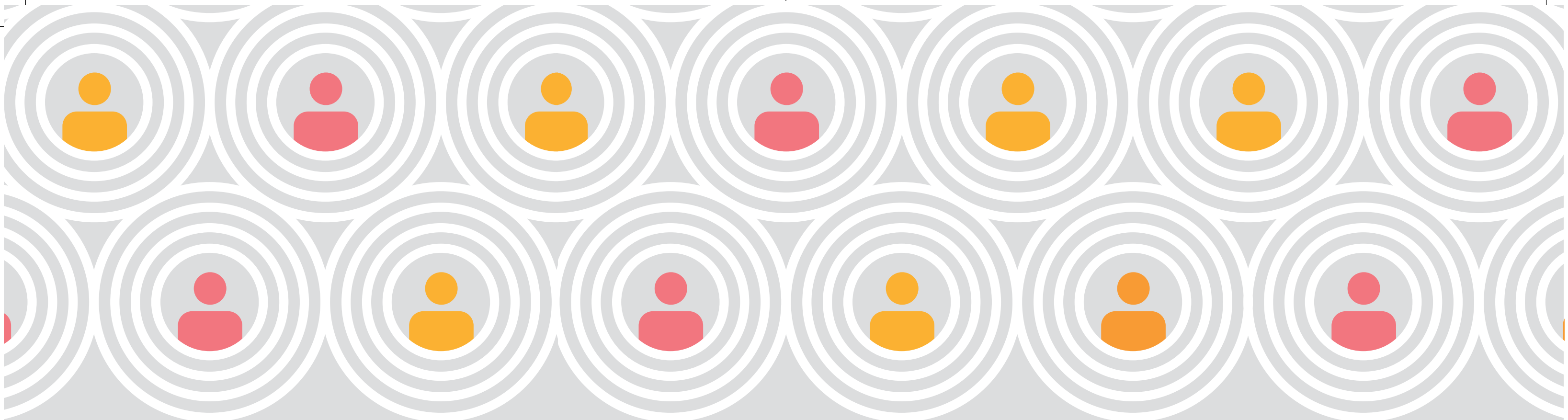

The UK Government has introduced new regulations on corporate governance for private companies, including subsidiaries. These companies will need to include explanations about their corporate governance policies, processes and controls and how they have applied them in their annual report and/or website. This will be the case even if the subsidiary's parent company already operates a corporate governance framework across the group.

Corporate Governance Reform: Implications for Financial Services companies

As part of a broader Trust and Transparency agenda, the UK Government has introduced new regulations on corporate governance for private companies. Effective for financial years beginning on or after **1 January 2019**, eligible UK companies, including subsidiaries of UK and/or overseas listed companies **('UK Subsidiaries')**, will need to report on how they have applied appropriate corporate governance arrangements; how directors have met their duties; and the impact of stakeholder and employee engagement on board decision-making.

In practice, the requirements are more than a simple reporting obligation; the regulations will require a fresh look at corporate governance and how policies and processes are applied at UK Subsidiary level to ensure that each eligible company is able to articulate its own governance arrangements.

Significantly Large companies – on a global basis exceed

1	2,000 employees; OR
2	£200 million turnover AND
3	£2 billion total balance sheet assets

Large companies – exceed two of the following three thresholds:

1	£36 million turnover
2	£18 million total balance sheet assets
3	250 UK employees

Medium companies – exceed two of the following three thresholds:

1	£10.2 million turnover
2	£5.1 million total balance sheet assets
3	50 employees

The table below broadly summarises each reporting requirement and the relevant qualifying conditions:

Reporting requirement	Threshold	Requirement
Corporate governance statement	Significantly Large	• Explain in the directors' report and on a website, which governance code is applied, how it is applied and the reasons for any departure. • If no code was applied, explain the governance arrangements in place.
Section 172 statement	Large and, for financial services companies, Medium	• Explain in the strategic report and on a website how directors have considered and applied their statutory duty to promote the success of the company under section 172 of the Companies Act 2006.
Stakeholder engagement statement	Large	• Explain in the directors' report how directors have had regard to the need to foster business relationships with suppliers, customers and others and the effect of that regard on decision-making.
Employee engagement statement	Companies with over 250 UK employees	• Describe action taken to engage with employees. Summarise how directors had regard to employees in decision-making.

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Reporting requirement	Consideration points
Corporate governance statement	• What governance arrangements are applied by the parent; are they applied across the Group? • What code is most appropriate to apply at a UK Subsidiary level?
Section 172 statement	• Which UK Subsidiaries within the group will be caught? • Are those companies able to make an individual statement? • Will existing board processes enable meaningful reporting? • How are board decisions recorded by each UK Subsidiary?
Stakeholder engagement statement	• Can you identify the relevant stakeholders for each company? • Can group stakeholder engagement mechanisms be used at UK Subsidiary level? • How are decisions influenced by stakeholder engagement? • How will you demonstrate that stakeholder interests are considered within the boardroom?
Employee engagement statement	• How can you create a 2 way dialogue with employees? • What engagement is taking place at the UK Subsidiary level? Is it appropriate to use group employee engagement methods? • How are employee views taken into account in board decision making? • How can you use technology to get unfiltered data to the Board in a way that is relevant and digestible?

How we can help:

We are working with the directors of UK Subsidiaries (and their parent companies), to address the implications of the new rules, including:

1. Assessing which qualifying conditions UK Subsidiaries satisfy in order to determine which of the new rules apply.
2. Undertaking a gap analysis in respect of the existing governance infrastructure in UK Subsidiaries against the required changes.
3. Designing appropriate governance policies and procedures for UK Subsidiaries, taking the strategic objectives of the company (and group) into account.
4. Identifying, constructing and implementing the most appropriate employee and stakeholder engagement arrangements.
5. Training and equipping directors of UK Subsidiaries with the requisite technical skills to meet regulatory requirements and to effectively communicate with stakeholders.
6. Supporting parent companies by ensuring adequate systems are implemented and defining clear protocols for decision-making e.g. global subsidiary governance.

PwC commentary

Acknowledging the increasing importance attributed by stakeholders to a company's governance infrastructure, directors of UK Subsidiaries will need to ensure that they have the requisite skills, systems and policies in place (at the local level), to enable them to understand, apply and report on the required governance matters. The new rules are likely to necessitate UK Subsidiaries undertaking a comprehensive review of their existing processes and procedures, independently of their parent company, to determine how they can most appropriately address the new requirements.

In practice, the requirements represent much more than a reporting obligation; in order to make the relevant disclosures, UK Subsidiaries will either need to design and implement their own policies and processes or explain how they have applied their parent's policies and processes. It will be important for UK Subsidiaries to begin preparing now.

Stakeholders widely recognise the value the new rules bring in seeking to mitigate potential risk and liability related to wider regulatory breaches and corporate failures. If companies do not respond appropriately to the new rules, in addition to reputational and brand implications for UK Subsidiaries (and potentially for their parent and wider group too), repercussions could extend to personal liability for the directors of UK Subsidiaries and potential litigation against UK Subsidiaries.

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190318-104053-DD-OS