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Client Alert
Commentary

Latham & Watkins Capital Markets Practice

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Key Topics for the 2023 UK AGM and Reporting Season

UK listed companies face regulatory changes and developing market practices in the areas of ESG reporting, executive remuneration, share issuance authorities, meeting formats, and structured digital reporting.

Key Points:

- Given the recent developments around climate-related reporting, companies can expect more scrutiny on climate matters in this reporting season. New boardroom diversity disclosure requirements will also apply to financial years beginning on or after 1 April 2022.
- Executive remuneration will be under scrutiny in terms of the cost-of-living crisis, windfall gains arising from the vesting of awards granted during the pandemic, and alignment of pension contributions across the workforce.
- Companies should consider recent guidance on AGM meeting formats and comply with requirements around the structured filing of annual financial reports.

ESG Reporting

Climate-Related Disclosures (TCFD, UK mandatory climate disclosures, and Transition Plans)

This is the first year in which both premium listed companies and certain standard listed companies are required under the Listing Rules to include a statement in their annual financial reports setting out whether they have made climate-related financial disclosures consistent with the TCFD recommendations and recommended disclosures, and explain any non-inclusion. The FCA's first review of TCFD-aligned disclosures by premium listed commercial companies, and the Financial Reporting Council's (FRC) complementary analysis, highlighted some common reporting gaps and areas for improvement in climate-related financial disclosures. As a result, the FCA has recently reminded companies (through Primary Market Bulletin 42) of its rules, guidance and expectations, including by:

- reiterating the importance of building capabilities now to make relevant disclosures;
- reminding companies to assess their disclosures against the TCFD's Guidance for All Sectors and, where relevant, Supplemental Guidance for the Financial Sector and for Non-Financial Groups;
- identifying areas for improvement in listed companies' disclosure of forward-looking information; and
- encouraging better consideration of climate-related risks and opportunities in financial statements, and better connectivity between non-financial and financial disclosures.

Further, with respect to financial years beginning on or after 6 April 2022, UK-registered listed companies are subject to new mandatory climate-related financial disclosure requirements under regulations made on 17 January 2022. These UK regulations require disclosures within the annual financial report that are aligned with, but do not directly mirror, the TCFD recommendations.

Regulators and investor bodies have commented on the quality of climate transition plans published to date which, according to the UK Transition Plan Taskforce (TPT), are “varied in detail and quality”. The TPT will, over the next two years, develop a “gold standard” for transition plans, initially on a voluntary basis but which may in due course reinforce the disclosure requirements for listed companies. On 8 November 2022, the TPT published a draft disclosure framework and implementation guidance for stakeholder consultation, with the consultation process running until 28 February 2023. In the interim, the FCA is encouraging listed companies, especially those making net zero commitments, to use the TCFD’s Guidance on Metrics, Targets and Transition Plans and, in addition, to consider the TPT’s disclosure framework and implementation guidance.

Listed companies can therefore expect more scrutiny on climate matters in this reporting season. Certain proxy advisors may recommend votes against the responsible board member(s) or other relevant agenda item(s) (such as the report and accounts or the remuneration policy) at the AGM if companies do not provide thorough TCFD-aligned climate-related disclosures and/or (particularly in the case of high-emitting companies) fail to set out emission reduction targets or net zero transition plans.

Diversity-Related Disclosures

Recent Listing Rule changes have resulted in additional reporting requirements for premium and certain standard listed companies for financial years beginning on or after 1 April 2022. Their annual financial report needs to include a “comply or explain” statement setting out whether they have met prescribed diversity targets, together with numerical data on the sex or gender identity and ethnic diversity of their board, senior board positions, and executive management (all to be displayed in a standardised table).

The prescribed diversity targets are:

- At least 40% of the board are women
- At least one of the senior board positions is held by a woman (Chair, CEO, Senior Independent Director, or CFO)
- At least one member of the board is from a minority ethnic background (defined by reference to categories recommended by the Office for National Statistics (ONS), excluding those the ONS lists as coming from a White ethnic background)

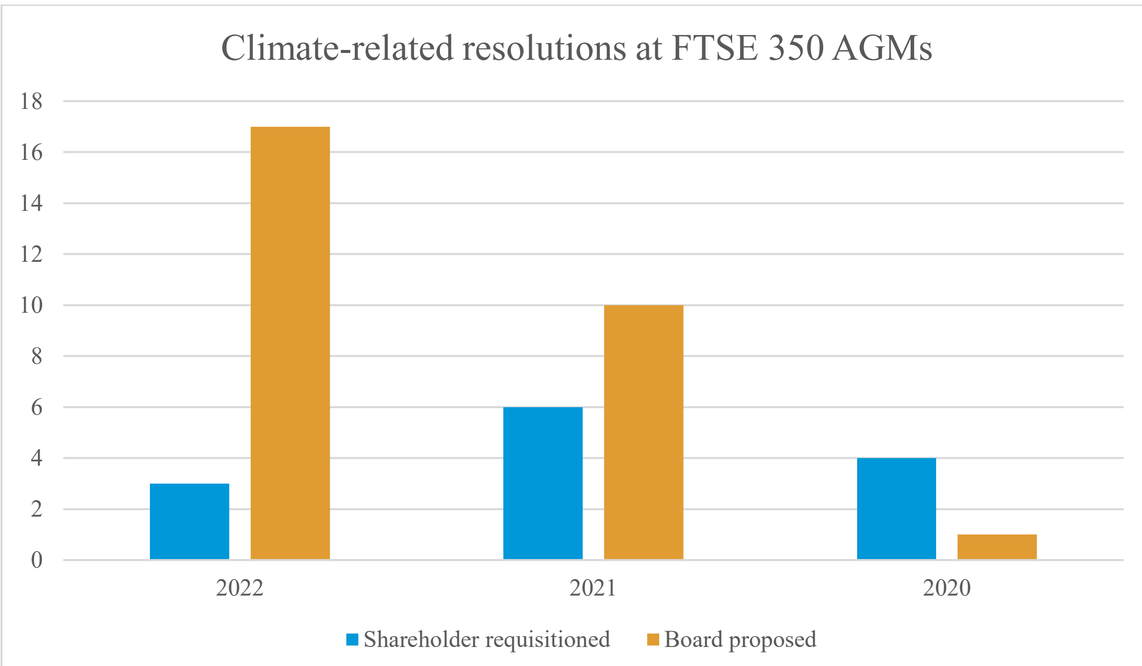
For companies with a 31 December financial year end, the first disclosures will need to appear in their annual financial reports published around Q2 2024. However, the FCA encourages voluntary reporting against these new requirements for earlier periods and expects that investors will welcome the enhanced transparency. Further, the inaugural FTSE Women Leaders Review, published in February 2022, sets out voluntary gender diversity targets which are largely identical to those of the FCA (albeit just for FTSE 350 companies) and to be achieved by the end of 2025.

Companies that fail to meet or appropriately disclose against the new Listing Rule diversity targets for financial years beginning on or after 1 April 2022 may, subject to mitigating factors, receive adverse voting recommendations (typically against the chair of the nomination committee) from proxy advisors at their upcoming AGM.

Climate-Related Resolutions

The last few years have seen a growth in the number of climate-related resolutions being tabled at AGMs. These typically take the form of resolutions proposed by the board inviting shareholders to approve the company's climate strategy or climate transition plan. Shareholders may also requisition these resolutions as part of a public campaign to effect change through requiring the company to submit a climate transition action plan, including emission reduction targets.

Proxy advisors generally determine whether to recommend supporting these resolutions on a case-by case-basis, taking into account the extent of climate risk faced by the company and the completeness and rigor of the company's climate-related disclosures and/or transition plan.



Source: Practical Law

Executive Remuneration

Amid economic uncertainty and a cost-of-living crisis, executive remuneration will remain under heightened scrutiny this AGM season, particularly for companies seeking approval on their remuneration policies this year. Recent guidance from the Investment Association suggest that remuneration committees should consider the following:

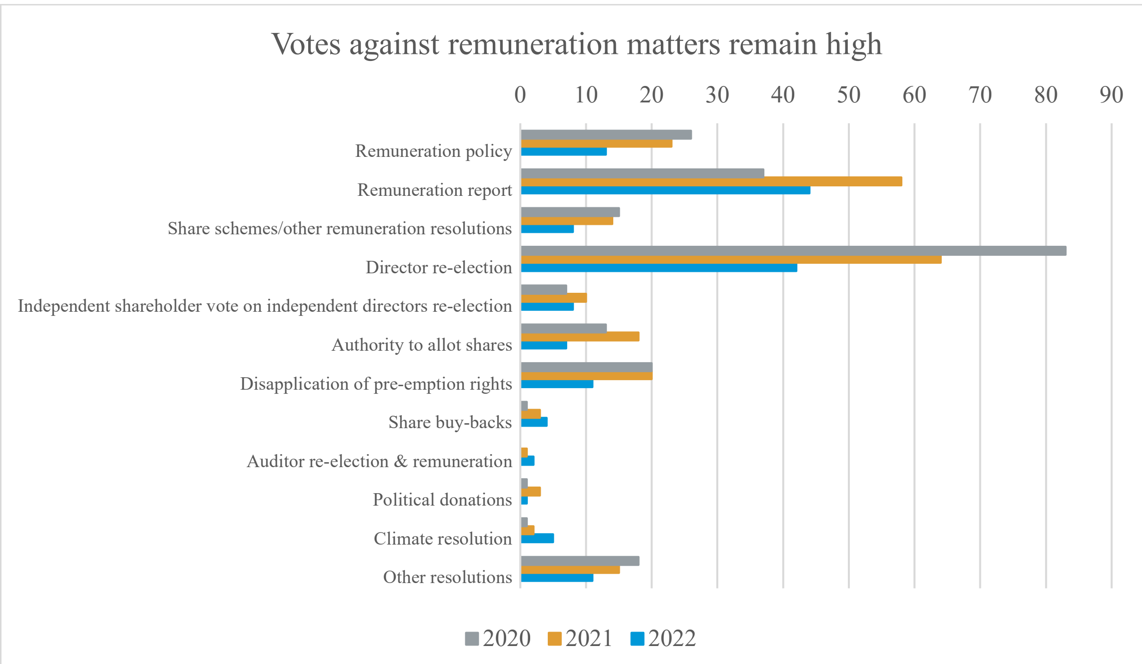
a) *Cost of Living, Inflation and the Stakeholder Experience* — the Investment Association has reminded remuneration committees to delicately navigate the general economic uncertainty when judging 2022 remuneration outcomes and setting remuneration for 2023. This includes:

   - consideration of the wider stakeholder experience,
   - ideally keeping salary increases for executive directors proportionally lower than general increases across the broader workforce, and
   - exercising restraint on any increases to variable pay opportunity in new remuneration policies.

b) *2020 Long Term Incentive Grants & Windfall Gains* — in 2023, many remuneration committees will be making vesting decisions with respect to LTIP grants made in 2020 when, due to the COVID-19 pandemic, share prices were depressed. Remuneration committees should consider if vesting outcomes need to be reduced. If committees do not adjust their windfall gains, they should explain and disclose their rationale.

c) *Pensions* — executive pension contributions should be aligned to the majority of the workforce by the end of 2022. For 2023, IVIS will "Red Top" any non-compliant remuneration policy or report.

d) *ESG metrics* — many more companies have incorporated an ESG metric into their variable remuneration in recent years. Companies need to clearly set out how they plan to incorporate ESG metrics into variable pay in future. Companies without ESG metrics should consider whether their shareholders would benefit from additional disclosure on how the company's executive pay strategy is otherwise aligned with its sustainability strategy.



Source: The Investment Association's Public Register which details companies in the UK FTSE All Share that have received significant opposition by shareholders to a resolution

Share Issuance Authorities

Recent reforms to the UK capital raising regime have prompted the Pre-Emption Group to update its Statement of Principles on 4 November 2022 to permit the annual routine disapplication of pre-emption rights covering:

- 10% of issued ordinary share capital which may be used on an unrestricted basis,
- an additional 10% of issued ordinary share capital to be used for an acquisition or specified capital investment, and

- an additional 20% of any issuance made pursuant to the authorities under the two bullets above, to be used only for follow-on offers to existing shareholders, not allocated shares under those non pre-emptive issues

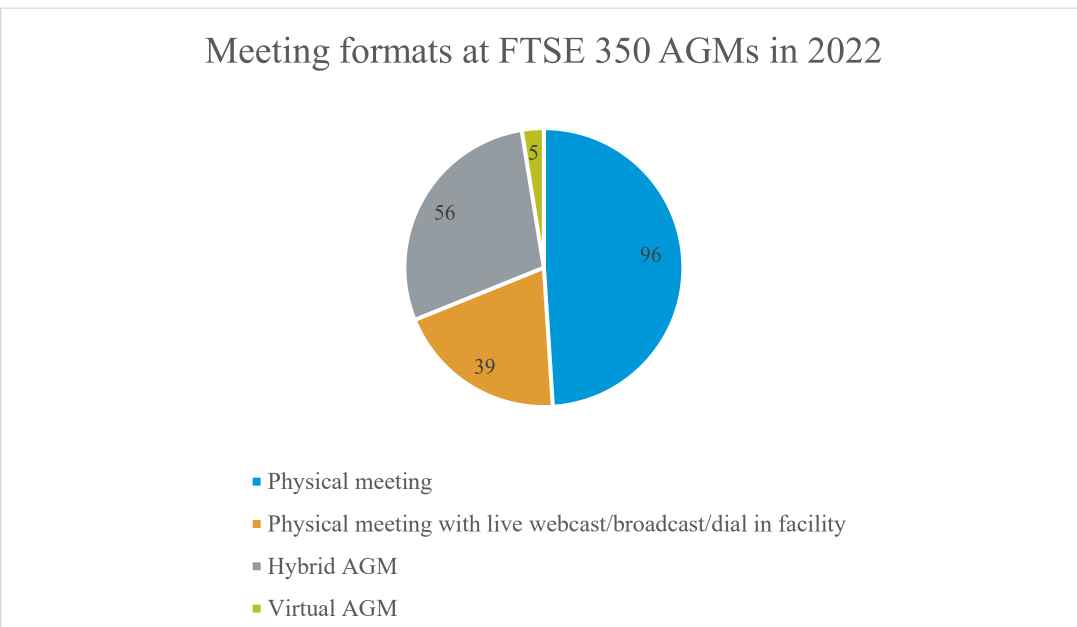
Companies should take advantage of these changes by ensuring that the resolutions within their AGM circulars reflect the increased routine disapplication authorities and also refer to the template resolutions issued by PEG to guide market practice. In addition, Institutional Shareholder Services and Glass Lewis have updated their 2023 policy guidelines to confirm that they support proposals to disapply pre-emption rights up to the thresholds set out in the updated Statement of Principles.

Meeting Formats

Proxy advisors remain broadly supportive of "hybrid" AGMs (i.e., in-person meetings with virtual participation) which have become more prevalent since the COVID-19 pandemic. Most UK listed companies are now able to convene hybrid meetings if they choose to do so, given the number of listed companies who have amended their articles of association in recent years to facilitate this.

However, virtual-only AGMs are still considered to obstruct shareholders from participating in the meeting and communicating with company management and directors. Further, there remains doubt as to whether virtual-only shareholder meetings are valid meetings under English company law, so for now, this format only suits non-UK companies.

Companies should consider recent guidance released by the FRC on planning and conducting general meetings (with a focus on AGMs). The guidance gives practical advice to help companies ensure that their AGMs are well-run constructive forums for effective engagement. In particular, the guidance sets out actions to help companies take advantage of the hybrid meeting format to increase shareholder engagement.



Source: Practical Law

Structured Digital Reporting

This is the second year in which companies admitted to trading on UK regulated markets need to produce their annual financial reports in the electronic reporting format specified in the TD ESEF regulation. For financial years beginning on or after 1 January 2022, companies must also tag the notes, including accounting policies. On 5 December 2022, the FCA announced that it plans to adopt the ESEF reporting manual in January 2023, including the guidance on text block tagging. This would apply in the FCA system for all filings from that point, regardless of the company's reporting period.

Companies should ensure compliance with these requirements and avoid the deficiencies identified in the report published by the FRC on 23 September 2022 which analysed a sample of UK filings. This report sets out the following areas of improvement:

- Process — Companies should implement better naming and structure of the files submitted to the National Storage Mechanism (the lack of which caused many rejected filings). The review and governance processes require more engagement and education, including at management and board level.

- Usability and design — Companies should improve the usability of the report by publishing a validated report on the company's website with an inline viewer.

- Tagging — When selecting tags, companies need to focus on the accounting meaning of their disclosures and avoid unnecessary extensions.

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