The Legal 500 Country Comparative Guides

United Kingdom: Corporate Governance

This country-specific Q&A provides an overview to corporate governance laws and regulations that may occur in United Kingdom.

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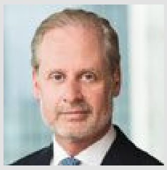

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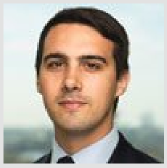

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1. **What is the typical organizational structure of a company and does the structure typically differ if the company is public or private?**

Most commercial companies in the UK adopt one of two forms: a private limited company or a public limited company. Each type of company has a share capital, which is held by shareholders. If a company intends to offer its shares or issue debt to the public, it will generally need to be a public limited company. Public limited companies are also subject to more stringent and detailed requirements under the Companies Act 2006 than private limited companies (for example, certain additional rules in relation to minimum issued share capital, dividends, the timing and content of annual accounts, and the number of directors).

Public limited companies are eligible to be listed on the London Stock Exchange whereas private limited companies are not. The applicable regulations will depend on the particular category of listing but will generally include the Financial Conduct Authority's Listing Rules, Prospectus Regulation Rules, Disclosure Guidance and Transparency Rules and the European Union's Market Abuse Regulation (the "**MAR**"). Foreign listings may also impose requirements. If the company is the subject of a takeover bid, the UK Takeover Code imposes limitations on how directors may act and impinge on the duties that directors owe.

2. **Who are the key corporate actors (e.g., the governing body, management, shareholders and other key constituencies) and what are their primary roles? How are responsibilities divided between the governing body and management?**

The key corporate actors for UK companies are the shareholders, the board of directors and management. Although shareholders automatically have control over certain matters specified in the Companies Act 2006, the company's constitution or other applicable legislation, rules or regulations (for example, changes to the company's constitution or share capital), day-to-day management of the company is delegated by the shareholders to the board.

A company's board may comprise executive and non-executive directors. The executive directors are typically the most important management individuals within the company (usually the Chief Executive Officer and the Chief Financial Officer). The board will often delegate authority to manage the day-to-day business of the company to the executive directors and the management team, but will reserve certain key matters that require specific board approval.

The company normally also appoints non-executive directors to constructively challenge the board and the executive directors in managing the company as agreed in their terms of appointment or service agreements. If the company applies the UK Corporate Governance Code, the non-executive directors should satisfy certain independence criteria (see question 7).

3. **What are the sources of corporate governance requirements?**

The Companies Act 2006 is the primary source of legislation governing all UK companies. All listed companies must also comply with the Listing Rules, Disclosure Guidance and Transparency Rules and the MAR to a certain extent, depending on the applicable category of listing. In addition, premium-listed companies are subject to the UK Corporate Governance Code (as updated in July 2018) on a "comply or explain" basis and must include a statement in their annual report setting out the company's reasons for non-compliance. Many standard-listed companies also choose to voluntarily apply the UK Corporate Governance Code on the same basis as a matter of good governance.

4. **What is the purpose of a company?**

The core or underlying purpose of an English company is the generation of profit for the equitable distribution to shareholders. Over the past 150 years, the statement of a company's purpose or objects within its constitutional documents has gradually eroded such that now many companies do not have a specific purpose specified other than to engage in general commercial activities. On the basis that public trust in companies has eroded alongside purpose, the 2018 UK Corporate Governance Code introduced a principle that the board "*should establish a company's purpose, values and strategy, and satisfy itself that these and its culture are aligned*". The company structure is often tax efficient for both the business and shareholders and provides shareholders with limited liability with respect to the acts or omissions of the company (including its debts).

5. **Is the typical governing body a single board or comprised of more than one board?**

UK companies typically have one single board, comprising a mix of executive and non-executive directors. The board may delegate some of its powers to individual directors, members of management or committees set up for specific purposes.

6. **How are members of the governing body appointed and removed from service?**

Both the board of directors and shareholders have the power to appoint and remove directors under the Companies Act 2006 and under a typical company's constitution. Directors of premium-listed companies may be appointed by the board of directors in the usual course, but their appointment is typically approved by shareholders at the company's next annual general meeting and re-approved on an annual basis thereafter.

7. **Who typically serves on the governing body and are there requirements that govern board composition or impose qualifications for directors regarding independence, diversity, tenure or succession?**

The boards of many smaller private companies comprise executive directors only. The boards of larger private and public companies typically comprise a mix of executive and non-executive directors. Under the UK Corporate Governance Code, at least half of the board (excluding the chairperson) should comprise independent non-executive directors and companies should identify those directors they consider to be independent in their annual report. If the company has established a nomination committee (see question 9), this committee will have responsibility for appointing new directors, arranging succession planning for existing directors and implementing the company's diversity policy. If a formal workforce advisory panel is not in place, the board should include one director appointed by the workforce and one non-executive director should be designated as responsible for workforce engagement.

The UK Corporate Governance Code sets out a list of non-exhaustive criteria that may impair (or appear to impair) a non-executive director's independence, including whether a director:

- is or has been an employee of the company within the last five years;
- has, or had within the last three years, a material business relationship with the company (either directly or indirectly);
- has received or receives additional remuneration from the company apart from a director's fee, or participates in the company's share option or pension schemes;
- has close family ties with any of the company's directors, advisers or senior employees;
- represents a significant shareholder;
- has served on the board for more than nine years; or
- holds cross-directorships or has significant links with other directors through other companies.

The UK Corporate Governance Code also states that there should be a formal and rigorous annual evaluation of the performance of the board, its committees, the chairperson and individual directors. In FTSE 350 companies, this type of evaluation should happen at least every three years. The chairperson should consider arranging external board evaluation and should act on the results of any evaluation by recognising the strengths and addressing any weaknesses of the board. Each director is encouraged to engage with the process and take appropriate action where required.

Boardroom diversity continues to be a major issue in UK corporate governance and, although almost all of the FTSE 100 companies now have a clear policy on boardroom diversity, there remains a perceived failure to improve both ethnic and gender diversity on boards of large public UK companies. FTSE 100 companies remain on track to hit their 2020 target of one-third female board representation, but the FTSE 250 continue to lag behind with only 27.5% in mid-2019.

8. **What are the common approaches to the leadership of the governing body?**

The chairperson's primary role is to lead the board and ensure that the board is effective in its task of setting and implementing the company's direction and strategy. The chairperson is also responsible for ensuring that each of the directors receives timely, accurate and clear information and for acting as the key liaison between the board and the company's shareholders.

The UK Corporate Governance Code recommends that the chairperson should be independent on appointment (see question 7), that the Chief Executive Officer should not also be the chairperson and that the Chief Executive Officer should not go on to become the chairperson. However, as the UK Corporate Governance Code is adhered to on a "comply or explain" basis, a very small number of companies choose not to comply with these requirements if there are good business reasons for not doing so and these should be explained to shareholders in detail.

The UK Corporate Governance Code also states that at least half the board, excluding the chairperson, should be independent non-executive directors. The responsibility of each of the chairperson, Chief Executive Officer, senior independent directors, board and committees should be clear, set out in writing, agreed by the board and made publicly available.

9. **What is the typical committee structure of the governing body?**

The UK Corporate Governance Code recommends that companies establish three primary committees: (i) a nomination committee, (ii) an audit committee and (iii) a remuneration committee, which should be comprised as follows:

- **Nomination Committee:** A majority of the members should be independent non-executive directors. The chairperson of the board should not chair the nomination committee when it is dealing with the appointment of his or her successor.
- **Audit Committee:** All members should be independent non-executive directors and the minimum membership should be three (or two for smaller companies). The chairperson of the board should not be a member. At least one member should have recent and relevant financial expertise.
- **Remuneration Committee:** All members should be independent non-executive directors and the minimum membership should be three (or two for smaller companies). The chairperson of the board should only be a member if they were independent on appointment and should not chair the committee. The appointed chairperson of the committee should have served on a remuneration committee for at least 12 months.

Companies may set up additional committees as required in specific circumstances where the board believes it would be beneficial to delegate elements of its authority (e.g., an M&A/special committee, a risk committee, a corporate governance committee).

10. **How are members of the governing body compensated?**

Most non-executive directors are compensated solely through a director's fee paid by the company, although some non-executive directors may also participate in the company's equity incentive plan in certain circumstances. See question 13 for compensation of executive directors.

If the company has established a remuneration committee (see question 9), this committee will have responsibility for determining the policy for executive director remuneration and setting remuneration for the chairperson, executive directors and senior management. Executive remuneration should be aligned to the company's purpose and values and be clearly linked to the successful delivery of the company's long-term strategy. Under the UK Corporate Governance Code, the remuneration committee is required to ensure that any compensation commitments included in directors' terms of appointment do not reward poor performance.

Directors of a quoted company are required to prepare: (i) an annual remuneration report as part of the company's annual report, which is subject to an annual advisory shareholder vote; and (ii) a remuneration policy, which is subject to a binding shareholder vote at least every three years. Voting on director remuneration has been a major issue in UK corporate governance and several notable shareholder rebellions have been seen where shareholders expressed the view that directors' pay did not fairly represent the performance of the company or that the board had not sufficiently addressed problems within the company.

11. **Are fiduciary duties owed by members of the governing body and to whom are they owed?**

Each director owes statutory duties to the company under the Companies Act 2006, including the duty to: (i) act within their powers; (ii) promote the success of the company; (iii) exercise independent judgment; (iv) exercise reasonable care, skill and diligence; (v) avoid conflicts of interest; (vi) not accept benefits from third parties; and (vii) declare an interest in a proposed transaction or arrangement.

The Companies Act 2006 states that, when considering what is most likely to promote the success of the company, directors should have regard to wider stakeholder needs, including: (i) the likely consequences of any decision in the long-term; (ii) the interests of the company's employees; (iii) the need to foster the company's business relationships with suppliers, customers and others; (iv) the impact of the company's operations on the community and the environment; (v) the desirability of the company maintain a reputation for high standards of business conduct; and (vi) the need to act fairly as between shareholders of the company. From 2019 going forward, all large UK companies (public or private) are required to include a separate statement in their annual report explaining how the directors have had regard to these stakeholder needs when complying with their statutory duties and to publish this statement on their website.

In addition to these statutory duties, directors also owe certain fiduciary and other common law duties (e.g., a duty of confidentiality). Although directors' duties are generally owed to the company rather than to shareholders, it is possible for shareholders to bring a "derivative action" for breach of duty against a director on the company's behalf. If the company is under the threat of insolvency, directors may owe additional duties to creditors.

12. **Do members of the governing body have potential personal liability? If so, what are the key means for protecting against such potential liability?**

Yes, directors may have personal liability in certain circumstances, including: (i) for breach of their statutory or common law duties (see question 11); (ii) for wrongful or fraudulent trading and certain other offences under the Insolvency Act 1986; (iii) for certain bribery offences under the Bribery Act 2010; and (iv) for certain market abuse offences under the MAR (if applicable to the company).

Directors may also be disqualified from being involved in the formation, promotion or management of any UK company in certain circumstances, including where a director has persistently failed to submit certain documents to Companies House or is deemed to be unfit to be a director. The length of time of any disqualification will depend on the specific circumstances but could range anywhere from two to 15 years.

Many companies arrange to purchase a directors' and officers' insurance policy in order to reimburse directors for any losses or costs they might suffer for any actions brought against them for alleged wrongful acts in their capacity as directors or officers of the company (other than as a result of illegal actions).

13. **How are managers typically compensated?**

Managers' compensation will often be a combination of base salary, cash bonus and share incentives under any plans set up by the company. The level of compensation will typically be set by the company's remuneration committee.

14. **How are members of management typically overseen and evaluated?**

Oversight and evaluation of members of management will vary from company to company depending on the management structure and complexity of the company. For smaller private companies, the evaluation process may be limited to an annual review by the company's internal HR function. For larger private and public companies, the evaluation process is likely to be more rigorous and detailed, especially for listed companies where shareholders typically take a deeper interest in the actions and behaviour of management.

The UK Corporate Governance Code states that non-executive directors should scrutinise and hold to account the performance of management and individual executive directors against agreed performance objectives. The chairperson of the board should hold separate meetings with non-executive directors without the executive directors present to facility this type of scrutiny.

15. **Do members of management typically serve on the governing body?**

The boards of many smaller private companies comprise executive directors only. The boards of larger private and public companies typically comprise a mix of executive and non-executive directors. For the majority of companies, the Chief Executive Officer and Chief Financial Officer will serve on the board of directors. The UK Corporate Governance Code imposes certain restrictions on the roles that executives should play within a company. For example, the roles of Chief Executive Officer and chairperson should not be exercised by the same individual and the Chief Executive Officer should not go on to become the chairperson of the same company.

16. **What are the required corporate disclosures, and how are they communicated?**

All UK companies are required to make certain information available to the public by filing it with Companies House. This information includes: (i) copies of the company's constitutional documents and annual accounts; (ii) details of the directors and company secretary (if any); (iii) details of the company's registered office; (iv) persons with significant control of the company; (v) details of the company's share capital; and (vi) copies of any special resolutions passed by the shareholders of the company. This information is publicly available on the Companies House website.

There are additional disclosure requirements for listed companies under the Listing Rules, the Disclosure Guidance and Transparency Rules and the MAR. These include disclosure of: (i) "inside information" (subject to a possible delay in disclosure in specific circumstances); (ii) information relating to significant or related party transactions; (iii) information relating to the company's corporate governance arrangements; (iv) voting rights notifications; and (v) information relating to share issuances or other material information.

The company may also be subject to additional disclosure requirements under the Companies Act 2006 and related legislation or, in a bid situation, the Takeover Code.

17. **How do the governing body and the equity holders of the company communicate or otherwise engage with one another?**

Shareholders and the board of directors have the opportunity to engage with one another through several different mechanisms:

- Firstly, the company's annual general meetings (and any other general meetings) provide a regular forum for discussion between the board and shareholders.
- Secondly, under the UK Corporate Governance Code, the chairperson is designated as the person responsible for monitoring and fostering a healthy relationship with shareholders by seeking regular engagement to understand their views on governance and performance against the company's strategy.
- Thirdly, if the company complies with the UK Corporate Governance Code, it should

appoint one of its independent non-executive directors as the "senior independent director", who will serve as a second intermediary (other than the chairperson) between the board and shareholders.
    - Finally, the chairs of any committees constituted by the board should also seek engagement with shareholders on significant matters related to their areas of responsibility.

The European Union has introduced additional legislation designed to foster long-term shareholder engagement. Following the First Shareholder Rights Directive in 2007, the Second Shareholder Rights Directive ("**SRD II**") came into force in the UK in June 2019. SRD II sets out to strengthen the position of shareholders and to encourage long-term shareholder engagement and transparency between companies and investors. It implements a variety of rules relating to, among other things, shareholder identification, company remuneration arrangements and transparency of certain institutions. Other than legislation, certain institutions (most notably, the Investor Forum) have lobbied for a notion of "collective engagement" and been instrumental in facilitating dialogue between institutional investors and companies.

In the UK, the Financial Reporting Council ("**FRC**") published a revised version of the Stewardship Code in 2019, which works alongside the Corporate Governance Code and is designed to encourage institutional investors, asset managers and their service providers to engage in sustainable and responsible investment and stewardship. Although adherence to the Stewardship Code is voluntary, signatories will be required to report on their methods of engagement with listed companies on an annual basis and this presents an incentive for renewed efforts.

18. **Are dual or multi-class capital structures permitted and how common are they?**

Under the Companies Act 2006, UK companies are permitted to have multiple classes of shares with different rights and restrictions attaching to each class. Under the Listing Rules, the premium listing eligibility criteria do not currently permit a dual-class share structure and, while it is technically possible for companies to list on the standard segment or AIM with such a structure, it is not as common in the UK as in other jurisdictions (notably, the US).

Despite the controversy surrounding dual-class share structures, there has been recent discussion in the UK around whether the Listing Rules should be reviewed to potentially allow premium-listed companies to have a dual-class share structure. In particular, this stems from the competitive desire in the UK to attract high-growth science and technology companies to the London Stock Exchange and the adoption of similar measures by the competing Hong Kong and Singapore stock exchanges to permit such structures.

19. **What percentage of public equity is held by institutional investors versus retail investors?**

Updated data released by the Office of National Statistics in 2019 estimates that the value of UK quoted companies listed on the London Stock Exchange at the end of 2018 was approximately £1.88 trillion, of which 54.9% was held by investors from outside the UK, 31.6% was held by UK-based institutions (including, among others, unit trusts, insurers, pension funds, banks and the public sector) and the balance of 13.5% was held by UK individuals. Although the data does not discriminate between individuals and institutions for non-UK persons, it is highly likely that the majority of these shares are held by institutional investors.

20. **What matters are subject to approval by the shareholders and what are the typical quorum requirements and approval standards? How do shareholders approve matters (e.g., voted at a meeting, written consent)?**

Under the Companies Act 2006, a range of matters are subject to approval by shareholders, including: (i) changes to the company's name, legal form, constitution and capital structure; (ii) removal of directors and auditors; (iii) authority to allot shares and make market purchases of a company's shares; (iv) disapplication of statutory pre-emption rights; (v) declaration of final dividends; and (vi) authorisations of directors' conflicts of interest. Premium-listed companies also require shareholder approval for certain other matters under the Listing Rules, including significant transactions above certain thresholds and related party transactions.

The quorum requirement for a company is set out in the company's constitution but is typically two shareholders (unless the company only has one shareholder). Resolutions may be either ordinary resolutions (which can be passed by a simple majority) or special resolutions (which can be passed by a 75% majority).

Only private companies are permitted to use written resolutions, which must be signed by all shareholders. At a general meeting, voting will either be conducted on a show of hands (one vote per shareholder) or on a poll (one vote per voting share). If a vote is proposed to be conducted on a show of hands, shareholders holding 10% or more of the company's total voting rights may demand a poll.

21. **Are shareholder proposals permitted and what requirements must be met for shareholders to make a proposal?**

Under the Companies Act 2006, shareholders holding 5% or more of any UK company's total voting rights may submit a request for a general meeting of the company to be held. This request must state the general nature of the business to be dealt with at the meeting and also include the text of any resolution that is intended to be moved at the meeting. The company must then circulate a notice of general meeting within 21 days of receiving such request and convene a general meeting within 28 days of the notice.

Shareholders holdings 5% or more of any UK company's total voting rights (or at least 100 members each holding on average £100 of paid up capital) may also require the company to circulate to its shareholders a statement of not more than 1,000 words with respect to any matter or business proposed to be dealt with at an upcoming general meeting. This request must identify the statement to be circulated and be received by the company at least one week before the general meeting to which it relates.

Finally, shareholders holding 5% or more of a public company's total voting rights (or at least 100 members each holding on average £100 of paid up capital) may require a resolution or matter to be put before the annual general meeting of the company. This request must identify the resolutions of which notice is to be given and be received by the company not later than six weeks before the annual general meeting to which the request relates (or, if later, the time at which notice is given of the annual general meeting).

22. May shareholders call special meetings or act by written consent?

Only private companies are permitted to use written resolutions. Shareholders may call a general meeting provided they satisfy specific criteria under the Companies Act 2006. See questions 20 and 21.

23. Is shareholder activism common and what are the recent trends?

Shareholder activism is increasingly common in the UK (as in many other jurisdictions). The most common trends continue to be: (i) advocating for change at the board level (e.g., seeking the removal or replacement of board members); (ii) advocating for or against specific M&A opportunities (e.g., seeking the disposal of particular business segments or the exploration of strategic acquisitions); (iii) lobbying in relation to specific corporate governance issues (e.g., director remuneration or accounting and internal compliance failures); and (iv) wider environmental, social and governance (ESG) issues (e.g., in relation to climate change or gender diversity targets).

24. What is the role of shareholders in electing the governing body?

See question 6.

25. Are shareholder meetings required to be held annually or otherwise, and what information needs to be presented?

Only public companies and private companies that qualify as "traded" companies under the Companies Act 2006 (i.e., any company with shares, securities or debt instruments traded on a capital market) are required to hold an annual general meeting.

The format of most annual general meetings is relatively similar and the typical matters dealt with include: (i) approval of the annual report and accounts; (ii) approval of the remuneration report; (iii) appointment/re-appointment of directors and auditors; (iv) seeking authority to issue and allot shares (including disapplication of pre-emption rights); (v) any amendments to the company’s share capital; (vi) adopting or amending an employee share scheme, and many other matters.

26. **Do any organizations provide voting recommendations or otherwise advise or counsel shareholders on whether to approve matters?**

A number of different organisations provide guidance to institutional shareholders on whether to approve shareholder resolutions of public companies and the impact of any shareholder rebellion votes on matters. These include the Investment Association (which includes the Institutional Voting Information Service), the Pensions and Lifetime Savings Association, the Association of British Insurers and the Pensions Investment Research Consultants. Proxy advisers (such as ISS) who provide services to shareholders of companies within the scope of SRD II are also subject to certain transparency requirements relating to the advice and voting recommendations they give.

27. **What role do other stakeholders, including debt holders, employees, suppliers, customers, the government and communities, typically play in the corporate governance of a company?**

Directors have a statutory duty to consider the interests of other stakeholders when making decisions relating to the company and are now required to state in the company’s annual report how the interests of other stakeholders have been considered in the board’s discussions and decision-making process. See question 11.

The UK Corporate Governance Code sets out several methods that are deemed appropriate for engaging with the company’s workforce: (i) using a director appointed from the workforce; (ii) using a formal workforce advisory panel; or (iii) using a designated non-executive director. If the board has not chosen to use one or more of these methods, it should explain what alternative arrangements it has put in place and why it considers that these arrangements are effective. Members of the workforce should be able to raise concerns confidentially and, if they wish, anonymously.

28. **What consideration is given to ESG (environmental, social and governance) issues, including climate change, sustainability and product safety issues, and are there any legal disclosure obligations regarding the same?**

ESG issues are increasingly important in the UK corporate governance landscape. In November 2019, the Financial Reporting Council published a revised Stewardship Code (effective from 1 January 2020), which redefines “stewardship” as ‘the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society’. The Stewardship Code applies to asset owners, managers and service providers who subscribe on a voluntary basis and is designed to encourage them to engage with listed companies on a number of matters (notably, ESG issues). Signatories are now expected to report on their specific stewardship activities and outcomes over a period of 12 months and the first reports under this new regime are due in March 2021.

Directors also have a statutory duty to consider other stakeholders and the way the company's business might affect such stakeholders when making decisions relating to the company. See question 11 for details on the new reporting requirements that apply from 2019 onwards.

29. **How are the interests of shareholders and other stakeholders factored into decisions of the governing body?**

Directors have a statutory duty to consider the interests of shareholders and other stakeholders when making decisions relating to the company. See questions 11, 27 and 28.

30. **Do public companies typically provide earnings guidance on either a quarterly or annual basis?**

Most UK public companies do not provide quarterly forward-looking earnings guidance, but may provide a quarterly trading update and possibly earnings guidance for the forthcoming year in the company's annual report or end of year trading update. Some UK public companies with a US nexus publish quarterly earnings guidance as a result of their US reporting obligations or practices. See question 16.

31. **May public companies engage in share buybacks and under what circumstances?**

In order for a public company to buy back shares, it must have the ability to do so under its constitution (which would typically be the case) and must seek authority from shareholders to do so (which is typically sought on an annual basis at the company's annual general meeting, subject to certain limits). Buybacks by public companies must be funded either through distributable profits or the proceeds of a fresh issue of shares for the purpose of financing the buyback.

Under the Listing Rules, buybacks must be made by way of tender offer if the price paid is 5% higher than average market value of the company's equity shares for the five business days prior to the day the purchase is made or if purchases are of 15% or more of any class of its equity shares.

Buybacks may be made on- or off-market, though typically listed companies purchase their own shares on market after announcing to the market that they intend to do so. Buyback programmes for listed companies are highly regulated and may be subject to the City Code on Takeovers and Mergers, the Listing Rules, the Disclosure Guidance and Transparency Rules and/or the MAR.

32. **What do you believe will be the three most significant issues influencing corporate governance trends over the next two years?**

We believe that the three most significant issues influencing corporate governance trends in the UK over the next two years will be: (i) ESG issues (including both company and investor reporting); (ii) shareholder activism and the increase in long-term engagement driven by increased transparency and communication between asset owners and asset managers; and (iii) board and management diversity.