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**The Future of Narrative Reporting – A Consultation**

The Department for Business, Innovation and Skills is currently undertaking a consultation on the Future of Narrative Reporting. In the foreword to the consultation, the Minister for Employment Relations, Consumer and Postal Affairs lists three key objectives for the consultation: to drive up the quality of corporate reporting, particularly on social and environmental issues, empower shareholders to act as effective owners of the companies they invest in, and achieve coherence without increasing the regulatory burden on companies. The foreword goes onto to confirm that the reinstatement of a mandatory Operating and Financial Review is central to achieving these aims.

However, the question of whether further legislation is required to improve the quality of companies' disclosure, and whether the reinstatement of the Operating and Financial Review is the right way to achieve this, needs to be seen in light of three key issues currently surrounding UK corporate reporting.

**1. The environment in which corporate reporting takes place has changed significantly since the last round of legislation covering narrative reporting**

The Companies Act 2006 introduced changes to the way in which companies publish and distribute their annual reports, paving the way for a rapid increase in online corporate reporting. Companies now make the annual report available on their website alongside other corporate information that is subject to different regulations, or in many instances not regulated at all. This has started to significantly alter the status of the annual report. Whereas it was once the preeminent source of information about corporate performance, its usefulness is now diminishing. For example, when the annual report is published on the company's website, the Directors' Remuneration Report is the only substantial piece of information that has not already been published on that site. All new regulations covering the content of the annual report need to take this change into account.

**2. Concerns have been expressed that UK narrative reports currently contain too much 'immaterial clutter.'**

The Accounting Standards Board (ASB) periodically reviews the standard of narrative disclosure by UK companies. In 2009 a report was published, entitled 'Rising to the challenge – a review of narrative reporting', in which the ASB expressed concerns about narrative reporting in two broad areas: the extent to which companies were effectively complying with existing regulatory guidance, and the extent to which annual reports were becoming difficult to use due to the inclusion of 'immaterial clutter'. In the review, the UK's principal regulatory body for corporate reporting largely declared

companies' compliance with existing regulation to be work in progress. It is difficult to see how the imposition of further regulation can improve this situation.

**3. The greatest block to effective narrative disclosure comes from the development of a compliance-only mindset in companies**

More legislation does not equal better disclosure. The more legal requirements are placed on companies, the more they take a legal mindset when considering how to comply. Increasing the regulatory burden on companies' narrative reporting, particularly in terms of their social and environmental obligations, will only exacerbate the tendency for companies to restrict their disclosure only to what is required of them.

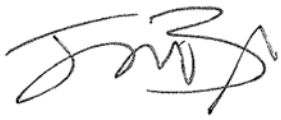
The desire to hold companies to account for their obligations towards society and the environment is legitimate, as is the expectation that corporate disclosure concerning non-financial matters should be of equal interest to shareholders and other parties.

But in a rapidly changing environment for corporate reporting, it would be a missed opportunity if regulators continued to see the annual report as the most effective vehicle for communicating these activities, for these reasons: as audiences increasingly turn to the website as the primary means of accessing key corporate information, so the relative importance of the annual report is diminishing; as the quality and accessibility of information found outside the annual report increases, so the growing complexity and size of company reports makes it harder for users to easily extract useful and relevant information from it, and; as the regulatory burden on the annual report continues to grow, so companies are resorting to a narrow, legalistic approach to disclosure, designed more to protect the company from potential legal action than communicate meaningfully with shareholders.

We do not believe that incremental regulation will have a positive impact on the quality of narrative reporting by UK companies. Instead, regulators should take this opportunity to address the relevance and applicability of all corporate reporting legislation, in light of the rapid and significant changes to corporate disclosure brought about by the Internet.

Finally, we do welcome the desire to explore non-regulatory options for improvement. However, we recommend that the many ways in which best practice reporting is already encouraged and promoted – through guidance, research, rankings and multiple award programmes – are taken fully into account before further activity is countenanced.

Yours sincerely



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