Governance Report

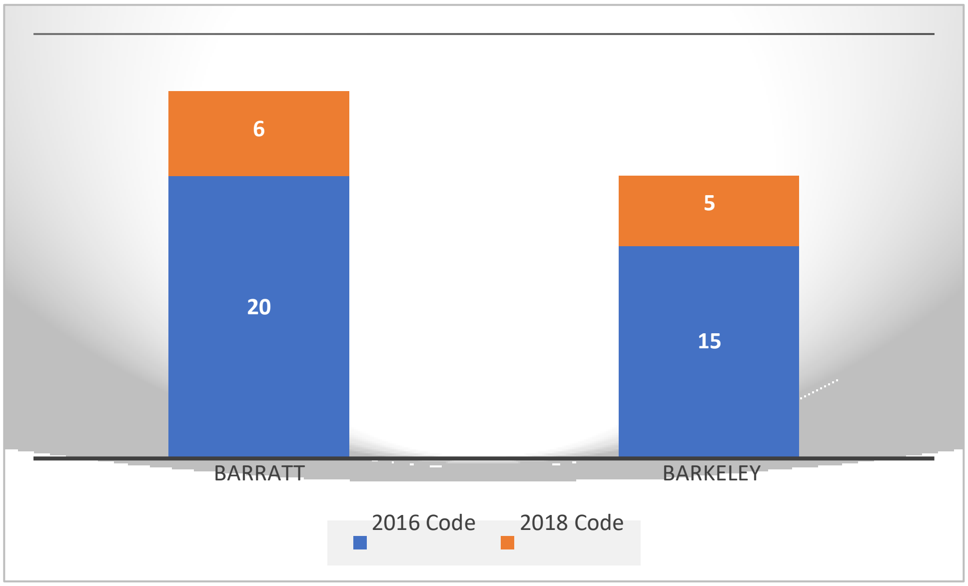
Below, I analyse and contrast the extent and structure of corporate governance ("Governance") quality and disclosure of two UK listed companies, Barratt Developments plc ("Barratt") and Berkeley Group ("Berkeley"). Specifically, I will focus on how Governance and its disclosure is aligned with the UK Corporate Governance Code ("the Code"). Note that I analyse disclosures contained in the annual reports for the financial year ended in 2018 (April 2018 in case of Berkeley and June 2018 in case of Barratt), implying that both documents still follow the 2016 edition of the Code. However, the 2018 edition, whilst maintaining the Code's objectives, has restructured its approach by grouping its prescriptions under a different set of headings.

Disclosures of the Code's Contents

Both companies repeatedly stress that their disclosure is driven and in accordance with the Code. Berkeley notes "the Company has fully applied the main and supporting principles of the Code issued in 2016" (2018, p.62) and Barrett describes its disclosure as "details of how the Company has applied the main principles and provisions of the UK Corporate Governance Code 2016" (2018, p.4).

However, their approaches are quite different. Whereas Berkeley's disclosure explicitly spells out the main principles of the Corporate Governance Code, Barrett's references to the Code are much more subtle. Even so, Barrett's disclosure arguably addresses the Code in more depth, as shall be explored. Thus, when reviewing a disclosure, it is important to adopt a critical focus in order to read between the lines where necessary.

Figure 1. Mentions of the Code in Relevant Sections of the 2018 Annual Reports



Both companies disclose a similar level of attention and effort with regards to the 2018 Code. Given that both companies operate solely in the UK, they do not mention Governance requirements in other jurisdictions.

<u>Leadership and Effectiveness</u>

Among the provision in the Leadership Principle, two stand out in this case: the need for high engagement from the board and sufficiently high independence of the board. The disclosure again differs. As per Figure

2, Barrett makes a clear summary. It had seven meetings of the Board that consist of nine members, of which five are independent (and non-executive).

Figure 2 Barratt's Table Describing the Board's Engagement

Table 1 – Board Membership and attendance to 30 June 2018

Member	Role	Number of meetings attended
John Allan	Chairman	7/7
David Thomas	Chief Executive	7/7
Steven Boyes	Deputy Chief Executive and Chief Operating Officer	7/7
Jessica White	Chief Financial Officer	7/7
Richard Akers	Senior Independent Director	7/7
Nina Bibby	Non-Executive Director	7/7
Jock Lennox	Non-Executive Director	7/7
Sharon White[1]	Non-Executive Director	3/3
Tessa Bamford[2]	Non-Executive Director	7/7

The roles of CEO and Chairmen are sperate. All these details are within Berkeley's disclosure, but they are not shown as succinctly. It had four meetings of the Board in financial 2018 with full attendance in each case. It has 16 directors, of which nine are independent (and non-executive). It also has an independent Chairman.

Figure 3 Approach to Director Independence as Disclosed in Annual Reports

Barratt	Berkeley
Their independence is of the **utmost importance** when considering the appointment or removal of Executive Directors and in the determination of succession planning for Board positions and other Senior Management roles within the Group. All Non-Executive Directors remained independent in character and judgement during the financial year, and as confirmed, as part of the conflict of interests review process, none of the Non-Executive Directors have business or other relationships with the Group (or other outside interests) that might influence their independence or judgement.	The Board **reviews the independence of Non-executive Directors on an annual** basis taking into account each individual's professional characteristics, behaviour and their contribution to unbiased and independent debate.

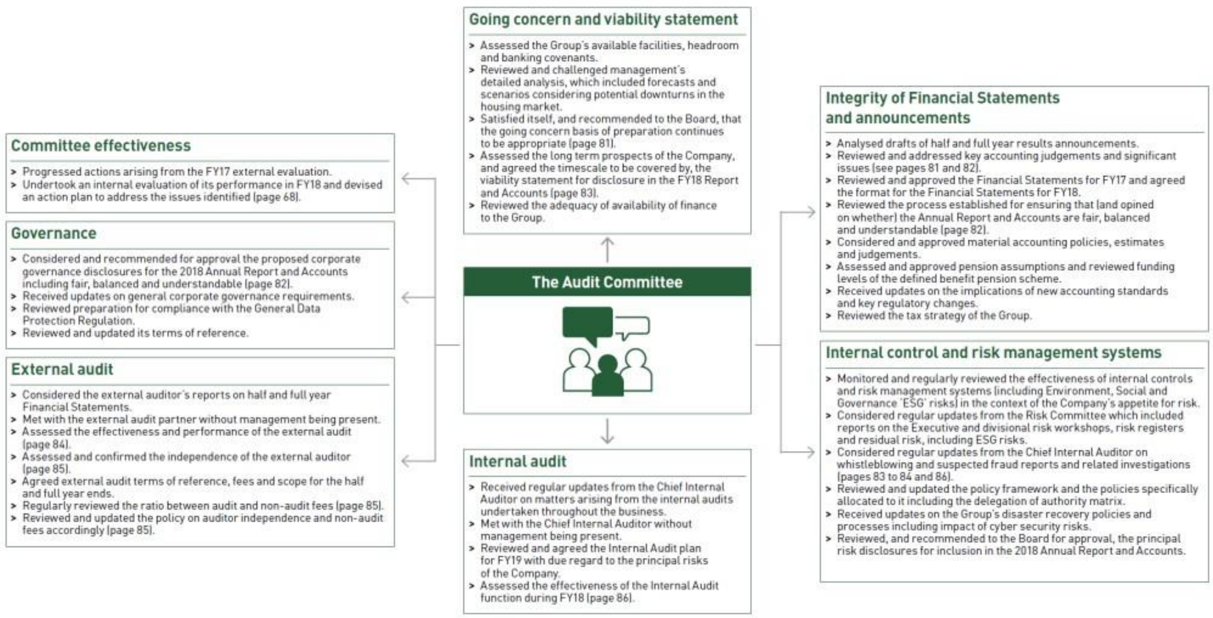
In their disclosure, the companies seem to value director independence differently. Barratt emphasises the importance it places on director independence, while Berkeley makes a note that it reviews independence on a regular basis.

Accountability

The third Principle in the Code has a very operational focus in that it contains provisions regarding risk control, internal controls, audit, and financial & business reporting. These tenants are somewhat removed from the purview of strict Governance, with the exemption of Audit Committee design and management.

Once again, in this case, the disclosure of Barratt is much more comprehensive. Berkeley's Audit Committee report covers two pages against Barratt's seven pages of disclosure. Barratt (2018) had a detailed discussion of topics such as the function of the Audit Committee (see Figure 4), "hygiene" level discussion of the Committee's membership & responsibilities, detailed & thorough discussion of the audit & auditors, which includes relevant areas that lead to a conflict of interest; as well as, novel areas such as cyber-security, EU's GDPR regulation and whistleblowing policies. Most of these topics are underdeveloped in Berkeley's disclosure and some are absent altogether. Both companies do discuss in details accounting issues that seem salient. In this case, Barratt has a discussion of inventory valuation & margin recognition and goodwill & intangible assets impairment policies. Berkeley also discusses inventory valuation & margin recognition policies, as well as accounting for provisions and recognition of revenue.

Figure 4 Barratt's Detailed Description of Audit's Committee's Processes



<u>Remuneration</u>

Given the topicality of Executive Compensation, both companies make a conscientious effort to provide detailed and comprehensive information with regards to their compensation policies. The disclosures run for about 20 pages in each case. As per Figure 5, the scope and content of discourse are similar for Barratt and Berkeley. However, the order and format of the disclosure differ somewhat. Both companies begin with a statement of the Chairmen Remuneration Committee. However, other information is usually presented in a different sequence and format. For example, Berkeley relies more on tables and charts to convey information. It has nearly 30 figures in its report against 23 figures found in Barratt's report. Also, Barratt has more disclosures with regards to the implementation of Executive Compensation. It has more details on the content and attendance of Executive Committee meetings and analysis of shareholder voting with respect to Executive Compensation.

Figure 5 Indication of Disclosure of Selected Executive Compensation Items for Barratt and Berkeley

Statement of Chairman of Remuneration Committee	Yes	Yes
Analysis of Elements of Executive Remuneration	Yes	Yes
Detailed discussion of Committee's Remuneration Policy	Yes	Yes
Description of Activity of Remuneration Committee	Yes	Yes
Discusssion of Implementation:		
Base Salary & Pension	Yes	Yes
Annual Bonus	Yes	Yes
LTPP	Yes	Yes
Tables with Single Figure Remuneration	Yes	Yes
Analysis of relative Remuneration to FTSE 100	No	Yes
Analysis of relative Remuneration to employees	Yes	Yes
Disclousre of Detailed Clawback Provisions	Yes	No

There is a significant difference in the metrics the companies use when setting Executive Compensation. Barratt focuses on total shareholder return relative to companies in the sector, earnings per share growth, and return on capital employed. Berkeley uses return on equity and net asset value growth as metrics. In my opinion, Barrett's approach is better as it incentivizes management to focus on shareholder wealth, operating growth and use of total capital. Berkeley's approach inadvertently incentivises management to take on debt, by focusing on return on equity and asset growth.

Conclusion

Both companies seem to be adhering to the Principles of the Code but differ in their approaches. Berkeley uses the Code directly from its Governance policies, while Barratt seems to have a set of internal policies that, when combined, adhere to the Principles of the Code. Nonetheless, I conclude that Barrett's Governance has higher quality and is better disclosed.

With respect to board engagement and quality, the companies also take a differing approach. Barrett has a smaller, somewhat less independent, but more active Board. Note, however, that Barratt seems to place much more emphasis on the independence of their directors. Berkeley has a less active Board, but it is bigger. It also has a much larger percentage of independent non-executive directors. Also, Berkeley's audit governance seems to be underdeveloped relative to Barratt.

With respect to Executive Compensation, both companies have high-quality policies and disclosures. However, in my opinion, Barrett's structure of compensation is superior.

[Word count: 1079]

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