The Money Charity Response – FCA CP 21/24 Diversity and Inclusion Reporting for Company Boards and Executive Committees (October 2021)

The Money Charity is a Financial Capability charity whose vision is to empower people across the UK to build the skills, knowledge, attitudes and behaviours to make the most of their money throughout their lives, helping them achieve their goals and live a happier, more positive life as a result.[1]

We welcome the opportunity to respond to the Financial Conduct Authority's Consultation Paper 21/24 *Diversity and Inclusion on Company Boards and Executive Committees.*

Reinforcing the response we made to the combined Bank of England, Prudential Regulation Authority and Financial Conduct Authority Discussion Paper on Diversity and

[1] See box on back page.

Inclusion,[2] we support (with some modifications set out below) the FCA's proposals on reporting, which we think are timely and capable of making a significant difference to how UK companies think about and practice diversity.

Key Points

1. We welcome CP21/24 with its discussion of diversity on company boards and executive committees, the targets to be set, the evidence of impact and the proposals for reporting.

2. We note that research has shown that Financial Wellbeing is an outcome of a range of factors, including socio-economic, so that if certain genders, ethnicities or other groups are excluded from peak positions in the economy, this must inevitably contribute to poorer wellbeing outcomes for these groups. To promote financial wellbeing, particularly in the context of an explicit government agenda of "levelling up", it is necessary that all parts and levels of the economy should be open to people from all backgrounds on an equitable basis.

3. We broadly support the reporting proposals, with the exception that we think that the proposal to have "at least one" board member from a minority ethnic background has an unintended tokenistic feel. We suggest that it would be better to set a range appropriate to the operating territory and markets of the company in question. Setting a range would indicate that the goal is to normalise minority ethnic participation at all company levels. This is particularly the case where the companies in question are large international companies with larger-than-average Board sizes and markets in Africa, Asia, Latin America and the Middle East, but should also apply to FTSE350 companies with large UK markets, given the increasing diversity of UK society.

Overall Comments

Diversity and Financial Wellbeing

As a Financial Wellbeing charity, we take an interest in research which explores the components and causes of Financial Wellbeing. A recent series of studies[3] in countries similar to the UK – Norway, Canada, Ireland, Australia and New Zealand – have quantified the different factors contributing to financial wellbeing. For our Financial Education work, we focus on the financial behaviours that lead to improved wellbeing, but what is relevant to this response is that the studies identify socio-economic factors

[2] https://themoneycharity.org.uk/media/The-Money-Charity-Response-FCA-DP21-2-Diversity-and-Inclusion-Sep-21.pdf
[3] Kempson and Poppe 2017, 2018a, 2018b, 2018c, Financial Consumer Agency of Canada 2019, Prendergast et al 2018.

as playing a major role.[4] There is a positive relationship between income and the rate of change of financial wellbeing, which increases at very high and very low levels of income. Negative impacts are recorded for being unemployed, experiencing a drop in income, being self-employed, experiencing an expenditure increase, having more children, renting and (on certain measures of financial wellbeing) being female.

It follows from this that where a society is marked by structural inequalities, these will also deliver different financial wellbeing outcomes. For example, if women and people from certain social and minority ethnic groups are more concentrated in jobs that are lower-paid and less regular in pay – for example, the gig economy, self-employed or part-time service work – these groups will experience lower financial wellbeing.

On the other hand, if certain groups – for example, white, male, privately-educated, middle or upper class – are over-concentrated in high-paying, full-time jobs, they will experience higher financial wellbeing.

These inferences have been supported by evidence of the impact of the Covid-19 pandemic, which many reports have shown to have had differential effects on wellbeing according to social class, gender and ethnicity, with these differences arising from the different structural starting points of different social groups.[5]

Consumer diversity

The other side of financial wellbeing is the experience people have as consumers. Diverse consumer needs can only be met by diverse management teams whose eyes, ears and hearts are open to the variety of lives that people are leading. Progress on diversity and inclusion complements other reforms such as the FCA's guidance on consumers in vulnerable situations and the introduction of a new Consumer Duty.

If the diverse consumer experience of financial services is improved, this will increase engagement with financial services, improve financial wellbeing and benefit the reputation of the financial services industry.

What should the targets be?

One of the key issues discussed in the Consultation Paper is the size of the targets to be set for gender and ethnic representation. The Paper proposes that at least 40% of the Board should be female and "at least one member of the Board should be from a non-White ethnic minority background (as categorised by the ONS)" (page 18).

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[4] The studies use Principal Component Analysis and Multiple Regression, so are not simple correlation studies, but identify the effect of each individual factor assuming all other factors are held constant.

[5] See, for example, our study for the Money and Pensions Service on the impacts of Covid-19 on financial education. Available at: https://moneyandpensionsservice.org.uk/wp-content/uploads/2021/05/financial-foundations-and-covid19.pdf

In our response to the BoE/PRA/FCA consultation, we said the following:

> "It is important to avoid tokenism. For diversity to feel natural, Boards should have several members from minority ethnic backgrounds and be 40-60% female. Similar targets should exist for senior executive appointments.
>
> Large SMEs should be able to achieve similar ratios to big firms while small and micro-SMEs should be able to achieve at least one or two dimensions of diversity each."[6]

Rather than there being a magic number ("critical mass") above which the effects of diversity kick in, the evidence seems to suggest that there is a continuous relationship between improved representation and better results for diverse populations.[7] The more people involved from diverse backgrounds, or the more women compared with men, the better the results for the relevant groups across the whole organisation. From this evidence, one is better than none, but two is better than one, and so on.

For women the goal should be equal representation, given that the genders are roughly equal proportions of the population. "At least one" for ethnic diversity has a tokenistic feel. We know this is not intended by the FCA. The problem is with the word "one".

For this reason, we propose in answer to Question 5 below that the target should be expressed as a range appropriate to the operating territory and markets of the company in question. In our view this would more appropriately reflect the size and global range of many UK companies. As part of our answer, we give an example of one FTSE100 company that has four out of eleven board members (36%) from "non-White" backgrounds. Looking at examples of companies which have significant diverse ethnic representation on their boards underlines the enormous range of international talent now available to company boards from Asia, Africa and other parts of the world, as well as from the UK, Europe and the USA.

When one looks at the impressive CVs[8] of ethnically diverse board members, it seems astonishing that 31 out of 83 FTSE 100 companies that provided data to the 2020 Parker Review and 119 out of 173 FTSE 250 companies that provided data had **no** persons of colour on their boards.[9]

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[6] The Money Charity response to the BoE/PRA/FCA discussion paper on diversity and inclusion, Sept 2021, page 10.

[7] See for example: https://www.researchgate.net/publication/231910711_The_Story_of_the_Theory_of_Critical_Mass

[8] See page 6 below.

[9] Consultation Paper, page 15.

Answers to selected consultation questions

Q1: Do you agree with the proposed comply or explain disclosure requirement on board diversity targets relating to gender and ethnicity?

Yes. We think that the need to comply or explain forces companies lacking diversity to address this shortcoming, think through the reasons for it and find potential solutions. Given the quality of diverse talent available, companies are likely to find that the process is less painful than they expect and will soon pay dividends in corporate governance and strategy.

Q2: Do you agree with the proposed disclosure obligation to set out numerical data on the gender and ethnic diversity on a company's board and its most senior level of executive management?

Yes.

Q3: Do you agree with the proposed scope of who would be required to report under the new Listing Rules proposals, and those we have excluded (e.g. issuers of listed debt)? If you disagree, please explain why.

We think this needs further thought, because the exclusions appear to leave out a lot of large and influential players in the financial sector and therefore in the development of the relevant talent pool. We see the argument for beginning with listed companies, but we think a strategy is needed to make sure that diversity expands throughout the whole sector.

Q4: Do you agree with our proposal to include overseas and smaller issuers in the new Listing Rules proposals? If not, please explain whether you would propose further flexibility within the rules, or would exclude such companies from scope?

Yes. As we submitted in our response to the BoE/PRA/FCA consultation on diversity and inclusion, we believe that companies of all sizes can and should make a serious commitment to diversity.

Q5: Do you agree with proposed targets on gender and ethnic diversity representation at board-level of companies? Should we consider any additional or different targets?

Regarding female representation we think that equality should be the goal, given that the genders are roughly equal proportions of the population. In our previous consultation response, we suggested the range 40-60% for female representation. The target that "at least one member of the board is from a non-White ethnic minority background (as categorised by the ONS)" is in our view not ambitious enough and has an unintended tokenistic feel. For ethnic minority representation to feel normalised, companies need to have several people from minority ethnic backgrounds in senior executive and Board positions. If there is significant representation at this level, then cascading through the organisation is natural and organic. On the other hand, a single person from an ethnic minority background cannot fairly be expected to carry the flag for diversity throughout the entire organisation. It is also the case that the size of Boards of in-scope companies varies considerably. The average Board size is around seven (for the FTSE 350),[10] but large FTSE 100 companies typically have larger Boards. For these reasons, we suggest that the target should be expressed as a range appropriate to the ethnic diversity of the company's operating territory and target markets. This is to indicate clearly that the intention is to normalise minority ethnic representation and not to encourage tokenism.

Some companies may resist the proposed targets on the basis that they think they will have difficulty in finding the talent they need. We disagree with this. Particularly where companies have large overseas markets, which many UK listed companies do have, the relevant pool of talent includes not only the UK, but the whole of Africa, Asia, the Middle East and the rest of the world. The rapid economic development of East Asia has produced a huge pool of relevant talent, which many UK companies are already tapping. Of course, FTSE companies should look inside the UK as well and there are many qualified people from minority ethnic backgrounds in the UK who could fill Board positions.

As an example of normalising ethnic minority representation, we refer to the example of Unilever, the largest company in the FTSE 100.[11] Unilever has a Board of eleven, four of whom (36%) are from minority ethnic backgrounds: one Chinese-Canadian (female), one Hong Kong Chinese (female), one Korean-American (female) and one UK-based Zimbabwean (male).[12] In terms of skills, the minority ethnic Board members comprise a global marketing expert and former microfinance CEO, a former Vice Chairman of the China Securities Regulatory Commission, a Harvard Business School professor and the founder of an international telecommunications company.

This is not an isolated example of the talent available. HSBC, for example, has three Board members from East Asian backgrounds, two of whom are female, comprising a former executive from an engineering multinational and two investment bankers.[13]

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[10] Calculated from the numbers in paragraph 3.21, page 15 of the Consultation Paper.
[11] The Money Charity does not have a relationship with Unilever, nor do we necessarily endorse or not endorse other of the company's practices. We mention the company purely as an example of Board-level diversity.
[12] https://www.unilever.com/our-company/our-leadership/
[13] https://www.hsbc.com/who-we-are/leadership-and-governance/board-of-directors

Many UK financial companies have large and/or head offices in London, which is a global city with a highly diverse population, nearly 50% from minority ethnic backgrounds. Other leading UK cities also have significant minority ethnic populations. So, finding UK-headquartered companies with *zero* minority ethnic board representation, as the Parker Review indicates is the case for the majority of FTSE 250 companies, is highly anomalous and needs to be addressed as a matter of urgency.

Q6: Do you agree with the format and extent of numerical data reporting proposed in the tables in Annex 2? If not, please explain any changes you would suggest or where further clarity is needed.

Yes.

Q7: Should we consider requiring similar numerical data reporting for the level below the executive management team of in-scope listed companies and / or seek data on representation by sexual orientation? If so, we welcome any drafting suggestions and views on any impact this may have for the CBA and scope of our proposals.

Yes, we think the FCA should consider reporting similar numerical data for the level below the executive management team. This is because of the importance of mid-career promotion for the advancement of women and people of minority ethnic backgrounds.[14]

Reporting on sexual orientation is tricky because not everyone is “out” or comfortable with their sexuality being a matter of public discussion. Where the numbers are small, individuals can be identified or guessing games triggered. We suggest that the FCA consult closely with organisations representing LGBTQ+ people to find the best approach to promoting and reporting on LGBTQ+ representation.

Q8: Do you agree with proposed amendment to DTR 7.2.8AR to add to the examples of diversity aspects included in DTR 7.2.8AR which issuers could disclose in their reporting on their diversity policy, and to extend consideration to key board committees? If not, please explain why.

No comment.

Q9: Do you agree with our proposed new guidance provision DTR7.2.8CG encouraging in-scope issuers to consider providing numerical data to further inform reporting on the results of their diversity policies? If not, please explain why.

[14] We present evidence for this point in our response to the BoE/PRA/FCA discussion paper on diversity and inclusion.

No comment.

Q10: Do you agree with the proposed implementation timing? If not, please explain why and indicate what alternative timeframe you consider appropriate

We agree with the proposed timing, i.e. reporting on the accounting year beginning in January 2022. The proposed reporting does not involve huge financial expenditures or new infrastructure. It can be done quickly and cheaply, so we see no reason for any delay.

Q11: Do you agree with our phased approach to improve our use of data over time? Should we consider other approaches? If so, please suggest these.

Broadly yes. We suggest that the FCA considers working with appropriate university researchers on cross-sectional and longitudinal studies examining the outcomes of a shift to greater diversity in the financial sector. Financial firms are subject to a multitude of simultaneous pressures, so a methodology to isolate the independent effects of diversity will need to be carefully designed.

The Money Charity is the UK's Financial Capability charity providing education, information, advice and guidance to all.

We believe that everyone achieves Financial Wellbeing by managing money well. We empower people across the UK to build the skills, knowledge, attitudes and behaviours to make the most of their money throughout their lives, helping them achieve their goals and live a happier, more positive life as a result.

We do this by developing and delivering products and services which provide education, information and advice on money matters for those in the workplace, in our communities and in education, as well as through influencing and supporting others to promote Financial Capability and Financial Wellbeing through consultancy, policy, research and media work.

We have a 'can-do' attitude, finding solutions to meet the needs of our clients, partners, funders and stakeholders.

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