BIS | Department for Business Innovation & Skills

Consultation response form: The Future of Narrative Reporting

A copy of the consultation available at: http://www.bis.gov.uk/consultations.

Responses to the Consultation by be received by 19 October 2010

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Please tick the box from the following list of options that best describes you:

	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
X	**Investor representative organisation**
	Non governmental organisation (NGO)
	Trade Union
	Lawyer or accountant
	Other (e.g. consultant or private individual)

General comment: We see that in his foreword the Minister refers to shareholders stepping up and acting as effective owners. This is usually thought of in the context of institutional investors. However, seeing that institutional performance is usually judged on a comparative basis, they have little incentive to devote the necessary resources to this end. On the other hand, we believe that progress is possible by using the knowledge and, more importantly, the independence of private shareholders, many of whom take a considerable interest in the companies in which they invest. This could be achieved through the mechanism of Shareholder Committees, as proposed by Bill Cash MP in his 'Protection of Shareholders Bill' and noted for further consideration by Lord Walker in his July 2009 review of bank governance.

Value of narrative reporting

Question 1: Are company directors providing useful and relevant information on the company's:

i) forward-looking strategy and
ii) principal risks and opportunities?

Comments
I) Varies from thoughtful and frank review of prospects and possible responses to uninformative and vague optimism unsupported by real analysis. There has been some improvement, but there remains considerable scope for more companies to take all shareholders (including private shareholders) into their confidence regarding their assessment of the competitive forces to which it is subject, its real competitive advantage and the true nature of its business franchise.
II) Again varies from a frank assessment to a formulaic listing of possible threats without a realistic assessment of probabilities. As well as numbers describing declared profits and cash generation, shareholders need to develop a deeper understanding of the factors governing success and failure in each specific company, and how the company's strategy will be adapted to cope with a range of possible developments in its business environment.

Question 2: What are the constraints on companies providing information on these issues?

Comments
i) Concerns regarding commercial confidentiality and possible undermining of competitive position. ***ii) Recognition that forward looking statements carry risks for the company and management, and fears of subsequent criticism.***

<u>Question 3:</u> Does the information provided reflect the issues discussed by the directors in board meetings?

Comments
It is not possible to answer this question adequately without broader knowledge of boardroom discussions, but a well-written report will reflect a range of possible viewpoints and assessments which should have been aired in the board room. It is essential that directors provide an assessment, in their own words, of how they see the strengths and weaknesses of the business for which they are responsible. It is not acceptable for the basic preparation of such information and analysis to be delegated to external consultants or public relations staff.

<u>Question 4</u>: Does the information help shareholders to press directors on key issues relating to strategy and risk, or inform their business decisions?

Comments
Private shareholders rely heavily on disclosures in the Annual Report & Accounts, as distinct from institutions which are able to commission supplementary research and analysis. Although private shareholders will also have access to press comment, the more experienced among them will recognise that they are primarily reliant on their own judgement and require realistic base data and other information to inform this process.

<u>Question 5</u>: If a company does not provide sufficient or material information to you, do you challenge it? Is there anything which could help you to do so?

Comments
Private investors may seek to improve the situation by direct action (sometimes through UKSA), but others will (and probably should) simply sell their shares and buy into a company which is more responsive.

<u>Question 6:</u> What other sources of company information do you use and how valuable are they (e.g. information provided on the website, analysts' briefings, dialogue with the company, corporate social responsibility report)?

Comments
Private investors do of course have some access to sources such as corporate websites, analyst research, company briefings and financial media, but most non-professional long term private investors will rely heavily on communications from the company plus, when possible, attendance at AGMs. ***Corporate social responsibility reports are seen as a useful component of the annual report, but are generally of less interest than financial results and an insight into future strategy.***

<u>Question 7:</u> Is there scope to reduce or simplify the requirements on which companies report?

Comments
i) It is worth noting that company reports are designed to a hard copy format, whereas distribution of company reports is increasingly soft copy. Soft copy material is normally screen read and rarely printed, partly due to cost constraints for smaller private investors. Thus less is being read at a time when company reports have increased markedly in size. ***ii) Private investors would mostly prefer a succinct and frank report on the progress of their investment. There is a strong argument for dispensing with inessential or highly specialist information, much of which is formulaic and of little interest to shareholders.***

<u>Question 8:</u> Is there scope to arrange the information in a more useful way?

Comments
Investors are familiar with present layouts, and significant changes might well cause confusion without compensating benefit.

Business Review

<u>Question 9</u>: Looking at an Operating & Financial Review and the existing business review (see Annex D), do you see value in reinstating elements of an OFR and if so what would they be? In particular, would a statutory reporting standard help to improve the quality of reporting?

Comments
Possibly. The objective should be to raise the standard of reporting among the tail of unresponsive companies and to ensure that accounts are comprehensible for those private shareholders who are not financial specialists (but are reasonably literate and numerate).

<u>Question 10</u>: The business review provisions require quoted companies to report, to the extent necessary, on:

- **main trends and factors likely to affect the future development, performance and position of the company's business**
- **information on environmental matters**
- **information on employees**
- **information on social and community matters**
- **persons with whom the company has essential contractual and other relationships**

i) is this information useful to you? How do you use it?
ii) Could disclosure be improved? If so, how?
iii) Are there key issues which are missing? If so, please explain?

Comments
i) ***These topics are clearly of interest to shareholders in assessing business performance (particularly the first and the fifth).*** ***ii) Clearly there is room for improvement in some cases, but research would be required before formulating specific suggestions.*** ***iii) As for ii) above.***

<u>Question 11:</u> Would more guidance be helpful? If so, what form should this take? For example, best practice example, sample Key Performance Indicators, etc?

Comments
Best practice examples might well encourage emulation (and pressure for emulation).

<u>Question 12:</u> Should there be a shareholder's advisory vote on the Business Review?

Comments
I) Yes. This would be a welcome initiative provided the Business Review was sufficiently informative.

<u>Question 13</u>: Are there non-regulatory solutions to increasing quality through better guidance or publicising excellence in business reports? If so, what?

Comments
Again best practice examples might well encourage emulation (and pressure for emulation).

Directors' Remuneration Report

Question 14: Do the current disclosure requirements provide clear and usable information about:

- **the total remuneration paid to directors, and how this is made up;**
- **the performance criteria for payments to directors, and how these relate to the company's strategic objectives;**
- **company performance against these criteria, so that there is a demonstrable link between pay and performance.**
- **the process by which directors' remuneration is decided?**

Comments
Some companies respond in a clear and open fashion. Shrewd investors will regard less frank responses with justifiable suspicion.

Costs

Question 15:

If you can provide any information on costs associated either with the existing narrative reporting requirements eg preparing your business review or your views on potential costs and benefits in relation to any of the ideas in this consultation, please give details

Comments
No comment.