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
x	**Business representative organisation**
	Investor representative organisation
	Non governmental organisation (NGO)
	Trade Union
	Lawyer or accountant
	Other (e.g. consultant or private individual)

Value of narrative reporting

<u>Question 1</u>: Are company directors providing useful and relevant information on the company's:

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

Comments
Over the last 10 years the Investor Relations Society has encouraged improvements in narrative reporting thorough its Best Practice Awards. Over this period we have seen significant improvements. The introduction of the Enhanced Business review in the Companies Act 2006 accelerated this process. We believe that the best companies are now communicating strategy, risks and opportunities in a much more joined up way. However, we think that there is still room for improvement in this area by those companies which have not yet focused on these challenges. We believe that the current framework provides all the necessary regulation to develop meaningful narrative reporting. We do not think that it would be helpful at this stage to open up the debate on changing the Business Review requirements as the current act provides substantially all that was proposed in the original OFR. We believe that a combination of peer review pressure and guidance from organisations such as the FRC, FRRP and BIS will help to push forward further improvements in this area of narrative reporting.

<u>Question 2:</u> What are the constraints on companies providing information on these issues?

Comments
In the past companies did not like talking about risk as it was perceived to be negative. However the introduction of the requirements of the CA2006 and the major problems encountered by many companies in the aftermath of the credit crisis have made companies recognise that it is important to show how they assess risk in their organisations, how it is balanced as part of the strategy of the business and what they do to mitigate it. Companies have also felt unwilling to discuss future strategy in too much detail as they are concerned that they will give away potentially useful information to their competitors. Companies have also felt constrained by the requirements to not provide profits forecasts which might involve them in additional verification work in a future M&A situation. However we believe that companies are beginning to recognise the benefits of increased transparency in reporting, which

outweigh the potential problems outlined above. We believe that more pertinent questioning from investors as part of their increased involvement through the new Stewardship Code should encourage companies to be more open in their discussion of these issues.

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

Comments
From our reviews of best practice reporting we have noted that some companies have specifically mentioned the issues which have been discussed at their Board meetings. We believe that this sort of disclosure is much more meaningful and is a welcome move away from the 'box ticking' mentality which is prevalent in some reports. Obviously we are not able to comment in detail on what is discussed in Board meetings but we believe that the process of reporting on annual basis on these issues should provide a useful focus for Board discussions.

<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
There is now a significant amount of useful information for investors which is required to be disclosed. How much use is made of this depends to a large extent on the resource which shareholders are prepared to put into assimilating this information. Through our Best Practice Guidelines and Awards we encourage companies to improve the quality of their presentation as this makes it easier for shareholders to use the information.

<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
As noted above we encourage better disclosure and transparency through our Best Practice Guidelines.

<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

We believe the website is now the first port of call for many interested parties.
We also believe that companies should be encouraged to take advantage of all communication channels.
These include meeting investors, analysts and other stakeholders, during which an investor presentation is often used. The investor presentation has a number of merits; timeliness, an 'informality' and absence of mandated structure. This allows the company's management team the flexibility to share the specific information that the investors need about *their* company. One size of information set does not fit all. Regular, timely updates are also key. Through regulatory disclosures such as half yearly results, Interim Management Statements and compliance with the DTR regime, regular updates to the company's non financial position are also provided. In addition, companies choose to update the market with non-mandated information throughout the year. This may be sales statistics, market share, production volumes etc. These are heavily used by analysts and investors.

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

Comments
We are concerned that the Annual Report is becoming a historical repository for regulators' mandated information – rather than a useful *additional* information source for the market. As a consequence of these and other changes, the required content of the annual report has grown exponentially. **We believe that the annual report is rooted in the earliest versions of the Companies Act, in a completely different information era. Changes in the 'audience' for the report, changes in investor decision making, rising focus on governance, and of course the way we consume information have made the concept of the annual report very different from its original intent. For example, as more and more companies have gradually taken up the opportunity presented by changes in Company Law to allow ecomms, fewer printed copies of the Annual Report are now necessary as investors generally look to the internet to provide far more up to date/relevant information.** **We therefore think that there is scope for putting more non-statutory information on websites to supplement the Annual Report disclosures and we think that there is a case for simplifying and reducing the amount of information that has to be disclosed in the Annual Report and placing it on the website.** **We believe that any changes should be in the form of principles based guidance and encouragement, rather than new standards or regulations. Creating a mandatory standard to be followed does not allow companies the flexibility to tell their own story, and risks a templated box ticking approach.**

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

Comments
As discussed above we think that there is scope to reduce the amount of mandated information in the Annual Report, including some of this on the website.

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
We believe that the current framework provides all the necessary regulation to develop meaningful narrative reporting. We do not think that it would be helpful at this stage to open up the debate on changing the Business Review requirements as the current Act provides substantially all that was proposed in the original OFR. We believe that a combination of peer review pressure and guidance from organisations such as the FRRP and BIS will help to push forward further improvements in this area of narrative reporting. **We believe that any changes should be in the form of principles based guidance and encouragement, rather than new standards or regulations. We are concerned that a regulatory approach may be inconsistent. The FSA Handbook regularly makes the point in its Disclosure and Transparency Rules that no two companies are the same, and consequently a principles based regulation is appropriate, rather than fixing a set of required disclosures. By contrast, the Companies Act, and the Financial Reporting Council's Reporting Standard 1, creates a 'standard' – regardless of whether the content of that standard is relevant or not.** **We therefore believe that creating a mandatory standard to be followed does not allow companies the flexibility to tell their own story, and risks a templated box ticking approach.**

<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
We have no specific comments to make on this question as it is mainly directed at users of accounts.

<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
We believe that a combination of peer review pressure and guidance from organisations such as the FRC, FRRP and BIS will help to push forward further improvements in the area of narrative reporting.

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

Comments
We do not believe that adding to an already crowded AGM agenda by including an advisory vote on the Business Review would make a difference to the quality of narrative reporting.

<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

Over the last 10 years the Investor Relations Society has encouraged improvements in narrative reporting thorough its Best Practice Awards. Over this period we have seen significant improvements. We believe that a combination of peer review pressure and guidance from organisations such as the FRRP and BIS will help to push forward further improvements in the area of narrative reporting.

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
The UK's statutory disclosure requirements on directors' remuneration are amongst the most extensive in the world. We believe that presentation of this information is however of variable quality. In the best companies we have seen good linkage between performance and pay, but in others there is room for improvement. **We do not believe however that this is a case for more disclosure, rather better disclosure, and that this will be driven by peer group pressure and guidance rather than additional regulation.**

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

Costs of preparation are an obvious concern for all companies. By simplifying the guidance on what companies should include, regulators would encourage companies to invest more on those areas that matter to them and to their stakeholders.

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