

# The Section 172(1) Statement and UK Public Companies & Bird & Bird



*With the AGM season for many UK public companies fast approaching, we have had a number of clients raising questions about the new requirement for a “s172 statement” to be included in their Annual Reports.*

## Introduction

By way of reminder, the Companies (Miscellaneous Reporting) Regulations 2018 (the "**Miscellaneous Reporting Regulations**") introduced the requirement for certain UK companies to include a statement which describes how the directors have had regard to the matters set out in section 172(1) of the Companies Act 2006 (the "**Companies Act**") in their strategic report, for financial years commencing on or after 1 January 2019. This article considers how this requirement will apply to UK public companies.

Section 172(1) of the Companies Act sets out the matters that a director of a company must have regard to in fulfilling his or her duty to promote the success of the company, which include the interests of various stakeholders.

## Section 172(1) of the Companies Act

Section 172(1) of the Companies Act provides that a director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to:

- a the likely consequences of any decision in the long term,
- b the interests of the company's employees,
- c the need to foster the company's business relationships with suppliers, customers and others,
- d the impact of the company's operations on the community and the environment,
- e the desirability of the company maintaining a reputation for high standards of business conduct, and
- f the need to act fairly as between members of the company.

The requirements under section 172(1) are consistent with the principle of "enlightened shareholder value"; recognizing that companies are run for the benefit of shareholders, but that the long-term success of a business is dependent on maintaining relationships with stakeholders and considering the external impact of the company's activities.

## The Section 172(1) Statement

Section 4 of the Miscellaneous Reporting Regulations has added a new section 414CZA to the Companies Act.

Section 414CZA(1) provides that a strategic report for a financial year of a company must include a statement (a "**Section 172(1) Statement**") which describes how the directors have had regard to the matters set out in section 172(1)(a) to (f) when performing their duty as set out in section 172 of the Companies Act.

Section 414CZA(2) provides for a carve out from the requirement to include a Section 172(1) Statement in the strategic report for "medium-sized companies".

However, section 467 of the Companies Act excludes certain companies from being treated as "medium-sized" regardless of whether they meet the relevant qualifying conditions. **This includes UK public companies.**

**As a result, all UK public companies listed on the London Stock Exchange's Main Market or AIM will need to include a Section 172(1) Statement in their strategic reports going forward.**

## Contents of the Section 172(1) Statement

The Financial Reporting Council has produced some useful guidelines (the "Guidance") on what would be needed to be included in a

Section 172(1) Statement.

Pursuant to the Guidance, the information contained in a Section 172(1) Statement will depend on the individual circumstances of each company, but companies will probably want to include information on some or all of the following:

- a The issues, factors and stakeholders the directors consider relevant, in complying with section 172(1)(a) to (f) of the Companies Act and how they have formed that opinion;
- b The main methods the directors have used to engage with stakeholders and understand the issues to which they must have regard; and
- c Information on the effect of that regard on the company's decisions and strategies during the financial year.

The Guidance provides that the Section 172(1) Statement should focus on matters that are of strategic importance to the company, and the level of information disclosed should be consistent with the size and complexity of business.

The Guidance also explains how the Section 172(1) Statement requirement may be met by companies, and highlights a number of important factors for consideration.



We have provided a summary of a number of these factors below:

### Long-Term Success

- Companies should consider providing information on how the long-term success of the company has been taken into account in making strategic decisions. This could include considering the interests of other stakeholders, the long-term impact of the company's activities on the community and environment or other broader matters that may affect company performance over the longer term.
- Companies are encouraged to consider the linkage between the principal risks disclosed in the strategic report and disclosures made in the Section 172(1) Statement.

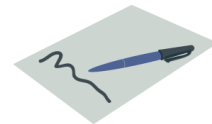
### Stakeholders

- Companies should identify their key stakeholders and explain the importance of those stakeholders to the long-term success of the company. In particular, companies are encouraged to consider disclosures regarding their relationships with pension schemes, pensioners and their entire workforce.
- Companies should explain the outcomes of their engagement with key stakeholders and the impact on the board's decision making, as the way in which a company engages and communicates with its stakeholders provides insight into the relative importance that it places on those relationships.

- Companies are encouraged to innovate and experiment in order to provide information which helps to explain the benefits created for other stakeholders, which may sometimes be difficult to measure but can provide significant insight.

### Principal Decisions

- Companies should identify the principal decisions taken by the board during the year, how regard was had to the matters set out in section 172(1) (a) to (f) of the Companies Act when making decisions and the effect of that regard.
- Where there are conflicts between the interests of one group of stakeholders and the interests of other stakeholders or the shareholders, or where the interests of one group have been prioritised over another, companies should consider explaining how the directors have considered the different interests and the factors taken into account in making that decision.
- Companies should consider explaining how directors have had regard to the long term and the interests of stakeholders, including for example the long term viability of the company, the need for research and development or capital investment and the interests of other stakeholders, such as any pension fund or current employees, both in the setting of the capital allocation and dividend policies and then in the application of those policies each year.



## Culture

- Companies should consider explaining how the company embeds the desired culture (which is a combination of the culture of the values, attitudes and behaviours demonstrated by a company) in its activities and relations with stakeholders.

## Publication Requirement

Quoted companies (companies listed on the Main Market of the London Stock Exchange) are already required to make their annual report available on their website.

Pursuant to section 426B of the Companies Act, other UK public companies must ensure that the Section 172(1) Statement is available on a website that is maintained by or on behalf of the company. The Section 172(1) Statement must be kept available on the website until either:

- the Section 172(1) Statement for the company's next financial year is made available; or
- if no Section 172(1) Statement is required to be made available for the next financial year, the end of the next financial year.

Under section 426B of the Companies Act, there are potential criminal offences and fines for directors for failure to publish information on a website where there is an obligation to do so.

## Consequences for failure to include a Section 172(1) Statement

Pursuant to section 414D of the Companies Act, if a strategic report is approved that does not comply with the requirements of the Companies Act (include the requirements regarding the Section 172(1) Statement), every director of the company who—

- knew that it did not comply, or was reckless as to whether it complied, and
  - failed to take reasonable steps to secure compliance with those requirements or, as the case may be, to prevent the report from being approved,
- commits a criminal offence and may be liable to a fine.

If you would like further information about this requirement, please contact:

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