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

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## 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 |
| --- |
| Based on our extensive experience working with preparers of annual reports:<br><br>**(i) Forward-looking strategy**<br>Most companies attempt to communicate their strategy, although companies often confuse strategies (the means by which you intend to achieve your objectives) – with the objectives themselves.<br><br>**(ii) Principal risks and opportunities**<br>Most companies struggle to provide useful and relevant information on their principal risks and opportunities. There are three regulatory influences on UK risk reporting: ASB guidance (explaining the requirements of the EU Accounts Modernisation Directive regarding risk reporting) IFRS7 (which requires an analysis of the risks inherent in financial instruments) and – for companies who qualify as a Foreign Private Issuer in the eyes of the Securities and Exchange Commission (SEC) in the US, SEC guidance on risk reporting. As a result, few companies are willing or able to properly identify which risks are principal, to provide any context for those risks or to give any meaningful information on how risks are mitigated.<br><br>Please see our web report www.addison.co.uk/riskybusiness for more information. |

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

| Comments |
| --- |
| The greatest block to effective narrative disclosure comes from the growing development of a compliance-only mindset in companies. The more legal requirements are placed on companies, the more the company will take a legal mindset when considering how to comply. Placing more regulatory requirements on companies' narrative reporting, particularly in terms of their social and environmental obligations, will only increase the tendency for companies to restrict their disclosure only to what is required of them. |

**Question 3: Does the information provided reflect the issues discussed by the directors in board meetings?**

| Comments |
| --- |
| We are not in a position to answer this question. |

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

| Comments |
| --- |

We are not in a position to answer this question specifically as shareholders, but we believe that shareholders already have numerous opportunities to press directors on key issues, or inform their business decisions, outside of the annual report. Instead, shareholders gain most of this information from quarterly, interim and annual results presentations, as well as frequent investor presentations and meetings with management.

**Question 5: 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 |
| --- |
| We are not in a position to answer this question as a shareholder, however we do challenge the companies we work with to include all material information. Similarly, opportunities do exist for shareholders to challenge the effectiveness of information provided – please see our answer to question 4. |

**Question 6: 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 are not in a position to answer this question as a shareholder. However, as an organisation that occupies a leading role in advising companies on corporate reporting, we believe that all sources of company information have value, and that it is not possible to form an accurate view on the performance, position and prospects of an organisation from the annual report alone. |

**Question 7: Is there scope to reduce or simplify the requirements on which companies report?**

| Comments |
| --- |
| In our view it would be helpful to remove the final paragraph in Section 417 (5), which states:<br>'If the review does not contain information of each kind mentioned in paragraphs (b) (i), (ii) and (iii) and (c) (environmental matters, employees and social and community matters), it must state which of those kinds of information it does not contain.'<br><br>Requiring companies to 'disclose what they have not disclosed' is fussy and unnecessary. In our view this encourages reporting for reporting's sake, rather than because there is something important to communicate. |

**Question 8: Is there scope to arrange the information in a more useful way?**

| Comments |
| --- |
| We believe that each company is different and it is for them to decide how to present the information. It is important that all current or proposed narrative regulation allows for this flexibility. |

## 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 are confused about the references to 'an' OFR. We are only aware of one OFR, which the ASB currently provides as a statement of best practice.<br><br>We do not think that the reinstatement of this - either in its entirety or certain elements of it - as a mandatory requirement is necessary or helpful.<br><br>If an alternative OFR is being considered, we would need to know its proposed content and regulatory status before we could comment further. |

**<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 |
| --- |
| In our view:<br><br>• A discussion of trends and factors is important information as context for understanding the rest of the annual report<br><br>• As noted in the answer to question 7, environment, employee, social and community matters should be reported only when they are material to a company – it is not practical or desirable for companies to have report on every one of these aspects<br><br>• We do not believe that there are any key issues which are missing from the business review provisions |

**Question 11: 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 can be helpful, as long as they are not seen as a template for all companies to follow. We do not support the development of sample Key Performance Indicators as these can often end up being seen as required KPIs. |

**Question 12: Should there be a shareholder's advisory vote on the Business Review?**

| Comments |
| --- |
| No. The recent changes to the UK Corporate Governance Code, whereby it is recommended that the directors of FTSE 350 companies should be subject to annual re-election, should introduce sufficient accountability. |

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

| Comments |
| --- |
| Yes, there are non-regulatory solutions to increasing the quality of narrative reporting. In particular the work undertaken by organisations such as ourselves, for example our *Risky Business* publication mentioned in answer to Question 1, champions high quality narrative reporting.<br>(Please see www.addison.co.uk/riskybusiness for more information)<br><br>We would not support the convening of an expert panel to rank company performance as suggested in paragraph 30 of the consultation document. There are numerous existing rankings and awards programmes that identify and champion best practice. |

## 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 |
| --- |
| Best practice remuneration reports will already contain the information set out above. However, remuneration reporting is another area where we experience significant involvement from the lawyers, who adopt more of a compliance mindset then seeking to communicate. |

## 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 |
| --- |
| Time and effort put into preparing an annual report are already significant. Adding further requirements will lead to an increase in costs as these are addressed, particularly in the first year. In addition we are concerned that any new requirements would lead to more of a compliance approach to reporting rather than seeking to communicate with users, which must be the primary objective.<br><br>Additionally, the desirability of further regulations covering the annual report need to be seen in the context of the changing status of the document in digital corporate communications. Please refer to our covering letter for more information. |