

The UK Corporate Governance Code 2024: "small, but important" revisions

February 2, 2024

On 22 January 2024, the Financial Reporting Council (the **FRC**) published a revised version of the UK Corporate Governance Code (**2024 Code**).¹ To support the 2024 Code, the FRC has also since published updated guidance.² The 2024 Code will replace the current 2018 version of the Code for financial periods starting in 2025, as discussed further below.

The UK Corporate Governance Code applies to all companies with a premium listing in the UK, though other companies may also choose to apply it. Under the Financial Conduct Authority's proposals for reform of the UK listing regime for equity shares,³ a new "commercial companies" category will replace the current premium and standard listing segments and it will be a requirement for companies in that category to apply the Code on a "comply or explain" basis. However, companies with a current standard listing of equity shares will not automatically transfer or be required to transfer to the new category and, for those companies, compliance with the Code will remain voluntary.

Background

The FRC originally consulted on revising the current version of the Code in May 2023. At that time, its proposals covered a wider range of issues. However, as the government is not currently taking forward its plans to modernise the legislative framework around audit, corporate reporting, and governance, and in the light of stakeholder feedback, the FRC has adopted a more targeted approach. It has prioritised its revisions to those parts of the Code that deal with internal controls and made a small number of changes to streamline expectations and clarify language.

This measured approach has generally been positively received by market participants, striking the balance between robust governance and minimising reporting burdens on businesses to increase the UK's attractiveness as an investment centre.

Main changes in the 2024 Code

The main changes are as follows:

Audit, risk and internal control

- Principle O has been expanded to make clear that the board is responsible not only for establishing, but also for maintaining the effectiveness of, the risk management and internal control framework.
- Provisions 25 and 26 have been updated to reflect the publication in May 2023 of the FRC's Minimum Standard on Audit Committees and the External Audit, and to remove duplicative language.
- Most significantly, Provision 29 introduces new reporting obligations. The existing expectations for the board to

monitor the company's risk management and internal control framework and carry out a review of its effectiveness, at least on an annual basis, are maintained. However, the updated Provision 29 now additionally requires the board to provide in its annual report:

- a description of how the board has monitored and reviewed the effectiveness of the framework;
- a declaration of effectiveness of the material controls as at the balance sheet date; and
- a description of any material controls which have not operated effectively as at the balance sheet date, including any action taken, or proposed, to improve the controls, and any action to address previously reported issues.

Board leadership and company purpose

- Principle C has been reframed and now requires companies to ensure that their governance reporting focuses on board decisions and their outcomes in the context of the company's strategy and objectives. Where the board reports on departures from the Code's provisions, it should provide a clear explanation.
- Provision 2 expands the board's role to not only assess and monitor company culture but also to ensure that the desired culture has been embedded within their organisation.

Composition, success, and evaluation

- The Code promotes diversity, inclusion, and equal opportunity, without referencing specific groups, through amended Principle J.
- Provision 23 has been amended to acknowledge that companies may have further initiatives in place alongside their diversity and inclusion policy.

Remuneration

- Provision 37 now specifies that directors' contracts and/or other agreements or documents which cover director remuneration should include malus and clawback provisions that would enable the company to recover and/or withhold sums or share awards, and specify the circumstances in which it would be appropriate to do so.
- Provision 38 requires companies to describe their malus and clawback provisions in the annual report. This includes:
 - the circumstances in which malus and clawback provisions could be used;
 - a description of the period for malus and clawback and why the selected period best suits the organisation; and
 - whether the provisions were used in the last reporting and, if so, a clear explanation of the reason.
- Provision 40, which previously detailed characteristics of effective remuneration policy and practices, has been removed.

The "comply or explain" principle

The well-established principle of boards having the flexibility to "comply or explain" remains the foundation of the 2024 Code. The FRC is clear that compliance can mean either complying with the Code's provisions or providing a "cogent

and justified" explanation for why a provision is not suitable in the specific circumstances for the company, whilst demonstrating the principles of good governance.

The FRC has also made it clear that "a good explanation illustrates better governance more than a situation where a board defaults to compliance with a specific Code provision that manifestly doesn't suit its circumstances but where the board lacks the confidence to make the explanation."

Guidance on the 2024 Code

On 29 January 2024, the FRC published guidance to the revised Code (**Guidance**). This provides advice, further detail and examples of good practice to support those who use the Code and will stimulate boards' thinking on how they can carry out their role in governing the company effectively. The FRC has confirmed that the Guidance is available online as a "living document" which may be updated from time to time.

During a webinar accompanying the launch of the Guidance, the FRC re-emphasised that the Guidance is not mandatory, nor an extension of the Code. The release of the Guidance was deliberately delayed to reinforce this point. Nonetheless, boards are encouraged to use the Guidance to inform their decision-making as appropriate. The Guidance incorporates previously published FRC guidance, including the Guidance on Board Effectiveness, Guidance on Audit Committees and Guidance on Risk Management and Related Financial and Business Reporting. Boards can also refer to the FRC's annual reviews for useful examples of good practice.

An area of particular interest in the Guidance for market participants relates to the new reporting obligations under Provision 29. While guidance is included on the new declaration on the effectiveness of the material controls, the FRC has deliberately not defined what constitutes "material controls". This is a matter for the board in the context of the company. The FRC has indicated that this Provision aims to ensure that the board is aware of material issues and areas within the business and how the control environment is performing to mitigate risks. Compliance does not require the board to seek external assurance, but the board can choose to do this if it is deemed appropriate.

It should further be noted that the Code remains "principles based", unlike the statutory prescriptive SOX regime established by the Sarbanes-Oxley Act 2002 in the US. Despite any perceived similarities deriving from the new declaration requirement, the FRC does not have any enforcement powers against the board and therefore parallels to the SOX regime are limited.

Implementation timeline

The 2024 Code will apply to financial years commencing on or after 1 January 2025. Provision 29 relating to the requirement for a board declaration on the effectiveness of risk management and internal controls kicks in a year later, on 1 January 2026. The extended period provides boards with additional time to strengthen their internal control processes and implement the new arrangements.

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1. https://media.frc.org.uk/documents/UK_Corporate_Governance_Code_2024_kRCm5ss.pdf ↩
 2. <https://www.frc.org.uk/library/standards-codes-policy/corporate-governance/corporate-governance-code-guidance/> ↩
 3. <https://www.dentons.com/en/insights/articles/2024/january/4/the-uk-listing-regime-the-fcas-detailed-proposals-for-reform> ↩

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