GOVERNANCE NEWS

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NED conference: 10 May 2016

The 2016 AFM conference for Non-Executive Directors will take place on 10 May, at the offices of Fidelity Worldwide Investments in London. These events have proved very popular in the past, and the range of challenges impacting on NEDs is greater than ever this year.

We are planning a wide ranging agenda with a primary focus on NEDs. More details to follow soon, but in the meantime to reserve your Society's free places contact martin@financialmutuals.org.

People with significant control

New regulations may require some friendly societies to keep Registers of People with Significant Control (PSCs). John Gilbert has produced an article on this; see page 3.

SIMR: grandfathering deadline passed

The deadline for grandfathering personnel into the Senior Insurance Managers Regime was 8 February.

Shortly after the deadline PRA issued a reminder to firms to submit applications as soon as possible: http://www.bankofengland.co.uk/pra/Pages/supervision/strengtheningacc/default.aspx

Reporting and governance in 2015

The reporting season has already started: AFM members that have published high level results for 2015 tend to be the largest ones, and these so far have shown strong levels of growth. We've also seen positive statements about the levels of claims paid in the year- where the sector has led the way in transparent reporting.

AFM members are now of course busy preparing for their AGM, and finalising their report and accounts. Prior to completing their annual report, AFM members should complete the Annotated Corporate Governance Code questionnaire; this is now available online via www.afmgovernance.co.uk. Log-in details are the same as for the previous exercise, and can be obtained from martin@financialmutuals.org. The deadline for completing the exercise is again 30 June.

Around a third of members have started the online exercise, including many that have also completed it. Encouragingly, the early results appear to indicate that the changes made to the Code for 2015 have been relatively straightforward for members to adopt. We will continue to monitor feedback via the website, and if this remains the case, give greater emphasis in this year's corporate governance report to the quality of reporting and narrative. In particular, to consider how effectively the strategic report provides the mutual's owners, its members, with a clear understanding of the nature of the business, its strategy, the risks it faces and its future viability.

The non-financial reporting Directive

The Department of Business, Innovation and Skills (BIS) has issued a consultation on the UK implementation of the EU Directive on disclosure of non-financial and diversity information.

The Directive introduces European wide disclosure requirements for environmental, social, employee, human rights, anti-corruption and bribery matters, and Board diversity.

Most of the requirements in the Directive will be familiar to UK mutuals, as they are covered in the Strategic Report, as set out in the Annotated Corporate Governance Code. There are though some differences in the Directive, which is due to take effect for financial years commencing 1 January 2017 of after: in particular an expectation that non-financial statements are validated by the external auditor.

AFM will consider responding to the consultation, which has a deadline of 15 April. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/500760/BIS-16-35-non-financial-reporting-directive-consultation-February-2016.pdf

Forthcoming iNED events

4 April PRA update
4 May FCA update
http://wci-ined-information-bank.co.uk/wp-content/uploads/2015/02/iNED_Temp-Calendar-Dec-2015.pdf.

Viability Statements

As covered last month, the Annotated Corporate Governance Code introduced the concept of a longer term assessment of the prospects of the company, as part of this year's report and accounts. This has become known as the 'longer-term viability statement', and is in addition to the short-term confirmation of 'going concern'; the relevant extracts from the Code is produced below.

The external auditor will be expected to verify that the firm's viability statement is appropriate. This will include considering the available evidence in support: much of the preparatory work for Solvency 2 will assist this, including risk assessments, the ORSA and the results of reverse stress tests.

The statement itself is intended to improve risk management and transparency. As well as the statement, the report should include an explanation of the time period Directors have adopted for assessing longer-term viability, the evidence considered and how principal risks are evaluated. A useful paper from KPMG gives some examples of statements in practice: https://www.kpmg.com/channelislands/en/IssuesAndInsights/ArticlesPublications/events/Documents/a-practical-guide-to-viability-reporting.pdf

Extract from Annotated Corporate Governance Code (v. April 2015)

C.2.1. The directors should confirm in the annual report that they have carried out a robust assessment of the principal risks facing the company, including those that would threaten its business model, future performance, solvency or liquidity. The directors should describe those risks and explain how they are being managed or mitigated.

C.2.2. Taking account of the company's current position and principal risks, the directors should explain in the annual report how they have assessed the prospects of the company, over what period they have done so and why they consider that period to be appropriate. The directors should state whether they have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, drawing attention to any qualifications or assumptions as necessary.

C.2.3 The board should monitor the company's risk management and internal control systems and, at least annually, carry out a review of their effectiveness, and report on that review in the annual report.

Registers of People with Significant Control

- the implications for Friendly Societies

At the end of January 2016 the Government published the final regulations and statutory guidance on the regime requiring companies to maintain Registers of People with Significant Control, which comes into force on 6 April 2016. This does not directly affect friendly societies themselves, but it does impose an extra layer of compliance on the subsidiaries of incorporated friendly societies. Compliance is not likely to be onerous but it is a legal requirement (and failure to comply would constitute a criminal offence by the company and each of its officers).

Legislative Background

The substantive legislation is in Part 21A of the Companies Act 2006, which was inserted into the Companies Act by the Small Business, Enterprise and Employment Act 2015. It comes into force on 6 April 2016 and applies, broadly speaking, to all UK incorporated companies except listed companies. This means that it does apply to any subsidiary of an incorporated friendly society that is a Companies Act company, ie to nearly all friendly society subsidiaries and jointly controlled bodies. It applies regardless of the size of the company and even if it is dormant.

The requirements

All companies (except quoted companies) will be required to investigate whether they have any People with Significant Control (referred to as "PSCs") and then to maintain a register of PSCs along with the company's other statutory books such as its registers of shareholders, directors and company charges. This applies even if the company does not have any PSCs, in which case it must still have a register, which will state that the company has no PSCs.

When the company makes its annual Confirmation Statement to Companies House it will also have to include information on its PSC Register – the annual Confirmation Statement is another innovation from the Small Business, Enterprise and Employment Act 2015 and will replace the Annual Return of companies from 1 July 2016 onwards.

As an alternative to keeping the PSC Register with its statutory books, the company may file the information centrally at Companies House, but if it chooses this option it must keep the central record updated. It is not sufficient to rely on the annual Confirmation Statement to update the central record.

Who is a PSC?

PSCs are defined to include individuals who hold 25% or more of the shares or voting rights in the company or who have the right to appoint or remove directors with 50% or more of the voting rights on the board. The definition extends more generally to anyone who "has the right to exercise, or actually exercises, significant influence or control" over the company either directly or through a trust or similar arrangement. However, directors and employees will not normally be PSCs.

With limited exceptions, which are unlikely to be relevant to friendly societies, a PSC can only be an individual, not a body corporate. However, companies must also note on their PSC Registers any "registerable relevant legal entity". This is an anti-avoidance measure intended to ensure a PSC can still be traced if he or she exercises significant control over a company through one or more holding companies.

How will this affect Friendly Societies?

Most friendly society subsidiaries are wholly owned by the society. An incorporated friendly society is not an individual and, although it is a "legal entity", it will not normally be a "registerable relevant legal entity" (although it could become so if it issues listed securities, such as debenture stock or, in due course, mutual deferred shares). Therefore, in most cases, the PSC Register of a friendly society subsidiary needs only to state that the company has no PSCs.

Where a society has entered into a joint venture and therefore has a "jointly controlled body" under the Friendly Societies Act 1992, the company will need to investigate whether the joint venture partner is a PSC or a registerable relevant legal entity. If a friendly society shares control of a jointly controlled body with another company, that other company is likely to be a registerable relevant legal entity.

Health Warnings

Part 21A on its own runs to 38 pages and is supplemented by regulations as well as by statutory and non-statutory guidance. This note attempts to summarise the important parts of all this material as it will affect most friendly societies but cannot be comprehensive and should not be relied on as such. We would be happy to advise further on how it impacts on the specific circumstances of individual societies.

Compliance with Part 21A is of course additional to compliance with the PRA's and FCA's requirements in relation to the control of any subsidiaries that carry on activities that are regulated under the Financial Services and Markets Act 2000.

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