HOUSE OF COMMONS

Business, Energy and Industrial Strategy Committee

Oral evidence: Corporate Governance, HC 702

Tuesday 20 December 2016

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Watch the meeting

Members present: Mr Iain Wright (Chair); Richard Fuller; Amanda Milling; Michelle Thomson; Chris White.

Questions 261-371

Witnesses

I: Denise Wilson, CEO, Hampton/Alexander Review, Tom Shropshire, Steering Committee, Parker Review, Rowena Ironside, Founder and Chair, Women on Boards UK, Edward Speed, Global Chairman, Spencer Stuart, Laurie Fitzjohn-Sykes, Head of Research, Tomorrow's Company.

II: Nigel Wilson, CEO, Legal & General Group, Mick Barker, Group Employee Director, FirstGroup, Tim O'Toole, CEO and Board Member, FirstGroup, Frances O'Grady, General Secretary, Trade Union Congress.

Written evidence from witnesses:

- Tomorrow's Company;
- Women on Boards UK;
- Spencer Stuart;
- Legal & General;
- TUC.

Examination of Witnesses

Witnesses: Denise Wilson, Tom Shropshire, Rowena Ironside, Edward Speed and Laurie Fitzjohn-Sykes.

Q261 **Chair:** Good morning. Thank you for coming to give evidence to us; we are very grateful. For the purposes of the record, could you tell us who you are and which organisation you are representing? I will start with Rowena.

Rowena Ironside: I am Rowena Ironside. I am representing Women on Boards, which is a four-year old UK business helping women of all ages to take on a board role and companies to build their talent pipeline.

Tom Shropshire: I am Tom Shropshire. I am a partner at Linklaters, but I am representing the Parker Review that looked into ethnicity in the boardroom.

Denise Wilson: I am Denise Wilson. I am Chief Executive of the Hampton/Alexander Review, formerly the Davies Review. I am also a NED on Ecclesiastical Insurance's board and a chair of a charity.

Laurie Fitzjohn-Sykes: I am Laurie Fitzjohn-Sykes. I am Director of Research at Tomorrow's Company, a non-profit corporate governance-focused think-tank.

Edward Speed: I am Edward Speed. I am Chairman of the search and leadership advisory business called Spencer Stuart.

Q262 **Chair:** Thank you. This is a question to you all, but I will start with you, Rowena. Is there a problem with corporate governance in this country and, if there is, are there any specific elements that we need to address?

Rowena Ironside: My area of focus is obviously around diversity. The UK is probably a leader in many ways around corporate governance in terms of the way we address it through a comply and explain code. Is it perfect? No. Are we making improvements all the time? Yes.

Tom Shropshire: From my perspective, I guess I have two hats, one as a law firm partner but also in terms of the review. In terms of corporate governance, I do not think of it as a system that is broken; it is a system that constantly has to evolve, because ultimately it is responsive to the environment in which businesses sit and the issues they face.

For me, the question is not whether it is right or wrong, or broken or not broken; it is just a question of constant evolution and being in the right place, enabling companies to move forward. From my perspective, the question around ethnic diversity is really about how we get that diverse thought, experience and forward-looking in order to enable British business to succeed.

Q263 **Chair:** The way you put that is really interesting, Tom. Do you think, given the environment in which we are operating, the ecosystem of corporate governance is fit for purpose?

Tom Shropshire: It probably is broadly fit for purpose. However, there are things that can be improved about it. A lot of corporate governance in my experience is certainly having a framework in place and the policies and procedures that reinforce behaviour. However, there is a lot about transparency, communication and being informed by a broad universe of stakeholders in order to make sure that your decisions are right for the long-term success of the business. It works well, but the factors that impact those various stakeholders are constantly changing, and therefore you need to have the right environment in order to make decisions.

Denise Wilson: I agree with Tom. It works well and it is fit for purpose. It relies on the people that constitute and run corporate governance, so those in boards, in exec committees and leadership teams. We have got an issue there with lack of diversity of race, gender, thought, experience and background.

Whenever you get a group of homogeneous people together, you are going to get some element of groupthink and following the pack, and that has led us to some of the problems that we have had in the past. Most of the research that we have done through the Davies Review has shown that the impact of diverse views—different people at the table, different perspectives and the challenge—is that the debate is richer and the decision-making is ultimately better.

Chair: I am going to come on to that in a moment, because that is really helpful. Thank you.

Laurie Fitzjohn-Sykes: I would take a slightly different view. While we have made much progress over the last few decades on ensuring responsible behaviour and trying to limit the number of scandals, we would say that we have perhaps created too much of a risk-averse culture in our boardrooms. Investment is very worryingly low, boards are using very high hurdle rates to reject profitable investment opportunities, and dividends are at all-time highs. If you look at the evidence, it is hard to say the status quo is working. The number of listed companies is declining by 30% in the last 15 years. Many individuals we hear refuse to be on listed company boards because of the compliance and process focus; they prefer to be on private equity and private company boards.

The irony is that shareholder returns are now the worst since the Great Depression. Public trust is low. Therefore, when you look at the evidence, yes, we have made much progress on limiting the number of scandals and improving the technical aspects of governance, but have we perhaps gone too far? Has the pendulum swung too far, and do we need to refocus boards on long-term wealth creation? How do we give them more courage and confidence to take those risks that work—that we know create success—for family-owned companies and entrepreneurs?

Have we taken away that vigour, which perhaps is behind the success of long-term business?

Q264 **Chair:** Do you link that culture back to corporate governance, in terms of that risk aversion, that poorer return and that low level of investment? Is that all thanks to corporate governance? I am distorting it for effect, but you know what I mean.

Laurie Fitzjohn-Sykes: There are many factors, but corporate governance plays its part. Ultimately, the decision of how much you invest is a boardroom decision, and therefore if you have a culture in the boardroom that is perhaps a bit too cautious, you are going to err on the side of not investing long term. You see that caution not only in low investment but also, perhaps, in the small number of executives and directors who are prepared to put their head above the parapet and tackle the thorny issues of executive pay and corporation tax. We often talk to people privately and they voice concerns, but how many people publicly try to take on these issues? That is another signal that there is too much caution in the boardroom bubble.

Q265 **Chair:** This is really interesting, and I will come on to this again. We might explore this in conversation. Is that because of too-dominant chief executives and executives, as opposed to relatively weak non-executives? Do boards not challenge enough as a result of this?

Laurie Fitzjohn-Sykes: Part of it is challenge. Part of it is clearly that executives could be making the case for more investment, but equally the non-execs could as well. One issue that I would like to move on to later on is that it is hard as an executive to challenge if you owe your position to the chairman and your peers, because the nomination process is internal to the board, and therefore all your information is in effect sanitised by the executive. It is then hard to be a really true, effective challenge on the board if those two things are in place. Therefore, we believe you need to make the nomination process more independent and try to increase the alternative sources of information to the directors, one means of which could be a stakeholder panel.

Q266 **Chair:** That is certainly a thing we would like to explore if we can. Edward, what is your take? Is there a problem, or is that the wrong way to look at it?

Edward Speed: There is definitely an issue with governance, because there is a breakdown of trust between society and business. We need to address that, and I agree with my fellow panellists that companies should represent the society in which they are grounded. Whilst there have been huge strides, and initiatives such as the various government-inspired reviews and the work that you are doing have helped to prompt that increase in diversity across the boardrooms of the UK, the job is not done. We, as search firms, are at the frontline of trying to engage with the candidate population to encourage them to go on boards, but also to convince chairs of companies that they should look more widely afield for their potential directors.

Q267 **Chair:** Thank you. Denise, I come back to you but, again, this is open to everybody. I am really interested in any correlation between diversity and company performance. I was really interested in what you were saying in terms of gender, thought, background and that there is some degree of groupthink. Is there a correlation in that where you have diverse boards where there is challenge, you get improved company performance?

Denise Wilson: It is very difficult to prove it is causal and say directly that one relates to the other. From the Review perspective, we have never done that. However, there is now a growing amount of research out there. McKinsey have a report on gender parity; Credit Suisse put a report out there showing share price performance improvement over the years. The research is much more credible as time goes by, because there is more of a history there, and you can track that.

Personally, it is not a place we have gone, because it is very difficult to prove cause. However, we do know that in our discussions with board chairmen and with boards, of the 152 all-male boards in 2010, I have not had a chairman—and we talk to many all of the time—say they would go back to an all-male board. They said the atmosphere, dynamics and decision-making processes in the boardroom were better than when it was all males. Yet in 2010, I would say around a third of FTSE 100 chairmen were saying, "Women will not make it; women do not have the skills; they are not quick."

Rowena Ironside: The research now does show quite a strong relationship between diversity and financial performance, and performance more generally. We now have a better understanding behind that as well, thanks to McKinsey and others. Diversity improves not only your financial performance but your talent attraction and retention; it improves your understanding of your customers; it improves your employee satisfaction.

There is also a very interesting area of research—and Google has done some stuff here—around how diverse teams perform better. They have looked at huge amounts of data on what it is that really makes a top performing team. Some of the factors in there, around things like conversational turn-taking and empathy, again link into other research that says putting the smartest bunch of people together does not make the best-performing team. You need diversity.

Tom Shropshire: I have just a couple of comments. If you look at a lot of what companies are saying these days, some of the most innovative companies have called out their own diversity as the backbone to their innovation. If you think about what is going to drive business—it has done for years but it is just a different type—it is innovation. If you think about where you need to innovate in order to grow, that is a broader range of markets, both geographic as well as product. You have to have people who are familiar with those markets. It just cannot be right that they come from the same pool that has been running business for a very long time.

It goes to competitive talent as well. Picking up on a point that Rowena said, if you do say you need to have diverse teams in order to develop better results, you need to have managers who are capable of managing those people in those teams. Therefore, the chances are that those managers, going right up through the organisation, have to be people who are familiar with diversity and managing that to get the best results. To think that again comes from a small pool of people, I just do not think can be right.

Laurie Fitzjohn-Sykes: Just picking up on Denise's point about proving causality, it is interesting to note that the academic literature struggles to often find causality between many aspects of what we deem to be good corporate governance and performance, diversity perhaps being the exception, where the evidence is the strongest. I would say while, yes, it is hard to prove causality, the context is that it is hard to prove causality for most aspects of corporate governance, because it is so complex. Diversity is where the link is strongest, which makes the case even stronger.

Q268 **Richard Fuller:** On the issue of diversity—notwithstanding Laurie's comments about other things being important to look at—we all think it is a good idea and we all think we are making progress. Should we just hug each other and sing "Kumbaya" and let the natural processes make the changes we want to make?

Rowena Ironside: No. Clearly, if natural processes were going to do it for us, we would be a long way ahead of where we are now, if you look at the length of time since women have been graduating on par or better than men.

Q269 **Richard Fuller:** That is if you expect progress to be a straight line. My experience in many cases is that, if you hit a crunch point, then suddenly you get take-off and there is substantial change. Has it not been the case that in the last few years there has been a significant change in the representation of women on boards? Therefore, it is working; should we move on to look at something else now?

Denise Wilson: I would say in the last five years we have seen pretty much a revolution in British boardrooms compared with where we were. In the two decades prior to 2010, the percentage of women on FTSE boards was between 10% and 12%, and it had not moved in two decades. We have now seen over 550 women appointed to FTSE 100 boards in five years.

Q270 **Richard Fuller:** What made it change?

Denise Wilson: The focus, the Review, the attention from Government, the calling leaders out, the showcasing of best practice and the naming and shaming of those that were not. Targets have worked for us; the voluntary regime has worked for us.

Q271 **Richard Fuller:** Targets are like quotas, are they?

Denise Wilson: No, targets are different from quotas. Quotas are generally legislative and government-imposed, whereas targets are voluntary.

Q272 **Richard Fuller:** You shame people if they do not hit a target, and that makes it different from a quota, which you legislate for.

Denise Wilson: No. We had a collective target for all of business. Chairmen, search firms, investors and businesses that were interested in developing women and different talent all got together. Arguably, I would say the UK's approach has been one of the most sophisticated of any country, and that has worked. The press as well has worked, and government support has worked, in order to keep the profile high on this issue and encourage greater diversity.

Q273 **Richard Fuller:** For many years, people like Rowena have been working hard, when it was stuck at 10%, saying, "Look, we really should do something about this." Have we reached a cultural point where people say, "Yes, this is kind of dumb. There are plenty of talented women out there. Let us just do something about it"? We all got to that point and we felt this was the right thing to do.

Rowena Ironside: No, I think that progress really is linked to the targets and data transparency. The thing about targets, if they are internally set, is that you are talking about enlightened self-interest, and that creates much more sustainable change than quotas, which typically come in from the outside.

Q274 **Richard Fuller:** That is useful to hear. Progress has been made on women on boards, but if you look at the representation of people from different ethnic origins, charities are better than the public sector. The public sector is appalling in having people from black and ethnic minority backgrounds. Do we need targets and naming and shaming, Tom, in order to implement the Parker Review recommendations?

Tom Shropshire: Rather than "naming and shaming", I would use "transparency". Part of it is giving transparency about what companies are doing in order to live up to their expectations across a whole stakeholder universe. Setting targets, if you will, can be helpful. In the Parker Review, we have set a target to get the conversation going, at least to the boardroom. There is other work that is going through the pipeline. Targets are clear and allow companies to—more importantly for me—do things that cause those targets to be met. That is the more important thing: getting companies to think about and deconstruct how they conduct business, and change that in order to achieve the end that has been set in front of them.

That is how companies work. They tend to think that way. They tend to talk about effectiveness and put in place policies, procedures and frameworks. That then gives something for the board and executives to measure against and achieve. Those things are helpful. Sometimes, though, you need something to break a little bit of a logjam, and sometimes it is the cultural coming together with the business imperative: the enlightened self-interest. Sometimes those things come together; at other times, they do not. Where you are can only be judged in hindsight once you have made that decision.

Q275 **Richard Fuller:** I agree with that, but there is another issue, is there not? In the Parker Review, you looked at the number of boards. I do not know what your ethnic groupings were, but there were something like 90 directors.

Tom Shropshire: At the time, we looked at a 1,087-director universe. Roughly speaking, about 90 of those were of ethnic minority background, essentially meaning non-white. If you look at that and pierce it even further, 40% of those were within seven companies.

Q276 **Richard Fuller:** Two were South American mining companies listed on the London stock market, so it does not really count. Why did you include them? Why did you not call that out? The actual number for people in this country who want an opportunity to say, "There are people like me on boards"—who have grown up in England and got to that position—was significantly lower than even the very low number that your report showed.

Tom Shropshire: We have that number. That is the second number in the report, which talks about 1.5%, or 16 people, being British-national non-white directors.

Q277 **Richard Fuller:** Sixteen people out of a population of 65 million.

Tom Shropshire: Yes, and 1,100—roughly—board directors. Tiny.

Q278 **Richard Fuller:** As you look to try to make the progress with the Parker Review that has been made recently with female representation on boards, are there differences, because there is a smaller talent pool and it is a much lower target you are aiming for? What would you say might be additional challenges for ethnic minority representation on boards?

Tom Shropshire: One thing to understand in the context of the Parker Review is that the FTSE 100 and 250—but mainly the 100—are global companies. The way that we framed our recommendation was essentially looking at diversity, not defining it by saying you had to be British in order to satisfy the recommendations. It was saying that they needed to look at diversity across their important stakeholders.

Just for argument's sake, using an example, if your headquarters are in the UK but most of your operations are in China, it may not make sense to have someone who is black on the board—maybe it does; maybe it does not—or equally someone who is Chinese or otherwise. That is how the recommendations were framed.

However, a big point going to why we called out the 1.5% is that if you look at the UK, it is an infinitesimally small number of people given the universe and given the available candidate pool. From an ethnic diversity perspective, there are a few things. One, there is an issue around identifying potential candidates. Executive search firms have issues in terms of retaining data over periods of time, which can present challenges. There is an issue around the pipeline in terms of the opportunities that people are afforded as they progress through their careers to become board-ready.

What we are not saying is that you should be appointing people just because of the colour of their skin; they need to be board-ready. However, that is a process that starts very early on. There are big changes there that were issues for gender, but if you talk about numbers and the percentage of the population, they are very different. If you look at the concentration of people of ethnic minority backgrounds, they tend to be in particular industries, and tend to be in professional services, which from a historical perspective is not where boards necessarily draw from.

There is an issue around getting people from ethnic minority backgrounds into mainstream business careers, but also the boards being open, going to diversity, to drawing from a wider talent pool. The issues are the same, but I would say they are exacerbated in key areas in terms of the talent pool, the pipeline, and then preparedness—not in the quality of the candidates, but in that it is even more important to make sure they are focused on the pipeline of getting people ready.

Q279 **Richard Fuller:** I should just mention, for the purposes of the Register of Members' Interests, that I am a director of two private companies. Can I just pass it to Edward on the issue of talent pool? Should we cast Spencer Stuart and executive recruitment or search firms as part of the problem, in that you have not historically built and identified a talent pool, and pressured boards to make change? Or are you part of the solution, in that you are the people pressuring boards that they ought to be looking to bring in more talent?

Edward Speed: I would like to think that we are part of the solution. I do not represent all my colleagues in the profession, but we have signed a voluntary code, and the voluntary code does prescribe certain percentages of diversity candidates on our long list when we are talking to our clients about board appointments. We have also—and this was prompted by the Davies Review and other reviews—looked at the intrinsics of a non-executive director. When we are looking at people who are outside of the commercial sphere, who have not necessarily come up through business, what is it about being a non-executive director that we can then gauge in what they have done?

We are looking at people who have run hospitals, people who have run universities and people who have run major Government Departments. We have five criteria, with interview questions, and we use that data then to convince chairs that a person they might not normally consider is somebody that has the intrinsics required to be a good board director.

Q280 **Richard Fuller:** Can I probe you a little on that? I have no idea if someone who runs a hospital would be any good in a corporate board or vice versa. The people who run those things would likely go to the same schools, same universities and have the same advantages. You are broadening the pool and not broadening the pool at the same time. What about someone who has been a cleaner in a hospital for 30 years? What are you doing to make them board-ready?

Edward Speed: You then get on to the whole question of training.

Q281 **Richard Fuller:** My question was: what are you doing? You talked about chief executives, and my concern is that one of the issues that the Prime Minister is trying to get at is that there ought to be more diversity on boards. Part of that, I am sure she also means, is people from different backgrounds. Maybe the difference between chief executive and a cleaner is too wide a difference, but there is a point there, is there not? We are drawing people from the same backgrounds, the same education. In the code of conduct you have signed and in the work that Spencer Stuart is doing, are you going out beyond that pool?

Edward Speed: We will certainly challenge chairs of boards to look at younger individuals and individuals who are not necessarily chief executives, whether or not they have all been to the same schools.

Q282 **Richard Fuller:** That is not quite answering the question, Edward, is it? Executive search firms like Spencer Stuart do a fantastic job; I have no problem with that. However, the challenge now is different. The challenge is that there is a framework being considered for people who should be in the governance of our major corporations that does not necessarily look for the things that we have historically looked for. What means someone is board-ready needs to change. That is the extent of the challenge in the Government's review. You may end up with what might, from where we sit today, look to be very odd future appointments to the boards. We will be talking probably about employee directors, not that that is odd; John Lewis do a very good job of that, and other companies as well.

On the frame of reference in executive search firms for non-executive directors, you in your opening said that you have signed a code of conduct and look out for new boards and this, that and the other. Are you prepared to look at a completely different frame of reference? Is there any demand from your clients—the companies—to say that, "We have heard what the Prime Minister is saying. Now let's look for completely different types of people"?

Edward Speed: That is the point. Is there the demand from our clients? We have to respond to our clients' needs. They are not saying that they want the cleaner from a hospital. They are saying, "We are prepared, Edward, to consider the person who has run this trust, because you have gone through the criteria and you have convinced us that they will make good board directors, and they have got a certain level of financial literacy," which is important, as you know, as a board director yourself. I thought the green paper was talking about stakeholder advisory boards. We need to take our guidance from the Government and from you all about how broad you want the inclusion on boards and how that is manifested.

Denise Wilson: Part of the solution goes back to business and educating business. People of all types, walks and backgrounds enter the workplace. A very big part of the problem we have is in the selection of who gets promoted, who moves up through the ranks, who gets the trading and who goes into what team. That starts way down in the workplace, at team-leader and middle-management level. That is where we have got the big issues, and that is where we have to look very clearly at unconscious bias.

That is where we have to have data that shows in business who is getting promoted: what backgrounds are they from, what educational backgrounds, what race, what gender? We have to make sure that we have a level playing field. Beauty is in the eye of the beholder, and we are finding that a very big barrier to people of all types and backgrounds coming up through the layers.

Q283 **Richard Fuller:** I am very glad that you mentioned that, because we are looking at corporate governance, which is one level. Should we really be looking at the executive people—the people who are being chosen to be the head of sales, the marketing chief, the head of legal affairs? Is the Government missing the point here that perhaps we have reached this "Kumbaya" point—I know you do not agree with me on that—where we are all generally aware there is a cultural position that we are now going to make those changes, although it may not come as a quickly as we want and we do need to have targets? The real debate now ought to be, why are we not doing enough to monitor, to set targets, to name and shame at the senior executive levels or the lead-up to the executive levels?

Laurie Fitzjohn-Sykes: I would add one thing. It is a key point you make in terms of the balance of expertise versus diversity. We found this when we looked at employees on boards. Often the strongest pushback is that they do not have the expertise operating at executive level to really be effective on a board. However, we found talking to people who had been on boards with employees that an employee representative perhaps does not have the senior executive experience but has a diversity of viewpoint and asks the different questions.

In a group of 10 people, often an oblique question that can prompt discussion is of value. There is a slight difference between that and ability to operate at an executive level. There is perhaps a mind-set shift; we do not need a whole board to have executive experience, because someone with a totally different perspective who does not have that executive background can enhance the overall quality of decisions of the board.

Tom Shropshire: Just to pick up on your point, outside slightly of the Parker Review, if we really want to make a change in terms of how British business does business and looks, it is about really looking right the way through the organisation. There are a lot of different incentives and disincentives at play within companies about taking risks and what they get rewarded for, the people that they are willing to invest in, and the areas and so on. If we are really talking about making a change that will have the benefit over time of trickling up and making a change, in addition to what one is doing at the board level, one has to look at how one builds incentives. I use that in a broad way: incentives for the board and executive management to make changes throughout the organisations.

What we do not see enough is people sharing the ideas and the information that they receive while they make those changes, and companies picking that up and running with it. I sense that there is a bit of reluctance in companies to make some of those changes, because they are not sure whether they feel confident enough that it is going to ultimately result in the return to the stakeholders to whom they answer. Therefore, they are these incentives. If you really want to make change, it is not just at the top; it is the way it filters through the organisation.

Q284 **Richard Fuller:** Looking at your résumé and where you are educated, I am guessing you are from North America.

Tom Shropshire: I am, yes.

Q285 **Richard Fuller:** But you chose to pursue your career in the United Kingdom.

Tom Shropshire: Yes, and I am a citizen; I have dual citizenship.

Q286 **Richard Fuller:** Was there any particular reason, from the point of view of the issues we are talking about today, why you came to the UK?

Tom Shropshire: Maybe fundamental issues—I saw London as a fantastic place to start a career. I have always been internationally minded, and I wanted to start in London because it afforded me the opportunities to do what I do, which is be a US lawyer sitting in London dealing with people around the world. That is probably why I feel so strongly about the benefits of diversity, because I see that every day in how I do my job.

Q287 **Richard Fuller:** Did you ever face discrimination yourself?

Tom Shropshire: It is interesting. I would say I was more discriminated against for being an American than I ever was for being black. That being said, discrimination has been a factor in my career, but at the same time I have never let it be a limiter. If I look at the legal profession, especially in the City, I could probably count the number of black partners—maybe I would get to the end of two hands and maybe I would get to my toes. There are not that many, and that to me says that there is an institutional issue around getting people of colour into professional services.

Some professional services are better; accountants are better. But if you look at business, still, at the top ranks, we are talking about four CEOs and chairs. I do not want to say that it is necessarily a product of discrimination per se, because that is always very hard and personal. However, I do say the facts alone suggest that something is not working right, and therefore those things need to be addressed.

Q288 **Richard Fuller:** Just for the record, I am very glad that you are here and that you think so highly of London. Bedford, by the way, is even better than London, and I would encourage you to visit often. My final question if I may, Chair, is on the same point to Rowena. Is it not the case still for women in executive roles that they face daily discriminatory practices in the workplace, and that in itself is an inhibition to their making progress?

Rowena Ironside: Yes. We have not yet really understood that talent decisions need to be much more evidence-based than they have been historically. You can see medicine, where it used to be eminence-based decision-making, is now moving to evidence-based talent. Everyone thinks they know what a good next promotion or employee looks like. When you look at that, have they really taken the evidence?

There are lots of myths about merit, with people assuming that it is an objective standard when it is subjective and hugely self-referential. We need to get that stuff out on the table, and the Hampton/Alexander Review has done a great job of being quite explicit about some of the things that firms can do in the pipeline to make things work better for any minority, which includes women and people of colour.

Tom Shropshire: I do think there is this point—and you see it in professional services—whereby when people come up and are the same, they will select the same. It is people who are willing to bring in difference that cause that system to change.

Denise Wilson: The barriers facing women are complex and compounding. We have seen that over the last five years. However, the very good news for the UK is that because we have had a voluntary regime, we have had to go around to persuade people that this is the right thing to do and get folks on board. We have had to look very hard and very deeply at what is going on in business, unlike many other quota countries, which have just had to fill the slots. We do have now a very good understanding of issues in the workplace, and we are working hard on the Review on a very inclusive basis with all of business to address that.

Q289 **Chris White:** Just to continue with Richard's questions, who do you think is responsible for the diversity on a board? Is it the chair, the chief executive, shareholders or the nominations committee?

Edward Speed: If I may, it is the chair working with the nominations committee. That is definitely the responsibility within the boardroom.

Laurie Fitzjohn-Sykes: Currently it is the chair's decision with the nominations committee.

Denise Wilson: Yes, I think so, but generally they are board appointments, so the board need to agree who is coming on. The board also have a responsibility, but it tends to be the nominations committee who will do the selection in the first place and then put that candidate up for the board to approve.

What we have seen very much is that for those boards that have moved far and fast, it has been about the attitude and approach of the chairmen. We have many zeroes to heroes who two or three years ago had no women on their boards, and now have 30% to 40%. The difference between those, and those who have put one woman on their board and are sticking, is whether or not the chairman gets it. When the chairman gets it, things can and do move very fast.

Tom Shropshire: I would agree with that, yes.

Q290 **Chris White:** You mentioned nominations committees. How do these work? How do you understand these to work?

Edward Speed: They are normally chaired by the chair of the company. They are responsible for four things, including board succession. Most enlightened chairs have a succession plan. They have a grid that links the skills they need around the board table to the long-term purpose and the strategy of a company. Because we have term limits in our code, they can work out when people will be rotating off or when people should be rotated off early, if that is the case.

Secondly, the nominations committee is responsible for the pipeline of talent in the executive ranks, and they should request to have exposure to the top talent coming up through the company. Some do it very well; some do it less well. We spend a lot of time advising clients on that. Thirdly, the nominations committee is responsible for board evaluation, and that is a point that this Committee should spend a bit of time on: the importance of evaluating the effectiveness of boards. You should not just do that yourselves. The code requires every three years for there to be an externally facilitated board effectiveness review, and that, if well done, can highlight all sorts of issues relating to groupthink, to diversity of thinking, and to having much broader involvement.

By the way, I do think that there should be some sort of FRC or oversight of external board evaluators to ensure that there is a minimum standard, so that these are well and properly conducted. Fourthly, the nominations committee has an overall remit around governance, and has to report to shareholders and the wider stakeholder community about quality of governance.

Q291 **Chris White:** Thank you. Is that a comprehensive answer, or does anybody have a different view? This is a very Christmassy, easy, relaxed panel this morning, Chair. It all seems very straightforward, but how do you make sure, for example, that if you have a very dominant chair, the board is not going to just fall into line? On so many occasions we have found that the problems result from having somebody who has a powerful personality. How do you prevent that from happening?

Edward Speed: The one thing that I have not seen in the literature of your other meetings is that much reference to the senior independent director. The senior independent director on boards really does play a very important role, in a way counteracting an over-powerful chairman.

Q292 **Chris White:** How do you identify that person?

Edward Speed: That person is named and is listed on all the company websites and company literature. You know if you are a shareholder and you have a problem or a potential problem—

Q293 **Chris White:** It is all very well to be listed, but how do you ensure an independence of purpose? How do you have that personality or character?

Edward Speed: The other board directors will nominate that individual from among themselves to be the senior independent director.

Q294 **Chris White:** Do you think there is a danger of it being a sort of perpetual motion machine? Are they creating somebody who will challenge them? How does that work?

Edward Speed: In some companies, the senior independent director is there because of their seniority. However, in many cases it is because of their independence of thought, the courage of their convictions, and the fact that they are usually one of the stroppiest board directors.

Q295 **Chris White:** Have you ever been nominated for this position?

Edward Speed: I chair a board, and I have three stroppy board directors. I am really glad that I have them; they are very important.

Laurie Fitzjohn-Sykes: Your point is exactly right, and highlights the issue that it is essentially a circular self-appointment. While it obviously works well in many boards, the issue is that it is slightly the board appointing itself, and that is the benefit of having some outside, independent nomination process with shareholder nominations committees.

One of the main pushbacks we get against that when we talk about shareholder-led nominations committees is that the chairmen often talk about it being, "My board, and I appoint my board." There is that mind-set in the UK; the chairmen think it is their responsibility to put the people in place. Slightly creating some independence to that could help get away from the slightly circular closed loop that we currently have. That has an important link to diversity, because it is hard to have challenge and diversity if you have got a group that appoints itself.

Q296 **Chris White:** To break the circle.

Laurie Fitzjohn-Sykes: To break the circle, not only in terms of getting other people in but in terms of giving the directors a mandate to challenge effectively. It is hard to challenge effectively if you owe your position to your peers and the chairman.

Edward Speed: Shareholders do have to vote those directors in, although I did see in one of your earlier discussions where the shareholder should have a choice.

Laurie Fitzjohn-Sykes: The votes are largely process. They hardly ever bind. One of the issues with our current governance process is that the channels of influence for shareholders are very weak through governance structures. Therefore, the primary influence of shareholders on the company is via the share price trading and the influence of the share price on long-term incentive schemes. That is one of the key issues we want to shift. The influence should be via the governance channels so it is long-term shareholders.

Q297 **Chris White:** You jumped quickly into this. Do you think that Edward is talking about effectively a rubber-stamping exercise in terms of shareholders having a say in who is on the board?

Laurie Fitzjohn-Sykes: There has been an improvement in engagement, and chairmen spend more time meeting the larger shareholders. The stewardship code has had some effect, so we have made progress in this regard, but we could go much further. People are trying to make change, but in reality the governance structures are not set up that way, and so it makes it hard.

Rowena Ironside: Can I add something less about the process and the external factors? Why is it, even with a group of good people in a boardroom, things still go wrong? A lot of it comes right back to some fairly basic human things around groupthink, around how difficult people find it when they are in a room of peers, even if they are not worried about reappointment, to challenge, and the way that diversity does tend to improve that. Diversity is the grit in the oyster.

Q298 **Chris White:** Could you explain that? Is it by definition you think that is the case?

Rowena Ironside: There are great quotes in the research around how it makes people work harder, because if you walk into a room and you know everyone is roughly on the same page, you are less well prepared than if you walk into a room and you know that people are going to be bringing other opinions in.

Chair: It is true of this Committee.

Rowena Ironside: Yes. There is now research around that.

Q299 **Chris White:** How do you balance this potential conflict between a shared strategic vision and the need to question and challenge?

Tom Shropshire: One of the things that oftentimes helps with that is radical transparency on the way in and on the way out: what a board is looking for; the basis on which it has made its determinations about who is a director and why; the expectations that they have and communications around that to shareholders and other constituencies; and transparency to those other constituencies without expressing a view as to whether they should be on the board or off.

There can be a whole lot of benefit to making sure those channels of communication are kept open and live. To me, once you start to engage more broadly outside of that particular boardroom, the way you engage in that boardroom changes, and the people you bring and their experiences also change. To me, transparency is the real key to getting effective boardroom dynamics. Some of those can be legislated for, and some of those have to be just through interpersonal dynamics.

Q300 **Chris White:** Tell me what you think about legislating for greater transparency. I am sure everybody would say they are transparent and this is the direction they want to follow.

Tom Shropshire: It depends a little on what aspect you want to make transparent. Just picking up on your example of nominations committees, what are the criteria that go forward for the board to consider in terms of terms of particular candidates? There are always, for example, terms of reference that are drawn up for the particular type of skill-set that a board is looking for. That is the sort of thing that can be productive to engage in with other stakeholder bodies before that goes out, getting people's points of view and assessment when it comes back in.

That does not necessarily mean that everybody in the world needs to know, but there can be levels of transparency, for example, which then also bring expectation. Just taking a narrow example of being able to share terms of reference, getting points of view, getting the candidates reporting on how internally or externally those stacked up, the considerations that the board went into—not in 50 pages of detail, but a number of bullet points—can create the transparency necessary for engagement. That is just a small example.

Denise Wilson: On the attributes of the individuals who sit around the board table, whether they are debating a new board appointment, the strategic direction of the company or signing off the annual report and accounts, the authenticity and the boldness, almost, of each individual director to know that they are valued, their views are respected and they have a point is a very important attribute for candidates.

If the chairman or the chief executive is overly dominant on that board, that can tend to break that down; it does not happen very well. However, with increased diversity, you get people who are not of a certain type or group, or pals outside of work, or from the same school or background; you get people who come in and sit as independent individuals who are competent in their field and comfortable in their own skin. That is when it works.

Laurie Fitzjohn-Sykes: Another aspect in terms of the ability to challenge and bring a diverse viewpoint is the information set they have available and the time and resources they have. Currently, most information comes through the executives. There is some means to broaden that—a stakeholder advisory panel or an office of the NEDs such as BP operates—to try to create a separate function that provides information to directors. The time they dedicate to a company could be part of that, because if you have very little time, it is probably hard to do the reading and research to give you the confidence to challenge.

We have increased to around 30 days' average commitment. Surveys show they would like to spend 40 days. Private equity companies spend 50 days, in terms of how much time you could spend as a non-exec director. If you have spent more time walking the business, that gives you more confidence in the boardroom to say, "I was visiting our plant in such-and-such, and that was not the case." Therefore, the information set is a key part of the ability to challenge the executives.

Q301 **Michelle Thomson:** Sorry I was a little late; I was at an APPG breakfast on corporate governance. I am interested in exploring all this just a little more. To what extent currently do you think there is an understanding of cognitive diversity? Why does it matter? How, ultimately, could it either potentially inhibit or enhance performance?

Rowena Ironside: Most board chairs would say they are looking at cognitive diversity.

Q302 **Michelle Thomson:** Do they understand what that means?

Rowena Ironside: Exactly. It is a little like merit. It is no good having lots of cognitive diversity if you do not have the soft skills around conversational turn-taking, which is one of these things linked to the psychological safety of a group that makes it effective. When you look at the skills directors need to have, I split them into wisdom, which is breadth and antennae, expertise, which is professional skills, and then interpersonal skills—harder to evidence, less discussed, but equally important. That is what helps to bring it together.

Tom Shropshire: From my perspective, the concept of cognitive diversity is interesting. Even within that, people have different priorities as to what they think contributes to someone's cognitive diversity. Certainly in some of the comments that we have got, people question how your race and ethnicity contribute to your cognitive diversity. In some respects, I am not overstating by saying it defines everything that I am. However, at the same time, it does not define every thought that I have. It is one of those sorts of things where, even within cognitive diversity, boards and chairs really need to think hard about the people they are putting in place, and think about the breadth of experience they have both in business and outside of it, and what they bring to the table in totality.

Denise Wilson: I agree. It is really important, but it is one of many factors that are important. It is part of a mix. I would not put it out on its own.

Laurie Fitzjohn-Sykes: I agree; it is critical. It is part of the benefit of encouraging diversity in all its forms and trying to bring that diversity of viewpoints to the board. As I have mentioned, we often hear from chairmen and board members we talk to that it is about the ability to have a diverse viewpoint but also not be too aggressive. You need to have that diverse viewpoint, but how you present that in the boardroom is critical to creating a good discussion.

However, as you say, it is very hard to measure. What is cognitive diversity? You can say you want it, but how do you implement it? A key part must be greater diversity of backgrounds, in terms of outside of listed companies: maybe civil society, maybe hospitals. Maybe we need to be thinking a little broader about what experience is relevant to a board.

Edward Speed: Maybe I should just quickly summarise what we look for in NEDs, and cognitive diversity is definitely in there. I have mentioned financial literacy. It does not mean you have to have run a P&L before; you can have run a very big budget or had some facility with numbers. That is important. You need to have the intellect to get up to speed quickly in that organisation's way of working, the business model. You need to have the interpersonal skills, and Rowena said it very well. You need to be able to read what is going on around the table—what is not being said as much as what is being said.

You need to know how to make your contributions effectively. That is really key. We all know people on boards who are one-trick ponies and go on and on about the same thing. You need people who have got real independence and courage of convictions. I have talked about that before; that is really key. Are they going to be like Henry Fonda in that amazing film, *12 Angry Men*, who manages to turn the whole jury round to his point of view? Do they really stand up for their convictions?

They must have integrity; they have got to be absolutely squeaky clean in terms of understanding where the line is, and what is grey, black and white. Finally, to Laurie's point, they need to have that inclination to engage. We think that a lot of the short-termism that is inherent in all our corporations is a lot to do with people just not having enough time to understand their businesses, to devote their time, to take a long-term perspective, to understand the overriding purpose. If the board is not the body that holds on to a longer term purpose, no other group within the company is going to do that.

Q303 **Michelle Thomson:** There is a lot to cover here. Picking up on a couple of words I was hearing earlier, I think it was Laurie who mentioned values. You were talking at the beginning of this discussion about having worker representation on boards, and I think you made the point that they would be the ones to bring out something related to values, because they may not necessarily get the complexity of the discussion. I am interested in how, going back to your point about groupthink, you really embed values in a board. How far are we down the track on that as compared with groupthink? Do you really see cohesive behaviour in terms of values, and therefore representing that wider stakeholder piece that we talk about in corporate governance generally?

Laurie Fitzjohn-Sykes: Tomorrow's Company has done a lot of work on values and the importance of culture in terms of business success. There has been a lot of progress on acknowledging the importance of having a set of values that are embedded throughout the whole organisation and the importance of having culture. There has been a lot of progress in that regard. There is clearly a lot further to go; too often there is more talk than action.

We often find the best examples are private companies, because to really create a set of values that filter down through the organisation, you need a consistency of action over a long period of time. That simply is not possible in a listed company structure. That is one of the battles we have: we cannot replicate the long-termism in listed companies, but how can we still create that consistency of values that lasts through time and is not just a three-year fad that comes and goes?

Rowena Ironside: Although it is the bad news that makes the press, in the vast majority of cases boards and companies are operating at a very high standard, and so we do get rather overexposed to some of the failures.

Q304 **Chair:** We have heard that ethnic and gender diversity, Rowena, is still really quite lacking. Is it working well despite the lack of diversity?

Rowena Ironside: I do not think there is evidence to say that the values in the boardroom are not where they should be in most cases. I do think most people are doing a good job. However, I would also say there is a moving moral boundary around many issues, and that can sometimes be difficult for boards to negotiate.

Laurie Fitzjohn-Sykes: No one in boardrooms intentionally sees themselves as bad. The issue is when you have a bubble. Often we talk to executives and everyone wants to do the right thing, but what that translates into is determined by the people you talk to in your peer group. This is why breaking that bubble of the business elite is so important.

Q305 **Michelle Thomson:** I suppose it is about a diversity of behaviours, and how you get to that. Edward, can I pick up on something that interests me? You mentioned a couple of times about the need to fundamentally understand the numbers, even if a candidate is not fully accountancy-trained. Do you then see some value, for example, in a banking board bringing in somebody who is a creative from one of those sectors? The sorts of questions they are going to be asking are absolutely not steeped in banking tradition.

You mentioned hospitals and running a trust, but obviously by doing that, they are always going to be looking at the bottom line, because that does drive a lot of things. I suppose I am trying to understand how far you would push it to get somebody who really has such a completely different outlook. I am thinking about an example of a creative: Darcey Bussell, for example, thinking about *Strictly Come Dancing*.

Edward Speed: The financial crisis is not that far away, and to start putting creatives on our big bank boards would not be a great idea right now. I admit that in other areas, yes, there should be greater creativity. However, frankly, not all of our big banks are through the woods, and I would prefer to have people who understand banking.

Q306 **Michelle Thomson:** We had people who understood banking, and look where that got us.

Chris White: Some of them were quite creative.

Michelle Thomson: Possibly too much so.

Edward Speed: I would say that in our banking boards we should have individuals who really do understand banking and have a good knowledge of how the world of finance works, because we are still not out of the woods in my view.

Denise Wilson: I agree in part, but I would put that slightly differently. You have to have people on the board who are capable of understanding banking and the banking business. They absolutely need to be financially literate. I do not think they need to be bankers per se or financial experts who are steeped in it. Banks have huge boards; banks have boards of 15 or 20 people. Is there space for one, two or three people who do not come from that background? Absolutely, there is.

It is dangerous just to bring one in, because the risk is you create a two-tier board where the conversation happens at the dinner the night before and there is not proper respect. You need more than one, but I absolutely think—on all boards, irrespective of discipline—that there is value in having somebody who comes from a very different background, providing they have the intellectual capacity and ability, and some financial literacy.

Q307 **Chris White:** What about other sectors such as retail?

Edward Speed: On other sectors, I would agree.

Q308 **Chris White:** Does your logic apply to them as well—that they need to know about manufacturing, and they need to know about retail?

Edward Speed: No. For me, it is just banks, given what they went through. If you look at the composition of the boards of some of the banks that failed, you would see that they were not necessarily all paying attention and capable.

Q309 **Chris White:** Do we go back to the beginning of this discussion, where it is people who went to the same school, who are mates, and there is insufficient diversity? Are those the more important things that you should look for, rather than just having a qualification in and understanding of finance?

Edward Speed: If you are referring, Chris, to the world of our big banks that are too big to fail and all that, then, sure, we should have diversity of thinking, but within the context of understanding, as Denise said, how banks work and the world of finance.

Q310 **Chris White:** The diversity of thinking sounds very thin indeed. Does that diversity of thinking exclude females? Does it exclude ethnic minorities? What about those diversities?

Edward Speed: Yes, absolutely. [Turning to Tom Shropshire, member of the Parker Review] A member of your committee, Ken Olisa, is a former banker.

Tom Shropshire: Yes, that is right. The way I think about it is: in any committee you are part of, you have to bring something to the table. You probably have to have some core skill-set that allows you to bring some skill to the table, and that probably has some commonality around some basic level of financial literacy, just because that is the nature of what directors do. However, at the same time, you will probably need to have some familiarity with operations, you will need to understand employees, and you will need to bring those skill-sets to the table. They do not all need to be honed to 100%, but they need to be there.

The big thing that one needs to bring to the table is a willingness to dive in and get to know that company, and the capacity to do so. One also needs to bring all the other skills that come in, and that to me is where diversity comes in. Again, each of us comes to the table bringing a different skill-set, and it is really important—going to the point of the chair, the SID, to make sure those are extracted and understood, and where to pull those into conversations and create an environment where people can add that value. To me, that is where the real skill of a really strong chair comes in.

Q311 **Michelle Thomson:** Just a last question about this, then, in terms of the wider societal link, ensuring that that awareness at all times is embedded in boards. That goes back to the banking example, which we have seen did not work terribly well. How do we get the composition and the diversity that ensures that continues to remain at the forefront? I feel that some of our business is quite disassociated from the wider world; it becomes almost like an end in itself. How do we get that diversity that ensures a link back to society? Business is meant to serve our society, not the other way around, and it sometimes goes a bit wrong. How do we get that right?

Rowena Ironside: I think it is Section 172 that talks about one's responsibilities as a director being to the stakeholders more broadly. That needs to be further discussed, and the public sector also needs to get its act together and have targets for its boards and board transparency. That would be a useful step.

Laurie Fitzjohn-Sykes: Section 172 is legally right, but it has not really had teeth; it is not really enforceable. We think there is a need now to create a mechanism to hold boards to account to their wider duties to stakeholders, as articulated in Section 172. We think that could be done through a stakeholder advisory panel of some sort: a panel that had the mandate to hold the board to account to Section 172 and long-term value creation. That could be given teeth through the ability to make a public statement. You would hope to create a consultative dialogue between the board and the panel. One of the non-exec directors could chair the panel.

However, ultimately, if the panel had the ability to make a public statement, there would be that ultimatum if they somehow had a complete disagreement. It is that sort of mechanism that might help ensure that boards do incorporate the wider view of stakeholders. While Section 172 was a step forward in the legal wording, it has not really had the impact we would have hoped in terms of the actual practice of boards.

Michelle Thomson: That would change behaviours, yes.

Denise Wilson: The Parker Review and the Hampton/Alexander Review—high-profile reviews that are on the back of business, report every year on progress and rank companies on how they are doing—are working. Nobody wants to be at the bottom. When I go to see a chairman, straight away they look to see where they are, and when they are 97, we look back in two or three months' time and things have changed. High-profile government support—from No. 10, the Cabinet

Office, and the Secretary of State—behind those two reviews is really important. Having Ministers out there talking about this, saying that it matters, is really helpful.

Tom Shropshire: In terms of creation of the environment, I do think, obviously, the whole purpose of these exercises is to reinforce that environment. The stakeholders are changing; consumers' expectations are changing; employee expectations are changing; stakeholder sophistication is increasing.

There is definitely a trend, but all of these things shape the boardrooms. I spend a lot of my time talking to boards around the things that are shaping their decision-making, and I can tell you without equivocation they are more complex and there are more things that they are considering than there have ever been before. I do not stand up here and say that all boards do it in the appropriate way, but I do say that it is changing. I do think things like this continue to contribute to that change.

Just speaking for boards for a second—again, not everyone—the boards that we have been to do consider the range of things. Whether somebody thinks they need to think more about X or Y is up for debate, but they also have to retain that business judgment to be able to say, "Actually, on the balance of things, this is what we need to do." That being said, from a diversity perspective, having 53 boards out of the FTSE 100 not having anyone of colour on them suggests to me that, if they thought about their wider stake in society, they might have made some changes already.

Q312 **Chair:** Thank you. This has been a really productive session, and as a Committee we are really grateful. Can I just ask one final question? It is in response to what Edward was saying about external board evaluation, and possibly having somebody outside of the organisation saying, "You have not got the diversity. You are not looking at the long term." How applicable and practical is that? Would boards quite understandably say, "Hang on, this is an internal matter. We are trying to improve." Should there be some sort of oversight compliance body that looks at this properly and formally, or does that just lend itself to a tick-box exercise?

Edward Speed: Yes, the code does require every three years. There ought to be not necessarily another regulatory body but a code of practice for those external facilitators. They should have a professional body to ensure that they really are getting to the heart of the matter and covering the right elements. A lot of internally administered board evaluations are pretty weak, and some of the externally facilitated ones are not that much better. However, they play a very valuable part and should continue to be mandated.

Q313 **Chair:** Laurie, is this what the panel would do?

Laurie Fitzjohn-Sykes: Partly, but it is also partly the role of good, engaged stewardship shareholders. Rather than creating a separate body, you should increase the ability for investors to engage effectively. Boardroom evaluations are currently done through a private process. Importantly, when the evaluator goes in, they need the trust of the board to talk openly with them. That does not work if they then publish it. There are two models: there is a private process, as we currently have, with a trusting relationship; or there is an open, external process, which we do not have, and is the role of shareholders.

Denise Wilson: What would help is better transparency around progress on gender and ethnicity. Strategic gender pay gap reporting will hugely help with that, because that gets gender pay gap right to the top table, and it will be part of the statutory reporting. That all helps. Asking companies to disclose every year where they are on gender, what they are doing, and what progress they have made in the year, is really important. That is part of the external audit and the whole annual report and accounts process, but it needs to be explicit.

Tom Shropshire: I agree on the transparency. I also do think that there is merit to consider the right avenues for engagement of internal stakeholders. It is very hard to have a second-guess oversight role, because the board executives will have a whole host of information available to them, experiential and otherwise, for decision-making. It is incredibly hard to second-guess. That being said, if you get people involved at the point of decision-making, they can probably have better impact. They may not necessarily be able to have oversight but they may have impact and create a record for accountability.

Rowena Ironside: The only thing I would say is that external board evaluations are important to have.

Chair: That has been really helpful. Thank you very much again for your time. Thank you.

Examination of Witnesses

Witnesses: Mick Barker, Frances O'Grady, Tim O'Toole and Nigel Wilson.

Q314 **Chair:** Good morning. Thank you for coming to give evidence. We are very grateful. Just to start with, for the purposes of the record, could you tell us who you are and what organisation you are representing, starting with you, Nigel?

Nigel Wilson: I am Nigel Wilson. I am the Group Chief Executive of Legal & General, and I am also the Chairman of LGIM, the UK's largest fund manager. I am a prominent supporter of corporate governance.

Frances O'Grady: I am Frances O'Grady. I am the General Secretary of the TUC, representing 50-plus unions and around 6 million members.

Mick Barker: Good morning. I am Mick Barker, the Employee Director for FirstGroup.

Tim O'Toole: Good morning. I am Tim O'Toole, the CEO of FirstGroup.

Q315 **Chair:** Thank you. I have asked everybody a general opening question. Is there a problem with corporate governance in the UK and, if there is, in which particular aspects is there a problem? Can I start with you, Nigel? Is that the right way to look at it?

Nigel Wilson: The way to think about corporate governance is we are the world leaders. If you travel around the world—go to Japan, China, America—we are definitely seen as the world leaders, and the firm I represent is probably the leader in that particular area. However, we cannot be complacent about that, and there are vast areas where we can still improve it, because it is a relatively low bar around the rest of the world.

We just happen to be the best at certain things, but we could be a lot better. Some of the issues that we are talking about, particularly around diversity, we are not particularly good at. There is a huge gap between men and women, between different ethnic groups, and there are intergenerational differences in pay etc. across different companies, which need to be resolved. There is a lack of representation in a number of boards around workers, and we at L&G, but also at LGIM, are very concerned with how we get more productive, less hostile engagement with workers.

Q316 **Chair:** That links very nicely into the work of the TUC, Frances, in terms of workers on boards. On that general point, though, is there a problem with corporate governance in this country?

Frances O'Grady: There is a problem with a system that is premised so heavily on shareholder supremacy at a time when the stewardship of the long-term best interests of a company does not sit as easily with shareholders as perhaps some will have argued it did in the past. We would argue that in fact one of the strongest correlations with the long-term success of a company is the interest of working people whose livelihoods depend on it and who face a much greater risk than many shareholders do if things go wrong. We are a strong advocate of workers on boards.

Q317 **Chair:** A major theme of this session will be about workers on boards. Mick and Tim, do you have anything to add in terms of a problem with corporate governance in this country?

Mick Barker: I agree with much of what the two people in front of me have said.

Tim O'Toole: I agree as well; it is a work in progress and always will be.

Q318 **Chair:** Nigel, I was really interested in what you said. Is there anything to be frightened of when it comes to workers on boards?

Nigel Wilson: No. It is how to get the best of the workers' representatives across the group. Many of the larger firms in Britain are very international, and so the UK component of that is often relatively modest. Therefore, you have to remember that it is not a UK-focused issue; it is an international issue for most of the larger companies in Britain.

Q319 **Chair:** Thank you. Frances, what would workers on boards add to the performance of a company?

Frances O'Grady: I hope that members of the Committee will have received the TUC's reports on this that set out the evidence very clearly in respect of the correlation—again, we are clear it is a correlation—between countries that provide for some form of worker representation, remembering that is now the majority in Europe, and positive benefits around greater investment in R and D, more commitment and investment in skills and training, higher employment levels, and a greater focus on broader stakeholder interests, whether that is consumers, the environment or working people. Chair, if you did want me to answer questions about some of those concerns that have been expressed, I would be delighted to.

Q320 **Chair:** Please feel free now—if you want to just highlight them, and then we can maybe explore them.

Frances O'Grady: I am conscious that a number of objections have been raised—for example, that workers on boards would not be compatible with a unitary board structure. Again, our report shows very clearly there are five countries that have workers on boards with a unitary structure. There are many more that offer companies a choice of structure, which again seems perhaps a sensible way forward. On concerns about confidentiality, an Irish survey suggests that there is no greater risk of leaks from the boardroom where workers are present. On the contrary, people reading the financial columns in newspapers will recognise that concerns about confidentiality are not restricted to worker representatives.

On conflict on the board, again, the whole mission of having workers on boards is a constructive engagement. They would not be there as delegates in our view; they would be there sharing the full responsibilities of other directors. However, they would bring a fresh perspective into the boardroom that would keep the board in touch with what is happening on the shop floor. After all, it is the workforce that is making a company a good deal of its money, and it seems sensible to have that connection. I could add a long list to this, and there may be opportunities to come back to them.

In the past, concerns have been expressed that workers would be out of their depth. I suggest that maybe some of those expressing those concerns have not had too much contact with workers, who may feel slightly patronised by those comments. Also, the TUC is very clear that we would be keen to provide a network, training, briefings and support in exactly the way that we do, for example, for pension trustees. I have full confidence in workers being able to make a positive contribution to a board.

Q321 **Chair:** Tim and Mick, that leads quite nicely into how this all works in practice. We are very keen to hear, in terms of the rationale behind putting a worker on the board, how it works in practice and how it improves your company and the decision-making. Tim, to start with, where did this come from? Where did the idea of having a worker on the board at FirstGroup originate?

Tim O'Toole: That, in many ways, is the key question. The reason it works so well for FirstGroup—and I can only speak to that, as opposed to the broader issue—is that it has grown up organically. A worker came on the board because FirstGroup originates in a management buyout of Grampian Regional Transport in Aberdeen. Workers were part of that financial arrangement and so naturally went on the board. Since then, it has just been the natural extension within FirstGroup that as companies were added—different bus companies, and later train companies across the UK—there was always an employee representative on the board.

It is those employee representatives who will elect the plc representatives. It is not a matter of just taking a worker and putting them on a big plc board; it is an organic communication structure within FirstGroup. There is a ready, recognised, and organised way for Mick to get and pass information. There is an infrastructure that supports what otherwise would just be a single person. It works very well for us.

Q322 **Chair:** Mick, what is your perspective on this in terms of it working well?

Mick Barker: It certainly does, in the way that Tim described it. This is ingrained within us. If any company can say, "Our employees are our greatest asset"—and there are many that do—and can add, "We are going to show that by having a frontline person right at the fulcrum of the decision-making and the strategic direction of the company," it means a lot to the employees.

Q323 **Chair:** I am really interested in what role you think you have, Mick. First and foremost, you are a director. Are you seen very much as the workers' representative, and do fellow employees see you as that? What is it that you are there to do? You are there to provide strategic long-term decision making for the company, are you not?

Mick Barker: Yes. As Tim described, there are 15 employee directors in all within the other eight companies that we have. I have a lot to do with those guys on a regular basis. However, from the point of view of how I am seen, I am a non-executive director. I carry out the same function as all the other non-executive directors. I am on there to add a perspective of how employees might feel or think, but I challenge Tim and his management team in exactly the same way as any other non-executive director.

Q324 **Chair:** We heard from Denise in the previous panel about a two-tier board. That is not the case when it comes to FirstGroup. You have access to all the same information; you feel privy to all the decisions made. In fact, you are contributing to those decisions. Is there any sense that there is a two-tier decision-making process?

Mick Barker: There is no sense of that whatsoever. I am in the end of my fifth year now, and there has not been a single occasion where I have felt that something has happened that I have not been party to.

Q325 **Chris White:** With regard to employee representation, we recognise that it is a good thing. Frances, how does this way of working, this structure, improve decision-making?

Frances O'Grady: I understand you just had a session on diversity. There are many echoes of some of the arguments that are put around improving diversity in respect of gender and race on boards in those for workers. There is also that additional issue of a very direct understanding of what is going on in what must be a key stakeholder relationship for a board, which is with its own workforce, and an important concern in respect of industrial relations obviously being key to success.

Q326 **Chris White:** Could you just be a bit more precise in terms of how it would improve decision-making?

Frances O'Grady: We are all familiar, particularly in debates around the crash, with concerns about groupthink and the domination of one particular way of thinking and one particular perspective. Many people now agree there is strength in diversity. At a very practical level, some of the evidence from the surveys that we quote in our report shows that workers on boards are much more likely to raise and argue the cause for a longer term vision for the company. Rather than just a focus on short-term profits to keep the shareholders happy, workers are often arguing for investment.

Q327 **Chris White:** Have you got a headline case study that you are really proud of—where a worker on a board has made a difference—that you would like to champion or talk about?

Frances O'Grady: You will find in the report Michael Gold's survey of workers' representatives, where they gave very specific examples of further investment in training, much better industrial relations, and investment in R and D looking to the long term.

Q328 **Chris White:** I want to come back to the R and D issue. Investment in R and D would be, I assume, in a board's best interests. How does having employee representation encourage a board to make those long-term decisions?

Frances O'Grady: Boards inevitably, because of our corporate governance system, have to focus primarily on keeping shareholders happy. Remembering that nearly half of all shares in Britain are now held overseas, and some of them are only held for a matter of months, and many shareholders have interests in a range of companies, keeping that constituency happy is different from keeping workers happy. Those workers who are hoping to work for their whole lifetime in a particular company, and are worried about their jobs, their kids' futures and the communities in which companies are sited, tend to take a longer view and a broader view. It is a helpful balance. As we say, it is a voice, not a veto.

However, it is helpful and enriches the experience, thinking and deliberations of the board to have those broader perspectives in there. By the way, I know there has been some talk about giving an existing non-exec director responsibility for that. I am not being flippant when I say that you cannot put a flat cap on somebody and hand them a whippet and pretend that they are bringing a worker's perspective to the board. In our view, we are very clear that they have to be elected by the workforce. Perhaps e-balloting would be helpful here—many companies already use it—in order to have that credibility and genuine perspective to bring.

Q329 **Chris White:** Thank you. I might come back to you. Mick, can you tell us a bit about how you were appointed, and can you tell us a bit about how you might be, for want of a better word, de-appointed?

Mick Barker: Yes. It was the ballot box, basically. Personally, I was elected as the Employee Director of First Capital Connect in January 2007, and I served two three-year terms on that board with an election after three years. The first time I stood, I believe that there were probably around 30 interested candidates; it was something that the employees really got behind. The second time, the amount of candidates was in double figures.

Q330 **Chris White:** Before you talk about how you might be deselected, could you tell me a bit about the skills that made you different from the other 30 or 29? Were you just very good at winning elections, or did you have the skills that they sought? Are you a very popular man?

Mick Barker: I would like to say that I was. The truth of the matter is that in the rail industry the drivers tend to be the biggest number, and I was a driver.

Q331 **Chris White:** Do you ever think that there is a danger of the final chapters of *Animal Farm*, when you are finally not recognised by your work colleagues? You have gone to the dark side. How do you stop that? How do you keep your flat cap?

Mick Barker: And a whippet, of course. I get the question. As a non-executive director of FirstGroup, you could ask that question of any non-executive. That is probably the reason why they do three three-year terms. After nine years it comes to the point when they are considered perhaps not to be quite so independent anymore. That question is the same for me. Certainly, I know where my whippet is and I have still got my flat cap.

Frances O'Grady: It is really important to draw a distinction between union representation and recognition of collective bargaining, and the role that is played as a worker director on the board. As in most of Europe, in this company Mick's role is totally compatible with the traditional union recognition and collective bargaining that goes on elsewhere. Mick is not a delegate.

Q332 **Chris White:** Do the union ever see the employee representative as a disappointment? They hope that that person is going to be looking at the HR issues, long-term investment and stability. Do they think that having their man or woman on the board may devalue the purpose of the union?

Frances O'Grady: Not at all. As I say, I do not think that British employers and British workers are that different from all the other 19 countries in Europe that already have some form of worker representation, with 13 of that 19 being very extensive in the private sector. For sure, there would be a building up of experience and understanding. There would need to be, dare I say it, a red, white and blue model, because there is no one off-the-shelf model. However, we can learn from elsewhere—and we should learn from elsewhere—and we would build up our own experience. However, that fundamental point I really do not think is an issue. No system is perfect, but this is better.

Q333 **Richard Fuller:** Ms O'Grady, you mentioned a couple of times these 19 countries, most of which are in Europe. Is it a concern to you that during the EU debate it was pointed out the only continent in the world that has not experienced growth in the last 10 years is Europe? Europe is not a particularly good model, is it, for growth and achieving living standards improvements? It is the basket case of the world. Why are those examples of corporate governance the ones you point to, rather than in East Asia or the United States?

Frances O'Grady: I am sure that we could get into a broader debate about measures of performance. I would have to challenge your premise in the first instance, but it is helpful to look at our near neighbours. More importantly, of course, it is many companies that are operating across borders. We do have, if you like, significant experience by proxy of companies that are very important to the UK economy and that already operate this system elsewhere.

In that broader context, if you raise it, I was very pleased to hear the Prime Minister's commitment to having workers on boards, and to not just protecting workers' rights but enhancing them. When we are thinking seriously about ensuring that our economy is fit for Brexit, this is a very important part of it, recognising that there are many people in Britain who do not feel the level of trust in business that we would like them to have. There are bigger considerations, not least on top pay but also on decision-making in the board that feels a very long way from ordinary people's lives even though they are most affected by it.

Q334 **Chair:** Frances, on the point regarding what the Prime Minister has said, you have said that you praised what she said about workers on boards. That was back in June or July. Since then, there has been a considerable rowing back, and the green paper has watered down proposals. Are you disappointed with the green paper?

Frances O'Grady: We do not think the green paper is good enough. I am still a little confused, because it was not just July, of course. We then got a particular statement at the CBI conference, and in Parliament—the day of the Autumn Statement, as I recall—there was a re-commitment to having workers on boards. When we got the green paper, our view was that it was not good enough. There is a key concern about how workers on boards would be selected in order to be worthy of that title. I know there were concerns raised in the green paper about that process of selection, but then exactly the same concerns would apply to the advisory panels that were referred to. It seems to be that there are some established ways of doing this to ensure credibility, and that has to be an election.

Q335 **Chris White:** Mick, you entered the board in a unique way, through an election. Under what circumstances could you be removed from the board?

Mick Barker: I could be removed from the boardroom in the same way as any other non-executive, with regard to the rules, conduct and all those sorts of things. I can be removed every three years with a vote by my peers.

Q336 **Chris White:** Say that you were not doing such a good job and all the rest of it. At the end of the day, you are an employee representative. If employees do not feel that you are representing their views, whether as a delegate or a representative, what is the mechanism for you to be removed?

Mick Barker: I would need to look into that. I would not be able to answer that exactly.

Frances O'Grady: I would say, by the way, Mick, that it is not just popularity; it is skills as well. Just like MPs or anybody else standing for election, you have got to have a bit of both, hopefully; otherwise we are all in trouble. This point that they are not a representative is really important. It is something that certainly the trade union movement has lots of collective experience of.

When we have people who go on to the health and safety executive or any other public body, they have to go through the Nolan process. Once they are inside that room, they are subject to the same requirements as any other board member. It is important not to confuse representation. They are bringing a perspective into the boardroom, but they are not reporting back as a delegate would. It is a big difference.

Q337 **Chris White:** Do you ever find that difficult to balance in your thinking, Mick?

Mick Barker: Personally, no.

Q338 **Chris White:** Do you get additional training and support?

Mick Barker: Yes. That would normally take place within the subsidiary companies. I get an induction and anything else I might need when I get to the plc board, but most of the training takes place in the subsidiary companies. That is when people can look at the individual and decide what is needed.

Q339 **Chris White:** On the last panel, Edward Speed said that banking is a special place, and you need to be fully qualified and well-versed in financial legislation and practice. What do you feel about that? Do you think there is any sector in which you could not play a more than adequate role?

Mick Barker: I can only talk about FirstGroup. I would not like to speak about banking. I did spend a lot of time back in the Capital Connect days with the finance director to get to the stage where I was happy and confident. I am not suggesting that Philip Hammond is going to ring me up for financial advice, but I am alright where I am.

Q340 **Chair:** Can I just ask a question of Nigel before I bring Richard in? Mick is a really explicit version of direct democracy; he is in through the ballot box. We have heard on this Committee's inquiry that re-election of directors through the AGM is not particularly seen as a priority. There is very often a lack of choice and it is done on the nod. Do you see real merits in having not just workers on boards but real, true business democracy for the election of directors?

Nigel Wilson: There are some myths about this whole thing. Very few investors are interested in short-term profits. The biggest investors in the world—us, BlackRock, Allianz—who all look after between $1 trillion and $5 trillion, are not interested in short-term profits. The trade union movement is wrong in the sense that these people all want long-term profit growth. There is no evidence whatsoever that these big companies do not invest. Most of the big investments in the UK come disproportionately from big companies. Our problem in Britain is one of smaller companies that do not invest for growth. We have got to figure out how we get the smaller companies in Britain growing much more quickly.

Q341 **Chair:** Can I just challenge you on that? It is slightly outside our remit, but in many respects it is not. Part of the problem of the last 10, 15 or 20 years is dividend policy; share buybacks at the expense of long-term investment has undermined the quality and innovation of our corporate base. Is that not a good, fair point that we are not investing, and shareholders want to extract value rather than put in for the long term and create value?

Nigel Wilson: I just do not think that is true. We have not created businesses in areas of high technology in certain sectors in the way that the United States has done. I went to MIT, which is a privileged place to go to. The model the US has is that of the universities producing incredibly entrepreneurial individuals who can get finance and create the businesses, whether that is an Apple, a Google or a Microsoft. We have never created those equivalents in the UK, and that is nothing to do with the likes of HSBC, Tesco or us not investing. It is whole different sectors that have not been created. We have never created the equivalent of German high-growth SME firms in the UK. There are lots of models we can use from elsewhere in the world to help the UK economy grow.

I would agree with Richard's point that we should not be looking at the worst of Europe as an example of how we can improve the UK; we should be looking at the best of things that go on around the world and borrow them—copy them here in the UK to create greater economic growth. There are too many myths and one-liners in the media that are then regarded as the truth. In fact, that is just not the case.

Q342 **Chair:** Can I just push you on direct democracy?

Nigel Wilson: It is a very good point. We look after about £940 billion. We vote on everything. We take diversity very seriously, and diversity in the wider sense. If we feel the board of a particular company is not exhibiting enough evidence of diversity, we vote against the chairman. We did that 10 times last year. It is not a box-ticking exercise. There were 25 other firms that failed our test of what appropriate diversity was, and we gave them all a health warning. They did not meet the standards that we had set, but the direction of travel on diversity was one we approved of.

We want diverse views in the boardroom. We want, as major shareholders, people looking at all the things that really matter. If worker representation is a part of that process—and is a constructive part of that process—then we would be encouraging that. On exactly what form it takes, we would probably give firms more latitude as to how that works. A lot of firms, as I was saying earlier, are very international. Not everybody works here in the UK; they work internationally, and we have to fit around that dimension. We would like to see all shareholders exercise their votes much more proactively around all of the issues that come out. It is quite amazing how few directors ever get voted down.

Q343 **Chair:** What do we need to do, and what does this Committee need to recommend, in order to push that culture of greater challenge from shareholders from big institutional funds?

Nigel Wilson: Some of that is covered in the green paper. We are hoping by the time the white paper comes out that there will be much more engagement with shareholders. Two of the committees I chaired, on mission-led businesses and executive pay, were all about how we get much more engagement and much more growth in the economy.

We are not getting that, because there is too little active engagement. There is not enough transparency in annual reports about the issues that really matter around diversity; there is not enough transparency about executive pay; there is not enough transparency about ethnic issues, which need coverage. We are heading in the right direction on gender, but in several other areas we are lagging well behind.

The Committee should be forward-looking and not just looking at the issues that are prominent in the media today. There are some very populist issues that are very prominent, but some long-term issues really need to be focused on. It is the smaller businesses. The big multinational businesses are all doing a reasonable job, to be honest. Some of the smaller businesses need a lot more work and a lot more effort to try to realise their true potential. If workers' representatives can play a more proactive role in that, we are absolutely 100% behind it.

Q344 **Chris White:** Sorry to interrupt. Can you clarify your point on where you said that the Committee should not concentrate on populist issues? What would you mean exactly by that?

Nigel Wilson: Executive pay has been one area on which there has been a huge amount of work done, and the various reports that have come out around that are very good and are definitely moving in the right direction. Frances talked a bit about how we get some of the SME firms, rather than the bigger firms, investing more in the UK in areas like R and D and training.

Britain has a big productivity problem, going back to the issue that we raised. We know the delta between us and the other G7 countries is about 30%, which is shocking, and that is driven off training and investment. It is not in the top companies; it is absolutely not. The best of breed over here are as good as anywhere in the rest of the world, and there are endless reports on that. How do we get all of those companies to be better? How do the CBI and the TUC, alongside us—the big shareholders—make more of a difference in those firms?

Q345 **Chris White:** I hope you do not think I am being irritating, but you said that we should not be focusing on populist issues. I would suggest that paying attention to executive pay is right and possibly populist. I would suggest also that investing more in R and D would be right and populist. If your advice to the Committee is not to focus populist issues, I just want to know what those populist issues are.

Nigel Wilson: You are not being irritating. I will just try to correct what I said, just so you understand. Our problem is productivity in Britain. It is the biggest problem we have. That is leading to a lack of real wage growth and all the rest, and lots of things fall out of that. How we solve that is an issue, and that is about better R and D and better training. If in lots of companies there is an issue of underinvestment, which I think is what everybody in the Committee was saying, that is what we need to be focusing on.

The direction of travel around executive pay has received a huge amount of attention in the last three or four years, and there is a massive momentum about that. That is being resolved, but these other problems are not being resolved at all at the moment in our view. Diversity is part of that. Whether it is groupthink or whatever, there is a lack of awareness of how well these companies could be performing relative to their potential. That is what we as big shareholders—maybe the biggest shareholders in UK plc—would like to see addressed.

Q346 **Chris White:** Do you think that there are issues such as productivity that need to be resolved before we pay attention to issues like diversity?

Nigel Wilson: No, they are part of the same issue. We have something called 50/50 by 2020, which is our goal around gender diversity and we are on track for delivering. The message I used to give to my women colleagues was, in one sense, 50% of our workforce are underachieving relative to their potential. It may be a controversial thing to say, but our productivity issue is that beyond grade 5 in our organisation, we have disproportionately fewer women than men.

It is my job as the Chief Executive and the board's job to make sure that happens but be accountable, reporting on that in our annual report and in other areas. It should be a goal of all companies to get the best out of their workforce, and I do not think we are getting the best out of our workforce through underinvestment in R and D and the gender issue. We want a balance rather than just headline-grabbing stuff around executive pay.

Q347 **Richard Fuller:** Mr O'Toole, if I could start this question with you, seeing as you have been there, done it, and got the t-shirt for having worker representation on your board, in the earlier session when we were talking about the representation of women and ethnic minorities on boards, there was a sense that much progress—after lots of years of waiting—was being made, because Government had put some attention to it. There were public targets and a sense of naming and shaming.

Do you think that, when it comes to worker representation for companies other than yours, the Government saying, "We are going to find these mechanisms of focus that take into account the interests of the workforce," would have the same beneficial effect? Or do you think that statutory underpinning through some form of representation that is required and mandated for all firms is the way to go?

Tim O'Toole: The direct answer is I do not know. I can speak to the experience we have had at First, but remember we are all talking about trying to predict an uncertainty, and that is what will make a firm more successful and what will make society more productive. We are making changes that increase our chances but do not lead to anything.

You could not make the case that if you put a worker on your board, you will be more successful. It is hard to tell what would happen. It may; the greater diversity might give you a better percentage chance of success, and in our case I think it does. What is true of another company, though, in another situation, with a different profile and different needs in terms of dealing with the future, I could not say. We have never been proselytisers for workers on boards; we just know it works for us.

Q348 **Richard Fuller:** Ms O'Grady, if Mr O'Toole is correct that there is no prediction, and given what we heard in the other panel—which I know you were not able to attend, but I think you get the gist that there was this particular emphasis that has made some progress particularly for women on boards—would you be satisfied with the Government's encouragements, some target-setting and some sort of public naming and shaming?

Frances O'Grady: I have certainly been a supporter of more diversity on boards in every context. I am sure you will have heard from the evidence you have received that it is important not to over-estimate the impact of a voluntary call to improvement when it comes to looking at how many women we have who are not just non-execs. There are questions about how successful that voluntary approach has been.

We are very clear in respect of workers on boards that it is important for it to be mandatory.

Richard Fuller: Underpinned by statute.

Frances O'Grady: Yes, and that is so that everybody is playing by the same rules.

Q349 **Richard Fuller:** Maybe you can help me with some examples. It is quite straightforward where you have a corporation that sources in the UK and has a UK-only workforce that are full-time employees; I can understand that. Perhaps FirstGroup is an example of that; most of your employees are here, and full-time employees. What about Unilever? It is a UK-listed company. It has operations and employees in different parts of the world. How do you get worker representation mandated there?

Frances O'Grady: Again, you will have seen from reading our report that there are principles that we would like to see apply on a mandatory basis. There are areas where we suggest this is something that we would have to look at more closely, or where there might be flexibility for companies in how they approach a particular issue.

Q350 **Richard Fuller:** However, you recognise that it is quite hard for Unilever to do that, is it not?

Frances O'Grady: Not necessarily.

Q351 **Richard Fuller:** Are the Dutch operations going to be on the Board? Are the British operations going to be on the board? Is it going to be the American operations?

Frances O'Grady: The principle is that the workforce should get the chance to choose who the worker is—or workers, ideally; we are very clear that we want more than one on a board. However, there are plenty of companies where that is not a problem, and there are plenty of other companies where, for example, you have an overseas-owned multinational that will have a shadow board in Britain.

Q352 **Richard Fuller:** Can I give you another example, then? We looked at Sports Direct. That was one of the reasons why we came to look at governance. Sports Direct has about 200 or 300 direct employees and about 3,000 agency workers. How would worker representation work there?

Frances O'Grady: Again, we are clear that it should apply to all workers, so all workers should get the chance to vote. Otherwise, you might be providing a perverse incentive for some bad companies to stick everybody on a zero-hours or agency worker contract in order to exclude them from having the opportunity.

Q353 **Richard Fuller:** It is someone who is working and someone who is working, and if they are subcontractors, it is fine.

Frances O'Grady: Perhaps the more interesting point is: had there been workers on the board at Sports Direct, would we have seen the appalling behaviour that we have seen, or not?

Richard Fuller: It is not clear, I would say.

Frances O'Grady: I agree that it is not clear, but perhaps what we can say is that the excuse that "I did not know it was going on" would have been removed.

Q354 **Richard Fuller:** Maybe. I think we can definitely agree to say that governance at Sports Direct could be a whole lot better than it has been.

One other point on workers: many companies employ an extensive supply chain, so they sit atop; they assemble lots of stuff that comes from people, both within the UK and elsewhere, so the employee in that business is not part of the business at all.

The employee interest—the returns to labour interest—is outside of the company. Should there be any requirement, when it comes to representation, for consideration of supply chain in some of our major companies? You talked about perverse incentives with employees and agency workers. There are tremendous potential conflicts involved in outsourcing your workforce entirely to other people.

Frances O'Grady: We have addressed it on a company basis. Again, we are very clear that it is companies over a certain size; we suggest 250. We also suggest starting with larger companies, taking a pragmatic approach about phasing in change. However, I have just one other point: there is a common theme around concern about the role of worker directors and their capabilities, and what difference they would make. I question—as I did very firmly when we had the debate about women on boards—the assumption that meritocracy already operates in Britain's boardrooms. We will never know, because most directors are tapped on the shoulder rather than recruited.

Q355 **Richard Fuller:** I agree with you completely, but that is why I cannot understand why you are not going for the persuasion focus and the things that Mr Wilson was talking about. He does not need the Government to tell him. He has recognised that there is an issue, as you have; as the Committee has; as the people on the panel have. We now have the ability to see talent for what it is, rather than what it appears to be because of its CV or the old boys' network.

Nigel Wilson: Can I come back on that? People think—and I am sure that my colleagues from FirstGroup will echo this—that boards spend all their time worrying about shareholder value creation. That is just not true. There are consumer and people issues.

Talent is tremendously important in the modern world, and so boards will spend huge amounts of time discussing the talent that exists within an organisation. They are not spending all their time worrying about short-term quarterly profits, and my experience from 30-odd years of being on many different boards across lots of different sectors has been that most boards behave in a pretty responsible fashion and look at a wide range of key issues. It is not all about shareholder value creation from when the board meeting starts to when the board meeting finishes.

Q356 **Richard Fuller:** Mr Wilson, do you think that this underpinning of statute that Ms O'Grady has talked about is necessary, or do you think that the informal approach will achieve results?

Nigel Wilson: The informal approach will work. In general, we want a direction of travel, and for boards to be given flexibility of interpretation.

Q357 **Richard Fuller:** Why should the people of this country trust you? The one issue for corporations over the last 20 years in this country is that they have presided over a growing disparity of returns, where the person who works every day in that company has seen flat or declining wages, and their working conditions, in many circumstances, worsen, while shareholders have done relatively well, and certainly the people who lead those companies have done relatively well. You are asking us to trust you for the next 10 or 15 years and not do what Ms O'Grady wants us to do to underpin some of these things in statute, when if we look back over the last 15 years, there is very little reason why we should trust you at all, is there not?

Nigel Wilson: I think it is very sad that you think that.

Richard Fuller: I am posing a point. I am not saying I think it. I am an MP; I can argue the other side just as convincingly.

Nigel Wilson: One of the problems has been that we have created a situation where the FTSE is about the same today as it was 20 years ago. It has gone nowhere. There has been a lack of transparency about executive pay over that period, which has caused all sorts of issues and unfairness. However, the root of the problem is productivity. At the end of the day, that is the measure in which we have lagged the most behind as a country, and that is the issue that we need to be addressing, because that is the thing that will drive better wage growth in the UK. It is better investment; better R and D; better training; a better educated workforce, and that is what we should be striving to get.

We have been around for 185 years. People trust us with billions and billions of pounds of their money and insurance policies, and Unilever is a trusted brand. People buy their products every day, so there is a huge degree of trust that exists between consumers and companies.

Frances O'Grady: I would suggest that there is a growing number of business leaders who recognise that trust is low. I personally and publicly debated this with a number of business leaders, including Simon Walker of the IoD, who is an advocate of the voluntary approach; he is not opposed to workers on boards but is an advocate of the voluntary approach. A number of years ago, I asked him to find me six volunteers, which I thought was a modest request, who we could work with genuinely to see whether we could trial a voluntary approach and make it work for everybody, and learn something. Not a single volunteer was found.

There is something very sad when we hear in every company report that "the workforce is our greatest asset", and yet there is clearly a concern, presumably, about the loyalty and capability and willingness to follow confidentiality of a member of somebody's own workforce in the boardroom. I find that extraordinary, and people far more cynical than me would suggest that some of those populist issues like top pay are one reason why there is resistance to this change. Of course, on average, in the FTSE 100, it has gone up £500,000 over one year. There is no sign of any restraint in terms of pay at the top, and the cynics will win out if we do not do something now.

Q358 **Chair:** Thank you. Tim, could I ask your advice on this? Frances makes an important point about having it as a voluntary thing or whether it should be mandatory. You have been in other companies; you are non-exec director of other companies. You have the example and the experience of FirstGroup, but why is it that what you do cannot apply equally across the board to every other company?

Tim O'Toole: The word I could not speak to is "equally", because of the different circumstances. Mick, and employee directors, are a strength of FirstGroup, and that is acknowledged, which allows it to be a strength. If it is turned into an imposed requirement, it will not be seen as a strength; it will just be seen as another thing of compliance, and that will lead to shadow board meetings and all the rest of it. It has to be organic; it has to work for your company, and the board has to embrace it. If more people did it, they would find it is a strength.

Q359 **Chair:** Is that what we have found with women on boards and what we have found with ethnic diversity? Is it a case of there being resistance to change, but, when boards experience this, they realise it brings a new perspective, diversity and avoids groupthink? They think, "This is great. We should have done it earlier."

Tim O'Toole: Absolutely, and so this Committee, Government, and business organisations beating the drum is very important, as is pressure from shareholders saying, "Why do you not have an employee director?" and constantly interrogating management, in the same way that the Davies Report came out and said, "This is an expectation of gender diversity on a board." The same things can be done, but a statute that would impose this would be a mistake; as Mr Fuller pointed out, you can come up with all sorts of examples that seem to make it a ludicrous requirement. If anything, it would risk competitiveness generally. An employee representative is a great strength, but people have to embrace that.

Q360 **Michelle Thomson:** Moving on a little bit, Mick, I wanted to ask you a question, because I am just interested. How challenging are you on the board?

Mick Barker: The same as the other non-executive directors, depending on the discussions. I participate in all of the different discussions. Obviously, I am continually thinking about the perspective of the workers, but I am just as challenging, depending on what the subject matter might be.

Q361 **Michelle Thomson:** Have you ever felt inhibited in being challenging?

Mick Barker: Absolutely not. If anything, I am encouraged to challenge.

Q362 **Michelle Thomson:** Okay, I am just interested. Thank you. It moves on to what the right balance is in the board between the challenge and the collegiate. I am interested to get your views on how we get that balance right. My limited board experience was that there was plenty of challenge—quite aggressive challenge, to be honest—that also was not appropriate, but I am interested in your views, and probably yours, Nigel, immediately.

Nigel Wilson: Yes, I have been on lots of boards. I have been a chairman of a board and a non-executive director, and I have been chief executive for a number of boards as well. They are not friendly, chummy places in the modern era. They have evolved dramatically over the last 30 years. There is a very high level of engagement. The other thing, as a person who comes from the land of flat caps and whippets, is that not everybody you meet on the shop floor, as it were, is a flat-cap-and-whippet sort of person.

Frances O'Grady: This was irony. I do not have one myself.

Nigel Wilson: I do not doubt that the worker representative will provide a strong intellectual and business challenge as part of the process. I am sure that Mick does that, but the idea that this is a chummy club of upper-class people who have gone to the finest public schools in Britain is no longer the case. I grew up on a council estate in the North of England, as an example of that. There are lots of examples of that.

How do we make the most of that challenge—as a big shareholder—in the most productive way, and how do shareholders get much more actively engaged in the process? A lot of this stuff has to be voluntary. As Tim was saying, it is a road and a journey that we have to go down, and people will go down it at different paces and learn by doing.

The Davies Report was a sense of direction and a direction of travel. Most people have seen it as very positive engagement, and we are going down that route. Those who are not performing as well are getting nudged in the right direction, as I said. We vote against them, and other large institutions do as well.

Q363 **Michelle Thomson:** Is change happening quickly enough?

Nigel Wilson: Change is happening quickly enough. The other issue, as I talked about earlier, that is not being addressed quickly enough is that the smaller companies—not the bigger companies, necessarily, but lots of the smaller companies—need to step up and have more investment. That is physical investment, digital investment, but also people investment, and that is a huge gap here in the UK.

Q364 **Michelle Thomson:** I sense Frances is eager to come in here. You look as though you wanted to.

Frances O'Grady: On your question, there is lots of good practice; there is lots of work on what makes for a good board and where that balance lies, so for me, it is about constructive challenge. It is about independence of view, and it is about bringing those different perspectives in. The role of the chair is very important in recognising the importance of understanding different stakeholders and recognising the importance of that to the success of the company, including, of course, the importance of the workforce.

I find the division between SME companies and larger companies interesting. I speak to many leaders of smaller companies in those supply chains that we have referred to earlier who are feeling absolutely hammered in terms of price and very little power, if you like, to negotiate their position. They would probably give you chapter and verse on the question of investment and why they are not doing better.

Q365 **Michelle Thomson:** I want to stay in this space, so talking about challenge again, do you think that a predominantly male board can accept and embrace a challenging woman?

Nigel Wilson: Oh, gosh, yes.

Michelle Thomson: I have just been on the wrong boards, obviously.

Nigel Wilson: I am the father of five beautiful daughters, so if you want to know what challenge feels like, come to my house any day of the week. I live in a world of challenging women. The world has moved on in the last 30 years, and certainly some of the industries that I have been involved in were very male-dominated, but we live in a world where we have to seize this meritocratic opportunity that we have. We have a huge opportunity to get more out of improved diversity. There are lots more capable people who need to fulfil their potential.

We have not done a brilliant job getting those more capable people to fulfil their potential, but in the modern era there are some brilliant women leaders of businesses. There are some great non-executive directors who are women. As we get more and more of them, that question will not be asked anymore, and I am hoping that maybe in 10 years' time we will not even feel the need to ask that question, because we will have moved on to different issues that need to be addressed.

Q366 **Michelle Thomson:** Tim or Frances, do you want to come in on that?

Tim O'Toole: We still have a long way to go. There is definitely sexism still in the way people define and react to an aggressive woman executive versus an aggressive male executive—which is not to deny the progress that is spoken of, but it is something we still always have to question ourselves about. I put it most simply that my other country elected a black President, but there is still a lot of racism.

Q367 **Michelle Thomson:** That is a good analogy. Frances, do you want to add anything?

Frances O'Grady: There are echoes. I remember, years back, in the debate it was suggested that all the big decisions would be taken in the gents', rather than in the boardroom, if women were allowed in. Lo and behold, there has been some progress and some understanding, but I do draw parallels. In some quarters—I am not suggesting your good self, Nigel—I would suggest an emotional resistance to workers on boards, in exactly the same way that there was an illogical and emotional resistance to women or BEM people on boards, too.

It would help to recognise that, because fundamentally, for all the objections that are raised and the big practical questions about models for corporate governance and workers on boards, we have 19 other countries doing it. There will not be a problem that this Committee encounters that has not already been encountered and solved in another country that already has workers on boards, so I find it hard to put too much weight on some of the objections that are being raised, because if there is a will, there is a way.

Nigel Wilson: If you look at gender, we have a woman Prime Minister. The Director General of the CBI is a woman. You are also a woman.

Frances O'Grady: I have managed alright. I think I could do on a board as well.

Nigel Wilson: We are seeing tremendous progress around this. There is obviously more we can do, and I agree with Tim's comments around that, but the direction of travel is pretty good. There is a huge opportunity still to come, and speaking with my institutional shareholder hat on for a moment, the potential is enormous in the UK, because we still have massive leaps to make. The speed of travel, for many companies, is not as fast as we would like it to be, but the direction of travel is certainly in the right direction.

Q368 **Michelle Thomson:** If we are all agreeing that diversity is good, how do we measure that in terms of overall contribution and performance of a company, or is it just that we generally agree it is good because it reflects our society?

Nigel Wilson: No, we should make boards accountable for it, and make sure that it is measured—that the number of people are measured by whatever categorisation individual companies have. I would not make that statutory; I would make it voluntary as to how they should be categorised, but the peer differential between people should be measured, and the overall mix. Everybody has this problem at about grade 5 of how you get greater representation.

Q369 **Michelle Thomson:** How about measurable output in terms of company performance?

Tim O'Toole: You cannot do that. You can measure this as an input because you believe in it, and statistically the odds will be in your favour, but this is not a formula. The world is finally getting that there is a little bit of truth everywhere, so if you go and gather, you have a better chance of being successful, rather than just being stuck in one paradigm. However, many people who go do the right thing will still fail, because there are just so many other variables.

The only measurement you can do is an input measurement: that is, how many women are on the board, whether you have worker representation, or whatever questions you think are appropriate for the diversity that you are trying to accomplish. However, you cannot create a formula in business that says, "If you do each of these eight things, you will be a big success."

Q370 **Michelle Thomson:** My last question is about cognitive diversity and measures of same. Is it reasonable to apply the same measures of cognitive diversity equally to men and women?

Nigel Wilson: That is a really deep, profound question. It will probably be difficult to answer that one.

Michelle Thomson: I just threw that in there. It is the last day of term, and my brain is still working slightly.

Nigel Wilson: You think you are home and dry on this one, and then you get a question like that. It is a very good question; Frances said the thing about groupthink, and there has been a risk of that over time. How do you therefore get cognitive diversity on the board? There are discussions about whether women and men are different, and I will plead the fifth on that, but the cognitive diversity question is something that, on a forward-looking basis, we should be considering much more.

We do worry, as institutional shareholders, that the same thing will happen: that we have all looked at a problem in a specific way and allowed banks to get massively over-leveraged, and we did not know that RBS had a £2 trillion balance sheet or whatever it was, and there was a whole bunch of groupthink going on and we did not know. Therefore, something arises that causes a massive disruption to the economy, and we should make sure that there is better cognitive diversity. Sitting here today, I honestly do not have the answer to how we do that, but I recognise that is a really good question that requires a very good answer. Sadly, I cannot give that answer today.

Frances O'Grady: I wonder if I might make a comment? It is slightly bizarre for me. On the one hand, we have now radically moved as a country to a position where we all think it is a good thing to have more women on boards, unless they are women employed in the company, in which case some people are concerned that they do not want workers on boards and do not want it to be mandatory.

Obviously, we have focused a lot on the benefits to the company—which I firmly believe in, and which a lot of the evidence supports—but there is a basic question of justice, both in terms of diversity on race and women, and also workers on boards. Companies do not operate on their own planets. They are located in real communities and societies, and society has a right to say, "We think this is what is good for our country."

We are approaching a very challenging time for the UK with Brexit. We have workers still £20 a week worse off on average than they were before the financial crash. We have seen a dramatic increase in executive pay. We have seen many people feeling that our companies are out of touch with lives on the shop floor and concerns in the community, so there is a basic justice point, as well, about opening that boardroom door to workers.

Q371 **Amanda Milling:** Sorry to be really late, first of all, Chair. I have one question, which is based on some of the things I have been hearing while I have been here. We talked about workers on boards, and there is one version, which is to legislate, and there is one that is just to let it happen. If we were not to legislate, fast-forwarding the clock 10 years, do you think there would be much greater presence of workers on boards, and would it be a case where you would be looking back, going, "I cannot believe we had that great long debate about it?" Would it just happen? I am just interested to see what you think it will look like in 10 years.

Frances O'Grady: I am not confident that we would see the change. Our economy, more broadly, needs to see change—and the role that companies need to play within it. As I was saying earlier, I made that call some time ago to business leaders to come up with volunteers. I would make that call today: it would be great if companies could come forward and say, "Let us work together and see if we can make this work on a voluntary basis."

However, I am not going to be waiting by the telephone, as it were, because all the experience in other countries, again, is that businesses quite like certainty. We saw that in quite different areas, like the minimum wage, where they ultimately came round to the idea that, although they opposed it to start with, "If it is going to be introduced, we want everybody to have to play by the same rules."

Our preference is very strongly for a mandatory approach, and for a pragmatic introduction and phasing of size of company, different models, and so on. Let's work it through together. Let's give companies autonomy in some areas, where they can work out what is best for them. But as a principle, if we do not have that as a mandatory principle, I am afraid that it just will not happen, and the Prime Minister's promise that we would have workers on boards will not be met, which I think we would all regret.

Amanda Milling: Has anybody else got anything to add to that? No.

Chair: Thank you very much for your comments. We really appreciate it. Thank you again; thank you, colleagues.