# 2024 UK Corporate Governance Code

## What's changed and what we can expect

January 2024

The FRC has just released the revised Corporate Governance Code 2024. The main impact will be on Audit and Risk Committees. Here we're aiming to provide a quick update and thoughts on what the changes might mean.

The main changes around reporting on risk management internal control effectiveness will apply from reporting years starting on or after 1 January 2026 but the other (more minor) changes from a year earlier.

## Our headline thoughts:

- It isn't Sarbanes-Oxley, either lite or full-strength. But it's going to have an impact all the same.
- The changes around internal control and risk management are likely to have extensive practical implications for boards, the audit committee, management and "third line".
- The changes are centred around new reporting. But there's a lot of work to do if you're to be confident of being able to tell a good story.
- Audit Committees need to start thinking, planning and overseeing change starting now (along with the Board Risk Committee if you have one). The thinking and changes will take time and need to be in place and working within two years.
- Reporting on control effectiveness as at the balance sheet date also raises a lot of questions about how to get it done and go final in the space of a few weeks.
- Other changes include extra work around emerging risks, and extra reporting for remuneration committees around malus and clawback.

## What are the internal control and risk management changes aiming at?

Mostly it's about making sure that boards are putting enough oversight effort into making sure that internal control and risk management are working effectively.

| Look at Principle O | The Board should: Establish and maintain an effective risk management and internal control framework |
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Typically this is going to be done by the Audit Committee, or it can be done by a wholly independent Board Risk Committee. Here we'll refer only to Audit Committees but mean either.

It's not a big change. Many boards will think that they are already doing this. That's particularly the case in regulated entities who for a long time have been used to explaining what they do to the regulators.

But what's changing is that the Code will require fuller reporting. The approach being used is to drive better practice through making sure that what you say in your annual report is fully supported by what you do in practice.

| Look at Provision 25 Bullet Four | The main roles and responsibilities of the audit committee should include... reviewing the risk management and internal control framework |
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That's pretty much what's already expected. But it's the emphasis on reporting that's different:

| Look at Provision 29: Bullet One | The Annual Report should provide... a description of how the board has monitored and reviewed the effectiveness of the framework |
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At present you've just had to report that you've completed the assessment. From 2026 it's going to be about "how".

This could well mean you have to take a more structured approach to reviewing the effectiveness of material controls. That will likely mean:

- getting a clear, documented picture of how the framework is supposed to work: its objectives, structure, processes, responsibilities, reporting, escalation, accountabilities... across all areas
- ensuring there is consistently visible linkage to strategic objectives
- introducing a model of effectiveness that you can use to answer some key questions: What do we mean by "effective"? How do we gauge "effective"? What are the factors impacting "effectiveness" for us? How do we influence these factors?
- defining what's a "material" control and what isn't
- determining how much to disclose, taking into account commercial sensitivities
- looking at how much assurance you can take from executive-level governance (quality review, reporting, executive committee review self-assessment, self-declaration peer review, data analytics...)
- working out how much "independent" assurance you need over "the effectiveness of internal controls", and where to get it from (internal audit? external audit? other sources?)

**From 2026, Audit Committees are going to be even more busy between year-end and the Annual Report date.** And Board Risk Committees. And Executives, and the Second Line, and Internal Audit too… oh, and the external auditors as well…

That's because the provisions state "at the balance sheet date". So you've got at most a few months between then and Annual Report publication to do the certification and have convincing remediation plans to report.

| Look at Provision 29: Bullet Two | The Annual Report should provide… a declaration of effectiveness of the material controls as at the balance sheet date |
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In practice, determining how things are working "at the balance sheet date" isn't something that can be done between then and the release of the Annual Report. So it will need monitoring processes to ensure control systems are continually effective.

This is very much linked to the assurance questions. Will the audit committee need new levels of assurance - and new types of assurance - on top of what they have already?

Will executive governance have to be strengthened? And how will executive-level assurance get communicated to the Board/Committee in a way that gives the Board sufficient comfort to make a declaration?

Will the executive risk management committee be enough (if you have one)? Is it focussed enough on how the framework works or more on the risk profile and emerging risks? Maybe it would help to have a disclosure committee specifically focussed on internal control and risk management?

| Look at Provision 29: Bullet Three | The Annual Report should provide:<br>A description of any material controls which have not operated effectively at the balance sheet date, the action taken or proposed to improve them and any action taken to address previously reported issues. |
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It seems that a lot is to be expected between balance sheet date and publication. Ineffective material controls need to have been identified as at the balance sheet date, then investigated, evaluated and responded to with a credible, cost-effective remediation action or plan in time for the Annual Report. Some serious planning will be needed…

## What else is there around risk management?

A small wording change around emerging risks will also need careful thought.

| Look at Provision 28 | The board should explain what procedures are in place to identify and manage emerging risks. |
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It's not 100% clear whether this applies only to principal risks or risks more generally: boards will have to make a call on this. But the insertion of "and manage" means that management's development of the response (not just the identification) will need to be sufficiently structured "as a procedure". Just monitoring the emerging risk will often sound pretty weak, which means you will often need to show that you have plans for mitigation.

Either way, it's going to have to be explained to the Committee in a clear and timely way. And if these are emerging material risks, the full board will probably deserve a bit of a briefing too.

This isn't straightforward. At what point does an "emerging risk" start being sufficiently solid to justify a response?

## What about external audit?

The new Code has been simplified by setting out the responsibilities of an Audit Committee by now referencing the "Audit Committees and the External Audit: Minimum Standard".

| Look at Provision 25: Bullet Three | The main roles and responsibilities of the audit committee should include:<br>Following the "Audit Committees and the External Audit: Minimum Standard". |
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This change has been well-trailed and we are not going to cover here this Standard as Audit Committees should already be familiar with its requirements and the implied actions.

The change has the benefit of ensuring there is full alignment between the Code and the Standard.

## What else has changed in the Code?

Not a lot. There are a few places where wording has been tidied up but otherwise the only changes are:

For the Board and Nomination Committees, the wording is simplified around diversity.

| Look at Principle J | Board appointments and succession plans...<br>Should promote diversity, inclusion and equal opportunity. |
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This replaces the somewhat convoluted formulation of "Diversity of gender, social and ethnic backgrounds, cognitive and personal strengths". The new version is simpler. It excludes the points about "strengths" but that is what nomination committees will be considering anyway so the new formulation is simpler and more direct.

For Remuneration Committees there are some reporting changes around malus and clawback (for reporting periods starting 1 January 2025). They should not be difficult to implement as the Committee will already have thought this through.

| Look at Provision 38 | The remuneration report should include a description of the provisions around malus and clawback:<br>• the circumstances in which malus and clawback provisions could be used<br>• a description of the period for malus and clawback and why the selected period is best suited to the organisation<br>• whether the provisions were used in the last reporting period. If so, a clear explanation of the reason should be provided in the annual report. |
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Possibly it's the second part of that last point which could prove tricky; how far should you go in providing an explanation? What will the commercial sensitivities, legal implications and other responsibilities mean for the extent of disclosure?

Around board performance review not a lot has changed. The Code (Provisions 22-23) now refer to "board performance review" instead of evaluation. It's a change - which we greatly welcome - designed to emphasise that board reviews should be focused on helping improve performance for the future, not giving a rating for past performance.

There's also a change to state that a Chair "should commission" a regular-externally facilitated board performance review (not just "consider having"). In practice, virtually all premium-listed companies have moved to this position already, along with many other boards. So its effect will be very limited.


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