

DIVERSITY AND INCLUSION ON COMPANY BOARDS AND EXECUTIVE MANAGEMENT: FCA POLICY STATEMENT

On 20 April 2022, the FCA published a policy statement ([PS22/3](#)) setting out its final policy decision on proposals set out in a consultation ([CP21/24](#)) launched in July 2021 to improve transparency on the diversity of listed company boards and their executive management teams. The measures being implemented are broadly similar to the proposals on which the FCA consulted, with the exception of changes to address concerns raised in consultation responses around the basis for reporting on the representation of women and feedback relating to overseas data protection laws. The new rules apply to accounting periods starting on or after 1 April 2022. However, the FCA is encouraging companies whose financial years began on or after 1 January 2022 to consider reporting on the targets and making the numerical disclosures required by the new rules in relation to their current accounting period on a voluntary basis.

The Listing Rules and Disclosure Guidance and Transparency Rules (Diversity and Inclusion) Instrument 2022 amends: (i) the Listing Rules (**LRs**) to require listed companies to publish annually: (a) a 'comply or explain statement' on whether they have achieved certain board diversity targets; (b) numerical data on the sex or gender identity and ethnicity diversity of their boards, senior board positions and executive management; and (c) an explanation of their approach to collecting the data used for the purposes of these disclosures; and (ii) the Disclosure Guidance and Transparency Rules (**DTRs**) to require companies to ensure that any existing disclosure on diversity policies and their results addresses key board committees and also considers broader aspects of diversity, such as ethnicity, sexual orientation, disability and socio-economic background.

Key issues

- Changes to the LRs introduce new reporting requirements in respect of: (i) board diversity targets on a 'comply or explain' basis; (ii) standardised data on the composition of boards and most senior level of executive management; and (iii) explanation of approach to collecting the data used in the new disclosures.
- Board diversity targets of at least: (i) 40% of the board should be women; (ii) one of the senior board positions (Chair, CEO, SID or CFO) should be a woman; and (iii) one board member should be from a minority ethnic background.
- Changes to the DTRs to widen the range of examples of diversity aspects for issuers to consider in their board diversity policy to include ethnicity, sexual orientation, disability and socio-economic background.
- LR proposals impact UK and overseas issuers with equity shares on premium or standard listing segments of the FCA's Official List; DTR proposals impact UK issuers admitted to UK regulated markets and, through the LRs, certain overseas listed companies.

Updates to the LRs

In-scope companies

The new LR requirements apply to UK and overseas companies with equity shares, or certificates representing equity shares (such as GDRs), admitted to the premium or standard segment of the FCA's Official List, including closed-ended investment funds and sovereign-controlled companies. Open-ended investment companies, shell companies (as defined in LR 5.6.5AR) and issuers of debt securities, securitised derivatives or miscellaneous securities are excluded.

'Comply or explain statement'

The FCA has introduced new LRs (LR 9.8.6R(9) and LR 14.3.33R(1)) to require, as an ongoing listing obligation, in-scope companies to publish in their annual financial reports a 'comply or explain statement' stating whether they have achieved specific board diversity targets (see below) as at a chosen reference date within their accounting period and, if they have not met a target, their reasons for not doing so.

Companies will also be required to set out in their statement:

- the reference date used for the purposes of the 'comply or explain statement' and, where this is different from the reference date used for the purposes of the 'comply or explain statement' in respect of the previous accounting period, an explanation as to why it is different; and
- any changes to the board that have occurred between the reference date and the date on which the annual financial report is approved that have affected the company's ability to meet one or more of the targets.

Board diversity targets

The new statement must disclose against the following targets:

- at least 40% of the board are women;
- at least one of the senior board positions (Chair, Chief Executive Officer (**CEO**), Senior Independent Director (**SID**) or Chief Financial Officer (**CFO**)) is held by a woman; and
- at least one member of the board is from a minority ethnic background (which is defined by reference to categories recommended by the Office for National Statistics (**ONS**) excluding those listed, by the ONS, as coming from a White ethnic background - see Table 2 of the annex at the end of this briefing (**Annex**)).

Numerical reporting tables

The FCA has also introduced new LRs (LR 9.8.6R(10) and LR 14.3.33R(2)) to require in-scope companies to publish numerical data on the sex or gender identity and ethnic diversity of their boards, senior board positions and executive management (see the definition in the box) as at the reference date selected for the purposes of the 'comply or explain statement' in a standardised table format as set out in the Annex.

Explanation of approach to data collection

In-scope companies will be required to explain their approach to collecting the data used for the purposes of making the disclosures set out above. The FCA has included guidance in LR 9.8.6IG and LR 14.3.36G as regards consistency in such approach and on its expectations of what this explanation should

Definition of "executive management"

"the executive committee or most senior executive or managerial body below the board (or where there is no such formal committee or body, the most senior level of managers reporting to the chief executive), including the company secretary but excluding administrative and support staff"

cover. The FCA expects companies to take a consistent approach to data collection, both across the individuals being reported on, and for reporting against the targets and numerical disclosures. The FCA further expects the explanation to include the method of collection and/or source of the data, and where data collection is done on the basis of self-reporting by the individuals concerned, a description of the questions asked.

Additional LR guidance

The FCA has included new guidance in the LRs (LR 9.8.6JG and LR 14.3.37G) to the effect that in-scope companies may also wish to include the following information in their annual financial reports to provide further context:

- a brief summary of any key policies, procedures and processes, and any wider context, that the company considers contribute to improving the diversity of its board and executive management;
- any mitigating factors or circumstances which make achieving diversity on the company's board more challenging (e.g. the size of the board or the country where the company's main operations are located); and
- any risks the company foresees in meeting (or continuing to meet) the board diversity targets in the next accounting period, or any plans to improve the diversity of the company's board.

Updates to the DTRs

In-scope companies

The updates to the DTRs impact UK issuers admitted to UK regulated markets and, through the LRs, certain overseas listed companies (subject to existing exemptions for small and medium companies).

Existing DTR requirements

DTR 7.2.8AR hitherto required an issuer's corporate governance statement to contain a description of the diversity policy applied to the issuer's administrative, management and supervisory bodies with regard to aspects such as, for instance, age, gender or educational and professional backgrounds. The existing DTR also required the issuer to outline the objectives of the diversity policy, how the policy has been implemented and the results in the reporting period. Where no such policy was applied, the issuer was required to explain why this was the case.

New DTR requirements

The FCA has expanded DTR 7.2.8AR to require a company's disclosure on its diversity policy (where it has one) also to:

- include the diversity policy applied to the company's remuneration, audit and nomination committees; and
- cover broader diversity aspects such as, ethnicity, sexual orientation, disability and socio-economic background.

Additional DTR guidance

The FCA has included new guidance in DTR 7.2.8CG that in-scope companies may, where they consider appropriate, include numerical data on the diversity of the board and board committees when describing the results of the diversity policy in the corporate governance statement.

Consistency with voluntary targets

The new targets relating to representation of women on boards are consistent with those recommended by the FTSE Women Leaders Review, an independent, voluntary and business-led initiative supported by the Government that published its first report in February 2022 on the representation of women on FTSE 350 boards and in their leadership teams. The reporting target for representation of individuals from minority ethnic backgrounds is in line with that set under the Parker Review, which recommended in its latest update report published in March 2022 that FTSE 100 companies continue to focus on meeting the "One by 2021" target and FTSE 250 companies continue to work towards meeting the "One by 2024" target (see further details in the box).

Changes of approach since the consultation

The FCA's proposed approach in its consultation included those who self-identify as women in disclosures relating to the representation of women. The FCA noted that some consultation responses highlighted risks to data quality if data collected under its requirements differed from that collected for the purposes of reporting under the Companies Act 2006, which requires reporting on the sex (as opposed to gender identity) of directors and senior managers, and that these differences could also lead to privacy risks. In light of this feedback, the FCA has removed the guidance on self-identification that accompanied the targets and disclosure table in the consultation, and has given companies more flexibility to determine how best to collect data from employees provided that their approach is explained and applied consistently. In particular, for the numerical disclosures, the FCA has made it clear that companies can report on the basis of either sex or gender identity, and may add to the categories included in the pro-forma table to reflect the basis on which it has collected data.

The FCA is also giving greater flexibility in relation to the numerical disclosures to in-scope companies that have board members or executive management situated overseas. In those cases, where local law prevents the collection and/or publication of relevant data, a company may instead explain the extent to which it is unable to make the numerical disclosures. In addition, closed-ended investment funds will be permitted to adjust their disclosures in relation to the target relating to the four senior board positions and their numerical disclosures in the event that these disclosures are inapplicable to the fund, provided that they set out the reasons why the disclosures are inapplicable.

The FCA has also expressly reminded in-scope companies that they remain subject to equalities legislation, including the Equality Act 2010 and its provisions on discrimination. Whilst the FCA has set targets on board diversity for issuers to report against, it is an issuer's responsibility to ensure that its practices (including in relation to board appointments) are lawful and compliant with equalities legislation.

Next steps...

The final rules apply to accounting periods starting on or after 1 April 2022, meaning that the new disclosures will start to appear in annual financial reports published from around Q2 2023 onwards. However, the FCA is encouraging companies whose financial years began on or after 1 January 2022 (the commencement date originally targeted in the consultation) to

FTSE Women Leaders Review

- As at 10 January 2022, women held 39.1% of FTSE 100 board positions (up from 36.2% in 2020) and 36.8% of FTSE 250 board positions (up from 33.2% in 2020).
- To build on the work of the former Hampton-Alexander and Davies Reviews, the Review recommended: (i) increasing the voluntary target for FTSE 350 boards and leadership teams to a minimum of 40% women's representation by the end of 2025; and (ii) FTSE 350 companies having at least one woman in the Chair or SID role and/or one woman in the CEO or Finance Director role by the end of 2025.

The Parker Review

- In 2017, the Parker Review set a "One by 2021" target for all FTSE 100 boards to have at least one director from a minority ethnic background by December 2021 and a similar "One by 2024" target for all FTSE 250 boards.
- As at 31 December 2021, 89 FTSE 100 companies met the "One by 2021" target, and of the 233 FTSE 250 companies that responded to the Review's voluntary census, 128 already met the "One by 2024" target.
- The Review's March 2022 update report recommended that, given that the majority of minority ethnic directors reported were non-executive directors, continued attention be focused on minority ethnic representation amongst executive directors.

consider reporting on the targets and making numerical disclosures in relation to their current accounting period on a voluntary basis.

In order to meet the new requirements, in-scope companies should:

- review any existing board diversity policies (and, if one is not in place, consider developing one);
- identify employees who constitute "executive management";
- consider their existing diversity ratios and, if these do not presently meet the targets, reflect on what steps they can take to widen succession planning and talent pools to include individuals from different backgrounds (whilst ensuring that they remain in compliance with their obligations under the Equality Act 2010); and
- assess how complying with the new rules will impact their data capture approach in the UK (and potentially internationally if their data capture approach is global in nature). This will include the terminology and categorisation they use in collecting data (for example, whether they will include sex or gender as an identifier), and whether this aligns with any separate ESG reporting obligations or voluntary frameworks to which they are subject or are considering adopting.

The FCA has acknowledged that companies must collect data within the prevailing data protection regime (e.g. the UK General Data Protection Regulation (**UK GDPR**) and potentially, in some cases, another jurisdiction's data protection regime) and must have a lawful basis for collecting and processing personal data. Personal data revealing racial or ethnic background are 'special categories of personal data' under the UK GDPR and other data protection laws and are subject to additional restrictions. Whilst there are helpful provisions within the UK GDPR and the UK Data Protection Act 2018 to allow processing of special category personal data for equality of opportunity monitoring purposes, in other jurisdictions the enhanced protections applicable to such data can be more restrictive. Companies with board members and executive management overseas that fall within the scope of these rules will need to understand what data collection and disclosure is permitted in the relevant jurisdictions in order to ensure that they abide by these laws and can make the appropriate explanation regarding the extent to which these laws impact their ability to make the disclosures. Companies with establishments outside the UK which provide data to meet these requirements may also need to consider international data transfer restrictions, both for the internal processing (depending upon the company structure and internal data transfer mechanisms) and in the event that any data provided to the FCA remains personally identifiable. In addition, companies will need to ensure compliance with wider data protection requirements, which in the UK (and many other jurisdictions) would include: (i) updating applicable privacy notices; (ii) minimising data processing so as not to go beyond what is proportionate, taking account of the FCA's requirements and recommendations; and (iii) ensuring that the data is protected by adequate safeguards, for example in relation to security, accuracy, and storage limitation.

...and beyond

The FCA intends to review this policy in three years' time to assess its impact. At that time, the FCA will consider whether to revise the nature or level of the

targets in its rules, and whether to consider targets on other aspects of diversity.

The FCA has indicated that its joint discussion paper ([DP21/2](#)) with the PRA on diversity and inclusion in the financial sector, published in July 2021, was the first step in setting out a new regulatory framework on diversity and inclusion. It is currently considering responses to the paper alongside responses to its recent diversity and inclusion pilot data survey and cost benefit analysis survey, and expects to publish a consultation paper in 2022 setting out proposals to apply broadly across the financial sector (including financial services firms authorised by the FCA which are also listed).

The new requirements should also be seen in the context of a wider global movement by regulators and legislatures (re-enforced by stakeholder pressure) to increase diversity and inclusion across the board, and so - depending on a company's international reach - are one of a range of measures that companies will need to follow in order to keep pace with change in this regard.

ANNEX

Table 1: Reporting table on sex/gender representation

	Number of board members	Percentage of the board	Number of senior positions on the board (CEO, CFO, SID and Chair)	Number in executive management	Percentage of executive management
Men					
Women					
[Other categories]					
Not-specified/prefer not to say					

Table 2: Reporting table on ethnicity representation

	Number of board members	Percentage of the board	Number of senior positions on the board (CEO, CFO, SID and Chair)	Number in executive management	Percentage of executive management
White British or other White (including minority-white groups)					
Mixed/Multiple Ethnic Groups					
Asian/Asian British					
Black/African/Caribbean/Black British					
Other ethnic group, including Arab					
Not specified/prefer not to say					

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