



Diversity and inclusion on company boards and executive committees

Women on Boards UK response to FCA consultation (CP21/24) September 2021

The FCA proposal offers a positive way forward to continue with the efforts of the last decade or more in the UK to enhance diversity in corporate governance.

Women on Boards UK has played a key role in supporting diverse candidates to step forward effectively and supported companies to recruit for diversity. We urge the FCA to implement these proposals, and indeed recommend the FRC consider them for all listed firms, to help ensure progress is maintained and advanced.

The Hampton-Alexander and Parker Reviews have gathered this data from FTSE350 companies for the last decade. We have seen progress over this period. In our view, this constitutes 'proof of concept' - i.e. that this type of monitoring can drive change. However, the data clearly shows we are far from 'job done'. We were extremely concerned to see the government-led reviews end earlier this year with no firm plans for continuation. Incorporating board diversity into reporting requirements would both continue and strengthen the work done by government, business and others, and ensure progress made does not roll back. We would like to see these proposals implemented as soon as is practicable to offer some continuity with the Hampton-Alexander and Parker Review.

We applaud the targets being set at levels representative of the UK population. Women on Boards has long advocated a 40:40:20 gender split, where 40% of the board is male, 40% female and the remainder the result of natural fluctuation. This represents a true gender balance. Moreover, this 'critical mass' is needed to release the benefits of diversity, most recently evidenced in the recent LBS, SQW and FRC report 'Board Diversity and Effectiveness in the FTSE350'.

The ethnicity target is in line with the Parker Review and broadly aims for representation of the UK population's demographics. However, this should be reviewed as new census data becomes available in order to keep pace with our changing society.

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Correlation vs causation

The correlation between diverse boards and strong company performance is well-established and covers multiple factors such as profitability, share price, shareholder dissent, less excessive risk-taking and even business failure. There is by now a significant and broad body of evidence establishing this strong correlation across territories and sectors, with a few notable studies including Credit Suisse 'Gender 3000', McKinsey's 'Diversity Wins', and the recent LBS, SQW and FRC report 'Board Diversity and Effectiveness in the FTSE350'.

It is likely that companies will be more successful where individuals' performance closely aligns with progression into senior leadership (no-one has yet found evidence - statistically significant or otherwise - of a gender or ethnicity performance gap). It also follows that boards who prioritise diversity of thought and recruit openly for specific expertise, rather than finding a 'good enough' candidate in an established network, will provide more balanced and expert judgement. Diverse board composition is a strong and measurable sign of both of these advantages for company performance being present. Many institutional investors understand this and are therefore pressing firms to diversify their boards.

The FCA rightly notes that this close correlation does not establish a statistically significant causal link between diverse boards and company performance. In our view, it is a combination of internal and external conditions which lead to a firm's success. Board diversity is a contributing, but not sufficient, factor. Whilst we share the FCA's interest in further research into a causal link, we are not aware of any other single reporting requirement that has established a statistically significant causal link to overall company performance.

The strength of the well-established correlation between board diversity and company performance more than justifies a reporting requirement to provide this information to current and potential investors. No-one would suggest investment decisions were made on board composition alone, but it is clearly relevant information when building a picture of a firm's culture, strategy and performance to guide investment choices.

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Numerical data

We believe numerical data, as well as overall compliance with targets, is important to give an accurate picture of a company's board diversity. There is also clearly investor and stakeholder demand for this - as evidenced by 'shareholder activism' on this issue and the strong interest in the detailed Hampton-Alexander and Parker Reviews.

The experience over the past decade has shown that progress in this area is achieved over a number of years. Reporting on the targets alone would mask significant progress made towards them by some firms, and also conceal those who are yielding little to no change in their board composition.

Scope - which companies to include

We are concerned that excluding a large group of firms would reduce stakeholder transparency and risk exaggerating what is a significant 'diversity divide'.

Our Hidden Truth report (June 2021) revealed this gap in the board composition of the FTSE All-Share firms below the 350. We found 48 firms with over 50% female board members and 98 companies with one or no women on their boards. Excluding a large group of companies from these reporting requirements could exaggerate this phenomenon.

It is also important to remember that the 'comply or explain' nature of the proposed requirements already offers a high level of flexibility, eg: for overseas companies whose territories may have significantly different ethnic compositions. We should also remember that biggest need not mean best in this field, and that smaller companies are just as able to excel in diversity and inclusion including at board level.

This is also the reason we urge the FRC to apply a similar requirement to all listed companies.

Timing

We support the proposed timing (introduction for accounting periods starting in or after January 2022). This offers as close to continuity with the Hampton-Alexander and Parker Reviews as is practicable.

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Below board level

We would strongly encourage numerical data on the level below the executive management team to be included in the reporting requirements. Companies should hold and analyse this data as part of monitoring their talent pipeline, so supplying it need not be onerous.

Indeed, the FTSE350 have supplied this information to the Hampton-Alexander (HA) Review for a number of years now. It enhances the picture for investors of how embedded diversity is in the organisation both now and prospects for future, and as such is relevant and useful information.

Our Hidden Truth research into the FTSE All Share, ex 350, shows that progress has been made at the FTSE 350 level in regard to women at the executive level because the spotlight put onto them by the HA report. However, progress at the FTSE 350 level has not trickled down to the executive level of the All-Share outside these larger companies. Our research found that 54% of these smaller listed companies had all-male executive leadership teams. In contrast, the HA Review 2021 reports that at the FTSE 350, only 8% of companies are now all-male at the executive level.

Sexual orientation

The FCA asks if targets on LGBT representation should be included. No comprehensive data has been made available on sexual orientation of board members and the groundwork to support suitable candidates and create inclusive environments has not been done. It is also important to note that individuals may wish - for good reason - not to disclose their sexual orientation and a drive for diversity should not pressurise them into doing so.

Therefore, we believe at this stage setting a realistic target for companies is something to work towards. We would recommend requiring numerical disclosure as a good first step in building an accurate picture of the current representation of this protected characteristic at board and executive committee level.

If you have any questions on this response, please contact:
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