review included a limited number of interviews with experts including Baroness Prosser, the Commission's Deputy Chair, who made a number of recommendations in her response as follows:

- The need for a more open and transparent appointments process.
- Utilising the 'comply or explain' approach to corporate governance in the UK to include a disclosure requirement on gender diversity for listed companies.
- There should be a timed review of progress built into the report and that this is done within a three year time frame.
- Options for further action should be cited in the report and should include the possibility of legal quotas if insufficient progress is made in the three years.
- Appointment of a recognised business leader or leaders to champion the strategy and action plan.

Baroness Prosser made clear that the Commission seeks both an increase in female board membership and greater diversity generally in the board room.

We recognise the role of the key regulator in the sector, the FRC, in moving this agenda forward. The business - led approach prescribed by Davies has the power and influence to succeed if supported by government, shareholders and regulators.

We believe that the Commission's involvement and influence would help to support and monitor change without the need for additional regulation. By for example ensuring that guidance is compliant with the legal framework and consistent with current best practice.

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<sup>4</sup> Lord Davies Review: *Women on Boards* 2010 brings together the evidence base, in particular: McKinsey and Company, 2007 "Women Matter; gender diversity, a corporate performance driver".

### 3. Summary

- The EHRC supports Lord Davies' call for amendments to the UK Corporate Governance Code and welcomes the FRC's constructive proposals for change.
- The EHRC believes that it is important for FRC to include in its case for change the strongly evidenced business case that companies with a higher proportion of women in their executive committees and Boards of directors are also the companies with the best performance.
- The EHRC welcomes the proposed amendment to Provision B.2.4, (the report of the nomination committee) and recommends some strengthening to include a description of the plan for increasing gender equality and a report on progress.
- The Commission believes that it would be helpful to set out the key elements to be covered by the diversity policy as a separate guidance note or as an Annex to the Code. This should focus on gender, including the importance of disaggregated information to identify intersectional issues such as under-representation of black and disabled women on Boards, and also address the wider Diversity agenda.
- The Commission supports the addition of a new supporting principle to Principle B.6 on board evaluation and recommends that this should also include 'progress on meeting its measurable targets'.
- The Commission would be in favour of an early implementation as suggested in option 1 so that the Code would apply to accounting periods on or after June 29 2011.
- The Commission would welcome the opportunity to work in collaboration with the FRC to ensure that the strategy adopted is successful in meeting the Davies Review target of all FTSE 100 boards to aim for a minimum of 25% women on their boards by 2015, without the need for regulation.

## **EHRC response to the Financial Reporting Council Consultation questions.**

Lord Davies' review made a number of recommendations, one of which was that "the Financial Reporting Council should amend the UK Corporate Governance Code to require listed companies to establish a policy concerning boardroom diversity, including measurable objectives for implementing the policy, and disclose annually a summary of the policy and progress made in achieving the objectives".

In its consultation document, the FRC is seeking views on:

1. Whether further changes to the Code are needed in order to help achieve more diverse and more effective boards;
2. If so, what these changes should be. The consultation document includes some draft revisions to the Code, on which comments are sought; and
3. If changes are made to the Code, when these should come into effect.

### **1. Whether further changes to the Code are needed.**

The EHRC supports Lord Davies' call for amendments to the UK Corporate Governance Code and believes that changes are needed to the current Code. We welcome the FRC's constructive proposals for change.

We recognise and appreciate that the FRC believes that diversity, in all its aspects, serves an important purpose in connection with board effectiveness. It has potential benefits in widening the perspectives on business issues and on decision-making, avoiding too great a similarity of attitude and helping companies understand their customers and workforces.

The FRC's specific issues with the low percentages of women directors are rooted in three concerns about board effectiveness:

- that a lack of diversity around the board table may weaken the board by encouraging "group think";

- that such low percentages of women on boards may demonstrate a failure to make full use of the talent pool; and
- that boards with no, or very limited, female membership may be weak in terms of connectivity with, or understanding of, customers and workforce and offer little encouragement to aspiration among female employees.

The EHRC would like to add that, importantly, there is also a business case to be made. The Female FTSE Reports, (Cranfield University, School of Management) and the Women Matter reports (Mc Kinsey & Company) have consistently indicated there are significant differences between companies with and those without female directors. Market capitalisation is significantly higher ( $p = 0.001$ ) in companies with women on the board, although firms with female directors do not have significantly larger workforces. (Cranfield)

The Women Matters reports (Mc Kinsey & company) indicate that companies with more women in their executive committees have better financial performance.

Companies with the highest share of women at Board or top management level out- perform companies with no women. In terms of return on equity the top quartile group exceeds by 41% the group with no women and in terms of operating results the more gender diverse companies exceeds by 56% the group with no women.

This statistically significant analysis confirms that companies with a higher proportion of women in their executive committees are also the companies with the best performance. While this link does not demonstrate causality it does provide a strong factual basis for greater diversity and a business imperative for change.

## **2. Possible changes to the UK Corporate Governance Code**

If a change were to be made to the Code to give effect to Lord Davies' recommendation, the FRC would propose to amend **Provision B.2.4**, which concerns ***the report of the nomination committee***:

'A separate section of the annual report should describe the work of the Nomination committee, including the process it has used in relation to

Board appointments. This section should include a description of the Board's policy on gender diversity in the boardroom, including any measurable objectives that it has set for implementing the policy, and progress on achieving the objectives.

An explanation should be given if neither an external search consultancy nor open advertising has been used in the appointment of a chairman or a non-executive director.'

### **EHRC Response**

- The Commission welcomes this amendment to the Code to give greater effect to the Davies' recommendation. The Commission would recommend that the wording is strengthened as follows (amendments marked in bold italics:

'This section should include a description of the board's policy ***and plan for increasing*** gender diversity in the boardroom, including ***the*** measurable objectives that it has set for implementing the policy, and ***a report on*** progress on achieving the objectives.'

In his report, Lord Davies recommends that "in line with provision B.2.4. Chairmen should disclose meaningful information about the company's appointment process and how it addresses diversity in the company's Annual Report including a description of the search and nominations process".

The FRC does not consider that this recommendation requires a change to the Code, but welcomes views on whether it would be helpful to set out some of the key elements to be covered by a gender diversity policy - such as the criteria used when recruiting directors, or the steps taken to develop senior executive talent - and if so, whether this should be done in the Code or elsewhere.

### **EHRC response**

The Commission believes that it would be helpful to set out some of the key elements to be covered by the diversity policy as a separate guidance note or as an Annex to the Code. This should focus on gender,

including the importance of disaggregated information to identify intersectional issues such as under-representation of black and disabled women on Boards. In addition, whilst recognising the imperative to act on gender, the EHRC believes that the guidance should acknowledge and address the wider Diversity agenda. The Commission would be happy to advise on this matter and work in collaboration with the FRC.

The FRC asks for views on adding a new supporting principle to ***Principle B.6 (on board evaluation)*** which sets out some of the most important elements of any review. For example:

“Evaluation of the board should consider the balance of skills, experience, independence and knowledge of the company on the board, the board’s policy on gender diversity, how the board works together as a unit, and other factors relevant to its effectiveness.”

### **EHRC Response**

- The Commission supports the addition of a new supporting principle on board evaluation and recommends the following (amendment in bold italics):-

“Evaluation of the board should consider the balance of skills, experience, independence and knowledge of the company on the board, the board’s policy on gender diversity ***and progress on meeting its measurable objectives***, how the board works together as a unit, and other factors relevant to its effectiveness.”

### **3. The timing of any changes to the Code**

#### **EHRC response**

The FRC indicates that early implementation to any amendments to the code may be desirable. It may also help in the context of the debate taking place in Europe by demonstrating a workable alternative to quotas. The Commission would be in favour of an early implementation as suggested in option 1 so that the Code would apply to accounting periods on or after June 29 2011. A clear, concise and robust set of amendments should guard against further changes and allow for



reporting by 2012. This would not prevent an earlier response as requested by Lord Davies and this would be appropriate given that the review and its recommendations were published in February 2011.

The Commission, as the equality regulator, would welcome the opportunity to discuss with the FRC how it can assist in the process and work in collaboration, to ensure that the strategy adopted is successful in meeting the Davies Review target of all FTSE 100 boards to aim for a minimum of 25% women on their boards by 2015 without the need for regulation.