The Chartered Governance Institute

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Governance Institute

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The Future of Corporate Reporting
Financial Reporting Council
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Dear Sirs

Discussion paper on the Future of Corporate Reporting

We welcome the opportunity to comment on the FRC's proposals for the future of corporate reporting.

As you know, the Chartered Governance Institute is the professional body for governance. We have members in all sectors and our Royal Charter purpose is to lead 'effective governance and efficient administration of commerce, industry and public affairs'. With more than 125 years' experience, we work with regulators and policy makers to champion high standards of governance and provide qualifications, training and guidance. The Institute is the professional body that qualifies Chartered Secretaries and Chartered Governance Professionals, which includes company secretaries. Company secretaries have a key role in companies' governance arrangements including corporate reporting. Our members are therefore well placed to understand the issues around corporate reporting and the practicalities of producing corporate reports.

In preparing our response we have consulted, amongst others, with members of the Chartered Governance Institute's Company Secretaries Forum, a group of company secretaries from more than 30 large UK listed companies from the FTSE 100 and FTSE 250. However, the views expressed in this response are not necessarily those of any individual members of any of this group, nor of the companies they represent.

Our views on the proposals set out in your discussion paper are set out below.

General comments

We support the FRC's initiative to undertake a comprehensive review of corporate reporting as we do believe that the current format and content of the annual report is in need of improvement. We also support the FRC's aim of replacing the existing corporate reporting requirements with a model that can be adapted and provide for continuous improvement in future years. However, we have a number of observations about the proposed new model, which we have set out below in our response to the questions in your discussion paper.

1. What are your views on our proposals as a whole? Are there elements that you prefer over others?

We understand the reasoning behind the proposal to separate the annual report into an integrated network of three shorter, more focussed reports to address the needs of different users of the annual report. The idea does, on the face of it, appear attractive. We also understand the desire to provide flexibility for readers to consume whatever information they wish. However, the annual report has always been regarded as the one place where all information about a company can be found and this would be lost if the report was divided in the way suggested. Information will inevitably be missed by a reader of an individual report.

We also believe the flexibility provided by the proposed model would be limited. For the reasons discussed in our response to question 2 below, it would be necessary to have one single publication date for all three reports, so many of the supposed advantages of separate reports would be lost. The report would simply become a three-volume document rather than a single document. Inevitably there would be a level of duplication with three separate reports as there would need to be elements of repetition to enable each standalone report to make sense. This would increase the volume of reporting overall. Cross-referencing to other reports will not be sufficient as this only works within a single document. We support the idea of 'digital by default' but digital does not work for everyone. Digital solutions such as 'tagging' would certainly help when reports are accessed digitally, but not when reports are accessed in other ways such as 'hard copy'. As a consequence, reports would need to be drafted without the assumption that additional 'tagged' information was available to the reader.

We would also point out that the proposal to require three separate reports runs counter to the integrated reporting initiative of recent years, which many companies have been striving to achieve and is likely to increase costs for smaller companies.

As an alternative, the FRC way wish to consider dividing the report into two separate sections with one section comprising the statements and disclosures that are required to be reported each year under legislation or regulation (such as the current Directors Report), and a separate section for the elements of reporting which tell the company's 'story' and discuss the past year. We believe this would result in a more concise, meaningful report which would be easier for the reader to navigate and understand.

Implementation

2. What do you see as the key practical challenges of implementing our proposals? Do you have any suggestions on how these could be overcome? What do you see as the costs and benefits of the new model?

As highlighted in our response to question 1, it will be necessary for all three reports to be published at the same time. This is important both from the perspectives of the reader and the preparer of reports. It is essential to investors that there is a regular reporting cycle and this would therefore need to be retained. Preparers would need to publish all three reports together to achieve cohesion, consistency and connectivity between the reports, and to avoid a continuous cycle of reporting by companies running throughout the year.

There is currently an established governance structure and process for the annual report as a whole. It is not clear what governance process is envisaged for three separate reports but there needs to be one process for the whole annual report, whether it is in one part or three, with board approval and 'sign off' at a single point in this process. By separating the reports, there is also a risk that the financial statements would become the priority over non-financial reporting because the financial statements are the most important aspect of reporting for many investors. This would frustrate an aim of the proposals, which is that the reports should be of equal standing.

There also needs to be more clarity as to where the current corporate governance report would sit within the three separate reports. This is an important element of corporate reporting and it covers much of the content of both the new Business Report and the new Public Interest Report.

Once there is an agreed approach to the future of corporate reporting, we believe it is important that there is a clear timetable set for implementation. Companies will need sufficient time to prepare for these substantial changes to reporting. The timetable will need to include an implementation deadline, a 'go live' date and examples of good practice will need to be provided for each of the new reports. There also needs to be a detailed list of content requirements for each report.

Annual General Meeting

A separate, practical point is how the proposed reporting would meet the requirements of the Annual General Meeting and we are not convinced the requirements of the AGM have been taken into account when considering the proposals for the future of corporate reporting. All three of the new reports would need to link with the AGM as various elements of all companies' annual reporting need to be put to shareholders for approval. There would need to be clarity over which parts of each report would be required to be put to shareholders, and when. All three reports would need to be published during the first few months after a company's year-end in order that sufficient Notice can be given of the AGM and the resolutions to be put to the meeting.

Objective-driven

3. Should corporate reporting focus on a wider group of stakeholders through multiple objective-driven reports, instead of a primary user focused approach?

We are concerned about the increased level of focus being given to a wider range of issues and a broader group of stakeholders. The discussion paper indicates that only 51 per cent of respondents had any interest in reading sustainability reports, and that a substantial minority of 49 per cent have no interest in such reports. We are concerned that undue weight may be given to reporting on matters that almost half of the users of reports do not appear to support and that companies will be spending significant time reporting on matters of little interest, rather than focusing on matters that are of interest to all.

We are also concerned about 'scope creep' in relation to the Public Interest report. We fear that companies will be required to report to an increasing number of stakeholders, leading to more extensive reporting or additional reports. Hence the importance of a detailed list of content requirements for each report.

One set of principles

4. Do you consider the set of principles (system level attributes, report level attributes and content communication principles) in section 2 would be helpful in improving the quality of corporate reporting today and in the future?

No, not on their own. Principles can be helpful as a guide and can support the understanding and interlinking of reporting, however we believe that principles alone without guidance, clarity and regulatory oversight are unlikely to improve the quality of reporting.

Reporting network

5. Do you agree with our proposals to improve the relevance and accessibility of information, involving more concise reports distributed across a reporting network?

Please see our comments on a network of reports in our responses to questions 1 and 2.

Materiality

6. We are proposing that there should no longer be a single test for materiality that is based on accounting standards but instead materiality will be dependent on the objective of a report. Do you agree with this approach, please explain why?

Yes, but guidance will be necessary. Without sufficient guidance as to the interpretation of materiality, we believe there is a risk that insufficient information will be provided in reports.

Non-financial reporting

7. Do you believe that there is a need for regulatory standards for non-financial reporting? If so, what do you consider the scope of the information that should be covered by these standards?

Yes. It would be helpful to use the proposal for a Public Interest Report to drive some consistency around requirements for non-financial information. There is currently no standard approach as for example exists with the UK Corporate Governance Code. We believe this would be particularly helpful in achieving the aim of increasing the standards of non-financial information to the same level as required for financial information.

Currently companies are inundated with requests for various types of ESG information from investors and other interested parties. These information requests are not confined to climate change reporting but include a wide range of issues including diversity and other aspects of social responsibility. The increasing number of ESG initiatives in the EU is also influencing requests for information in the UK and these requests for information are becoming very difficult for companies to manage. Institutional investors are all competing for ESG investment by differentiating their offering, which also increases demand for information and poses a further challenge for companies. Reporting against a set of Principles and Provisions similar to those set out in the UK Corporate Governance Code would be useful, together with clarity as to the level of granularity required in reporting. We would also support a set of global standards for ESG against which companies could report

In addition we would highlight the need for better alignment with other reporting requirements and communication with shareholders, including the output from the Brydon review. It is essential that there is greater clarity over which information should be subject to audit, to assist preparers of reports in deciding what should be included, and where. It will also be necessary for government to align other reporting such as Modern Slavery statements. The Modern Slavery statement is required to be prepared as at 31 March each year and, with very many companies having a 31 December year-end, requiring these companies to include a Modern Slavery statement dated the previous 31 March is unhelpful for both the companies and readers of their reports.

8. Do you agree with the need for companies to provide information about how they view their obligations in respect of the public interest?

Yes, but we would expect the guidance to establish clearly what information is expected here in the same way that the provisions of the UK Corporate Governance Code identify the factors that are likely to indicate compliance with the principles.

9. Do you agree with the introduction of a Public Interest Report and the suggested content as set out in Section 6?

In principle, yes, but we are concerned that the content of a Public Interest Report discussed in section 6 does not reflect the type and volume of information that is being requested from companies, as described in our response to question 7. It would be helpful to use the proposal for a Public Interest Report to drive some consistency around non-financial information requirements.

Technology

10. Do you see any other ways that current and new technology could be used to facilitate the proposed model, and support the system level attributes of corporate reporting identified in section 2?

No. Our only observation would be to comment that although the move to a ‘digital first’ approach will be welcomed by many ‘professional’ users of annual reports, there remain many who prefer to work with paper and their needs should not be disregarded.

Proportionality

11. Do you agree that the model we propose will achieve a proportionate reporting regime for companies of different sizes and complexity?

We believe that this needs more research. Back in 1992, companies were permitted to publish a summary financial statement and send it to those shareholders who had not requested a copy of the full annual report and accounts. For some larger companies – in particular those with larger registers of shareholders - it was viable to produce a summary financial statement and ‘the rest’ of the annual report as separate documents, but for most the summary financial statement and the full annual report were separate documents, with associated duplication and cost, albeit it reduced postage costs. For many smaller companies, the most cost-effective solution was to continue to produce one full annual report and send it to everyone. We are concerned that the cost burden of the model that you propose might fall disproportionately on smaller companies.

Other

12. What other areas do you see being necessary or relevant to the development of a model for corporate reporting that is fit for the future?

We believe it is important there should be a degree of consensus amongst regulators and investors as to the information that needs to be reported by companies. We do not subscribe to the idea that reporting obligations should be imposed on companies simply because one or two investors or other stakeholders would like to see particular information disclosed. It would be helpful if requests for additional reporting outside that which is already required included an explanation as to why the information is considered necessary and, more importantly, that a detailed cost/benefit analysis should be applied to any new requirements.

It would also be helpful were all existing reporting requirements subjected to a similar cost/benefit analysis. One of the simplest ways of making corporate reporting more fit for the future would be to remove redundant reporting requirements.

As discussed earlier under our response to question 7, we would emphasise the need for government to align other reporting requirements in order to achieve cohesion, consistency and connectivity in reporting.

If you would like to discuss any of the above comments in further detail, please contact me.

Yours faithfully

Peter Swabey
Policy & Research Director