Reporting under the new UK Corporate Governance Code

Earlier this year, the Financial Reporting Council ("FRC") announced some important revisions to the UK Corporate Governance Code 2018 ("2018 Code"). The revised document will be known as the UK Corporate Governance Code 2024 ("the Code"). The changes are intended to enhance the transparency and accountability of UK public limited companies and help support the growth and competitiveness of the UK as a place to invest.

In earlier indigoINSIGHTs we have reviewed the amendments to the Code, discussed the FRC's accompanying Guidance and outlined the steps that boards should take to prepare for the changes. In this fourth and final edition in the series, we focus on how companies should report against the Code, the timing of the changes and how compliance will be monitored.

What is the background to the changes made to the Code?

A series of challenges within the UK economy, coupled with several large corporate failures involving high street names, prompted a 2021 UK Government consultation on strengthening the UK's audit, corporate reporting and corporate governance systems. Learnings from the consultation prompted the publication of the 'Restoring trust in audit and corporate governance' reform package.

The Government asked the FRC to use a Code-based approach to support the reform package, and the FRC launched its own consultation on a series of changes to the 2018 Code. However, the Government went on to withdraw the draft secondary legislation it had introduced under the reform package, citing feedback received from companies that the proposed changes were too far-reaching when they already considered themselves to be trading in a challenging market. As a result, the FRC scaled back its proposed revisions but, significantly, has included a specific new reporting requirement on internal controls.

Reporting under the Code

All main market companies are subject to the Financial Conduct Authority's Listing Rules, which require them to state how they have applied the Principles of the Code. This will mainly be communicated through their annual report and accounts.

At the crux of the new reporting requirements is a move away from the tick box compliance approach, which was never encouraged under the 2018 Code, but which has continued to prevail. The new Code requires organisations to explain *how* they have applied the Principles in relation to their own position, outlining the actions that have been taken and the impact that those actions have had. The direction of travel is towards a much more discursive and informative style of narrative, all of which is intended to provide shareholders with a clearer picture, particularly in relation to the outcomes of the board's governance approach. This should help to ensure that annual reports are more reflective of companies' individual contexts and intentions, thereby enhancing transparency and helping to build investor confidence.

Companies will continue to be expected to either comply with the Code's Provisions in full or provide a considered rationale for why they have not done so. From these explanations, shareholders should glean sufficient knowledge to evaluate the effectiveness of the company's approach and its impact on outcomes. This arrangement leaves companies some flexibility to adopt governance arrangements that best suit their business but does not permit them to simply sidestep the Provisions without explanation. Under the Code, detailed clarification must be provided around the reasons behind any non-compliance and the rationale behind the choice of alternative approach pursued. Where applicable, a meaningful target date and clear route to future compliance should be outlined.

Arguably the most significant change introduced to the Code is new Provision 29, which stipulates that boards' risk management and internal controls monitoring and review must cover all material controls, including financial, operational, reporting and compliance controls. As part of the requirements of this new Provision, boards will be required to provide a detailed declaration in their annual report on the effectiveness of both financial and non-financial controls as at the balance sheet date. In order to make this statement, boards will not only want to review the financial and non-financial controls within the business, but will also need to consider what assurance they require in order to give them confidence in the accuracy of the statement they are making. Some assurance may come from internal sources, such as the internal audit team, or from the external audit findings, whilst for other controls bespoke forms of assurance may need to be obtained.

When will the changes take effect?

The Code's changes will apply to financial years beginning on or after 1 January 2025, other than reporting under Provision 29 (internal controls) which will apply to accounting periods beginning on or after 1 January 2026.

How can high standards of reporting on Code compliance be developed?

Compliance against the Code should initially be evaluated internally so that full and transparent reporting can be adopted. As the new reporting requirements include additional emphasis on outcomes, case studies could offer an ideal medium to bring reporting of a company's governance arrangements to life. To aid production of a useful report, it will be essential to keep track of board decisions made, their intended outcomes and timeframes so that actual outcomes can be monitored and reported against them.

Checklists outlining the necessary disclosures will likely be helpful in tracking that the narrative adequately covers the key points, but care should be taken that, in the spirit of the new requirements, such checklists do not encourage tick-box reporting. Under the usual annual report framework, some of the disclosures will likely sit more naturally in the strategic report than the corporate governance statement and, as such, cross-referencing will be essential to avoid repetition and help ensure coherency.

Those responsible for reporting outcomes and explanations for their own company may find inspiration and helpful ideas from other companies' approaches. The annual reports of early adopters of the new Code will likely be eagerly awaited by others who can use them as examples for their own later year-end reporting.

Whilst not subject to audit, the board's disclosures will be reviewed by the auditors for consistency and completeness, adding a further layer of review prior to publication.

The FRC itself monitors reporting against the Code each year via reviews of a sample of companies' annual report and accounts. The assessments cover reporting against both the Principles and Provisions, although the emphasis can vary from year to year. After these reviews, the FRC publishes a report outlining the key themes identified and tracking collective year-on-year progress and areas for development. This can be a great source of information against which to critique your own company's last report & accounts when considering enhancements for next year's version.

Just as significantly, companies' compliance with the Code will naturally be considered by existing shareholders and potential investors. These groups are undoubtedly well-positioned to promote effective governance practice in compliance with the new Code, which is intended to drive improvements in companies' resilience and competitiveness and should ultimately help support economic growth and the UK's attractiveness as a place to invest.

Next steps

If you have any questions or would like to discuss your board's readiness for the changes in reporting requirements, please contact one of our directors:

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