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
X	**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
Listed companies are providing useful information on their forward-looking strategy and principal risks and opportunities but the quality of narrative reporting in these areas is variable and there is scope for enhancing it in some instances. **On risks and opportunities, some boards could improve the linkage in their annual reports between their principal risks and how they are being managed whilst in some other instances a clearer distinction between principal risks and other risks would be helpful.**

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

Comments
The constraints would include: - **absence of a clear strategy or of high quality information on risk,** - **insufficient focus on high quality reporting leading to relatively poor disclosures** - **fear of litigation, especially if the company has a US listing, eg leading to a tendency to list many risks** - **commercial confidentiality concerns leading to vagueness on future strategy** - **a consciously emergent strategy making the discussion of future strategy inherently very tentative.**

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

Comments
It should do but the extent to which it does in the case of a particular company will depend on the extent to which some of the issues discussed in the response to Question 2 are present. **Concerns are sometimes heard that the principal risks identified by some companies are fairly generic with regards to the industries or markets concerned and that there is scope for them to be more company specific. That said there are some natural limits to the extent of disclosure, for example if there is concern in the marketplace on the quality of some members of the management team it would be hard realistically to expect this matter to be disclosed as a risk whether or not there had been board or committee discussions of it.**

<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
If the information is of the appropriate quality it clearly will assist shareholders in asking directors questions on key issues relating to strategy and risk.

<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 auditors our formal responsibilities are limited to reviewing whether any information in the narrative part of the annual report is inconsistent with that in the financial statements. This naturally does not preclude us from making suggestions to the client on information contained, or not contained, in the business review, corporate governance or directors' report. **There are currently suggestions that information contained in the business review, or part thereof for example in relation to future strategy and risk management should be subject to a fuller degree of assurance. We believe it would be helpful to further explore these issues with shareholders, especially institutional shareholders, and to ask them what form of additional assurance, if any, they would find valuable and whether the benefits they would gain would justify any additional costs involved.**

<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
There are plenty of other sources of information on companies, a number of which are set out in the question. Depending on the circumstances, they will be of varying degrees of relevance and reliability to shareholders.

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

Comments
We broadly support the current requirements and the differentiation in them that is drawn between fully listed and other companies.

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

Comments
This question alludes to a very important issue for discussion, namely that the quality of reporting depends on the presentation and ordering of information as well as the fact that particular information is included. **There has been a strong tendency in recent times to focus on the provision of necessary information and rather less on how presentation and ordering can have a significant impact on the messages conveyed. For example, if important information is concealed among voluminous disclosures of less relevance, key messages may be hidden. We therefore support FRC's project on reducing complexity and clutter in annual reporting.** **A full review of which information should be required to be published in the annual report and which may be provided by way of the company's website is also long overdue.**

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
For fully listed companies the Companies Act 2006 reinstated much of that which was lost when the OFR was originally replaced by the business review and the last redraft of the UK Code on Corporate Governance now calls on listed companies to disclose their business model. **On cost/benefit grounds, we do not on balance see merit, especially at this stage in the economic cycle, in reintroducing the above requirements for other companies, eg AIM-listed companies and private companies required to prepare a business review.**

<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 believe this information is generally useful to readers of annual reports .

As previously discussed, the quality of disclosure provided does vary between companies and so the issue of whether improvements could be made in disclosure will need to be looked at on a company by company basis.

We are not aware of any key issues that are missing from disclosure requirements when one has regard also to the UK Code on Corporate Governance for listed companies.

<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 do not believe there is a need for more statutory guidance **There may be merit in the development of a Reporting Standard or alternatively non-mandatory guidance on the business review, including the enhanced disclosures for quoted companies. Such a standard would have significant regard to the content of the existing Reporting Standard on the Operating and Financial Review.**

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

Comments
We would, in principle, support a shareholder's advisory vote as it would increase the attention paid by investors, and in particular institutional investors, to the information contained in the Business Review if they were asked to vote on it. The views of shareholders would be very important on this matter.

<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
We also support best practice guidance, probably from the FRC, based on reviews of annual reports of listed companies. **In addition, there is scope for an authoritative set of awards for high quality reporting, including narrative reporting, especially with respect to that by listed companies.** **We are not persuaded of the merits of generic lists of, for example, KPIs. There will be a risk that they will be adopted as a standard list of measures whereas we believe those reported on should be company-specific and based on the measures actually used by the board and management to steer its business.**

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 current arrangements with regard to director's remuneration seem broadly to be working satisfactorily and we would not propose changing them at present.

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
We doi not have any such information readily available.

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