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Jane Leavens
Corporate Law & Governance Directorate
Department for Business, Innovation and Skills
1 Victoria Street
London
SW1H 0ET

By email: narrativereporting@bis.gsi.gov.uk

Dear Jane

THE FUTURE OF NARRATIVE REPORTING – A CONSULTATION

The ICAEW is pleased to respond to your request for comments on the consultation document *The Future of Narrative Reporting.*

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

John Boulton ACA
Technical Manager, Financial Reporting Faculty

The Institute of Chartered Accountants in England and Wales
Chartered Accountants' Hall
Moorgate Place London EC2R 6EA UK
icaew.com

T +44 (0)20 7920 8100
F +44 (0)20 7920 0547
DX 877 London/City

ICAEW REPRESENTATION

THE FUTURE OF NARRATIVE REPORTING – A CONSULTATION

Memorandum of comment submitted in October 2010 by the ICAEW, in response to the Department for Business, Innovation and Skills (BIS) consultation *The Future of Narrative Reporting* published in August 2010.

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INTRODUCTION

1. The ICAEW welcomes the opportunity to comment on the consultation paper *The Future of Narrative Reporting* published by the Department for Business, Innovation and Skills.

WHO WE ARE

2. The ICAEW operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, we provide leadership and practical support to over 134,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. We are a founding member of the Global Accounting Alliance with over 775,000 members worldwide.

3. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. We ensure these skills are constantly developed, recognised and valued.

MAJOR POINTS

High quality narrative reporting enhances company financial reports

4. We support the government's objective of driving up the quality of and improving coherence in narrative reporting. The need for contextual and forward-looking narrative reporting has increased in recent years. The credit crunch and recent market turmoil in particular have been reminders of providing sufficient insight for shareholders and potential capital providers into corporate performance and the longer-term sustainability of businesses. Our recent response to Tomorrow's Company (ICAEW REP 94/10) on their consultation *Tomorrow's Corporate Reporting* summarises our views on how we believe corporate reporting could best develop. A copy of this representation is attached as an appendix to this letter.

Significant progress has already been made in improving narrative reporting

5. We applaud the significant efforts made by many companies to provide high quality narrative reports, which often go far beyond the requirements of the Companies Act 2006. There are many examples of outstanding transparency in UK corporate reporting, one example being those companies celebrated by PwC through their annual Building Public Trust awards.

6. We are also appreciative of the significant progress made by regulators in recent years towards this objective and believe that we are starting to see the fruits of these endeavours in the form of continuing improvement to narrative reporting. Since October 2007 UK quoted companies have been required to comply with the enhanced narrative reporting requirements of section 417(5) of the Companies Act 2006. This includes the requirement to disclose information about environmental, social, community and employee matters to the extent that these are relevant to meet the objective of the business review, which is to demonstrate how directors have met their duties under section 172 of the Companies Act 2006, to promote the long term success of the business for the benefit of shareholders as a whole. More recently the remit of the Financial Reporting Review Panel (FRRP) was extended to include these disclosures in its review of company accounts, and the first results of this extended exercise were seen during its most recent review cycle.

Quality narrative reporting is bespoke to a company's circumstances

7. It should be recognised that narrative reports differ from other information in the financial statements in that their form and content is much more variable based upon the circumstances of the company and the judgments made by management. Indeed the value of narrative information is directly derived from its bespoke nature. Whereas financial information may benefit from being communicated in a standardised format (for example the familiar fixed assets table), such standardisation in narrative reporting invariably results in 'boiler-plate' disclosures of little value for users.

The UK has an effective framework for narrative reporting

8. In our view, the solution to the improvement of narrative reporting will not be in the form of increased regulation. Increased prescription, which must necessarily be generic, is very likely to lead to increasingly generic 'boiler-plate' descriptions. This reduces the quality of narrative reporting. Further, in this judgemental, bespoke context, where companies need to develop their own communication style, stability is particularly important. Rather we are supportive of the current position. We believe that the provisions of the Companies Act provide an appropriate legal framework, based on the section 172 duties, which focuses on the success of the company for the benefits of the shareholders, while taking account of wider stakeholder interests when these are relevant to that long term success. This legal framework is helpfully supplemented by non-mandatory guidance in the form of the Accounting Standards Board's Reporting Statement *Operating and Financial Review*. The work of the FRRP is also important in providing an external incentive for companies to make effort to improve their reports whilst not acting as a deterrent against those companies seeking to present information in more innovative ways. This framework combines statutory, regulatory and non-mandatory guidance in a well-balanced and effective manner and is fit for purpose. (The requirements in the Listing Rules are judged to be broadly consistent with the legal requirements, although duplicative for UK companies.)

9. While we applaud the generally high standard of narrative reporting by UK companies, we do accept that the risk disclosures made by banks in the years before the financial crisis could have been more far reaching in their consideration of systemic risks and their possible effects on the business. Therefore we would welcome further evaluation of the risk disclosure requirements to determine whether systemic issues could be more completely addressed.

THE QUALITIES OF GOOD FINANCIAL REPORTING

10. Notwithstanding our view that current requirements provide an adequate framework for narrative reporting, we acknowledge that there are certain areas in which those requirements can act as a barrier to effective communication or could be streamlined. The FRRP set out in their 2010 annual report a number of features that they believe make for good reporting. We strongly agree with these features and believe that they may be applied to narrative reporting. We have selected below three of their headings which we believe are particularly illustrative of how companies can improve the quality of their narrative reports with no changes required to the existing regulatory framework:

A single story

11. The FRRP, in its 2010 report, stressed the need for consistent messages within the annual report, i.e. the same story should be told throughout. We believe that it may be possible to go further that this: the interests of users are best served where communication is approached holistically, such that information on a particular topic or item is grouped together in one place. To achieve this objective, there needs to be clarity about what belongs in the notes to the financial statements (information that is essential to an understanding of the elements of the financial statements, as well as the fair presentation of the entity's financial position, performance and cash flows) and what represents narrative reporting (information that places the results and financial position in context). Without resolving this question, there is a risk that the volume of disclosures may continue to grow with no improvement, or perhaps even deterioration, in the clarity and coherence of the annual report.

12. Overlap currently exists between the type of information that is disclosed in the notes to financial statements and that which is included in narrative reporting. For example, certain information on financial risk is required to be disclosed by IFRS 7 *Financial Instruments: Disclosures*, but is also likely to be included in narrative reporting. In our view, limiting this overlap is strongly desirable and will greatly assist in the representation of a coherent story throughout the annual report.

Consistency

13. Consistency between narrative reporting and the financial statements is also an important issue. This goes beyond ensuring that where the same numbers appear in each section they are in agreement, to a consideration of the measurement basis and terminology used. One example of where inconsistency has the potential to arise is the segmental disclosures of IFRS 8 *Operating Segments*. IFRS 8 requires the measures of segment profit or loss to be those amounts that are reported to the chief operating decision maker and used to manage the business; we would expect those same measures to form the basis for narrative reporting.

Cut the clutter

14. Good narrative reporting tells the story of the business. It is relevant. As such its volume and format should be expected to vary with the circumstances of the individual business. Reports that are padded with generic text, included with a view chiefly to satisfy regulatory requirements are unattractive and uninformative. Aside from being unwanted, such generic information detracts from the real story being told. In addition, companies should be encouraged to focus on what they perceive to be the most significant information; a list of principal risks should include the few truly important factors of specific relevance to the company and not extensive lists of generic risks applicable to any company. To facilitate the necessary focus it is imperative that management is allowed sufficient discretion; guidance should be built around core principles (already provided in the existing legislation), which gives a high-level framework to allow management to determine the most useful information to include in their narrative reporting.

SUPPLEMENTARY REPORTING

15. We strongly believe that the annual report should form a coherent stand-alone document that clearly articulates a consistent narrative demonstrating how the business achieves success in the long term, on behalf of its shareholders, as currently required in the law. Such a narrative combines both financial and non-financial information in the most effective way to convey its message. We also believe that the purpose of the annual report is to provide useful information to shareholders. We are therefore concerned that some of the non-financial information required or suggested for inclusion in the annual report is ancillary to this process. Squeezing this information into the annual report reduces its clarity and quite often deprives the information of the focus and attention it deserves.

16. Therefore we find much to support in the third bullet point to paragraph 30 of the consultation document. Limiting the narrative report in the annual report to a summary of the strategic issues is likely to increase clarity and relevance and therefore improve quality. Additionally, by allowing the presentation of more detailed information in a separate report, additional messages could be addressed more coherently and in greater depth.

17. A separate report could provide a platform for the introduction of additional information that is inappropriate in an annual report produced to primarily meet the needs of shareholders. For example, the country-by-country segmental disclosures advocated by the Publish What You Pay coalition may be considered desirable for public policy reasons, but it is not necessarily relevant to the direct financial report to shareholders. Similarly, other social, environmental, community or employee information outside the Section 172 objective of the business review, could also usefully be reported elsewhere, so as not to detract from the central messages of the annual report. Given the ubiquity of electronic communication in business today it is now feasible to publish such a separate document with equal prominence to the annual report, for example by inclusion on the company website.

RESPONSES TO SPECIFIC QUESTIONS/POINTS

1. Are company directors providing useful and relevant information on the company's:

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

18. We believe there is much to applaud in the progress that has been made in recent years in improving the quality of narrative reporting. Underpinned by the Business Review requirements of the Companies Act 2006 (CA 2006) and then the extension of the FRRP's remit to its review, we feel that there has been tangible improvement in recent years and that this is continuing.

19. We agree with the second bullet point of paragraph 30 of the consultation document. Ultimately, meaningful improvement in this area is most likely to be achieved as a result of market pressure, as those companies providing inadequate information are compared unfavourably with their peers. To this end, measures that recognise and promote good reporting, such as PwC's annual Building Public Trust awards, are likely to yield significant dividends.

2. What are the constraints on companies providing information on these issues?

20. We believe that it is important for the annual report to articulate a single, consistent narrative, which would incorporate management's view of the risks and uncertainties facing the company and the strategy they have adopted. The communication of this message is impaired where its presentation is disjointed through the haphazard distribution of its constituent parts throughout the annual report; where presentation follows the pattern of the many and various accounting requirements rather than forming a coherent whole. The picture becomes particularly blurred when disclosures are duplicated in different sections, for example the financial risks disclosed by IFRS 7 may, or may not, also feature as section 417 (CA 2006) key risks. Similarly, the messages can get confused when the same subjects are covered in a chairman's report, CEO's report, sector COO reports and so on.

3. Does the information provided reflect the issues discussed by the directors in board meetings?

21. We would prefer to re-phrase this question to a consideration of whether the information provided is a true reflection of what directors believe to be the principal issues facing the company. The answer to this question would be, yes; quoted companies do generally make significant efforts to effectively communicate both their principal risks and strategy through the Business Review.

22. Whether these issues are those discussed in Board meetings is a different question. In the case of risks this is because they can be split into two specific groups. Inherent risks are those present in the business environment in which the company operates, and over which management have little control. For an airline, the risk of aircraft failure is an extremely significant risk, although with a low probability. Stringent external regulations are in place to guard against this occurring and all airlines must comply with these. The mechanisms in place to ensure compliance are likely to be largely fixed and to involve little discretion; therefore, Board scrutiny will be focussed on compliance with external regulation, encompassing operational reports and updates on best practice. Conversely some items discussed by the Board may not be seen by some as fundamental business risks, for example risks of failure of a marketing strategy to achieve its target. Furthermore, it should be noted that the matters discussed by the Board may be rather more prosaic in reality than popular imagination may like to suggest – this expectation gap will not be bridged by the production of regulations that attempt to extract disclosure of discussions that never actually took place. Consequently we see little value in rigidly relating the contents of the Business Review to the Board agenda, when in fact what matters is the identification of principal issues facing the company, whether

discussed by the Board or not. In addition, while there may be lessons from the financial crisis on how risk disclosures are framed by financial institutions, we would be concerned that additional onerous requirements result for other corporates.

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

23. This main aim of corporate reporting is to provide information about financial position at the balance sheet date and performance over the period under review. This allows investors to assess management's stewardship of the resources under its control, and as such ensures the accountability of Directors for their past actions. The annual report is largely seen as a confirmatory document that provides information about events that have occurred in the past. Other information arguably can have a more direct role to play in meeting this need, being more timely (for example price sensitive disclosures of real-time events and trading updates).,. It is also important to recognise that, although the annual report provides details of management's policies and assessment of risk, it cannot predict the future. That said, the fulfilment of the objective of the business review according to Section 417 CA 2006 (to demonstrate fulfilment of the Section 172 duty on the Directors), does partly help the shareholders to assess how directors are dealing with strategy and risk issues.

24. The annual report is prepared for an external audience and published some time after the completion of the events to which it relates. It is not designed to inform the Directors' business decisions (if that is what is being inferred in the question) and it is unlikely that it would be used for this purpose given the availability of internal data for management purposes. That said, the annual report does have an important role in informing shareholder governance decisions and investment decisions and is effective in fulfilling this.

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?

25. We are not responding in the capacity of a shareholder and as such do not request this information from reporting entities. However, we would like to highlight here that quoted companies do have an obligation under the listing rules to disclose any information they hold that is 'likely to have a significant effect on the [share] price'[1]. In light of this requirement we are unsure as to what 'material information' a company could be perceived as withholding.

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)?

26. Company websites are being used with increasing effectiveness for the dissemination of company information to shareholders and potential investors. Indeed some companies are exceedingly good at this, maintaining well ordered, frequently updated and comprehensive online resources; award schemes are in operation to recognise company achievement in this respect. It should be noted however that a major driver of online publication is the deficiencies in the regulatory mechanism. Frankly, given the ubiquity today of electronic forms of communication it is unacceptable that the RNS system is unable to accept documents in pdf format and this is an area where the government could seek to encourage improvements.

[1] FSA Disclosure and Transparency Rules, Section 2.2

7. Is there scope to reduce or simplify the requirements on which companies report?

27. We believe that the current requirements work well in practice; the real danger is incremental regulation obfuscating the principal message relayed by the annual report. Section 417 (CA 2006), as well as including a coherent objective for the business review, contains a sensible summary of disclosures and is phrased in suitably high-level terms; we therefore would not seek changes to any of its provisions. However, we have frequently pointed out in the past that there is substantial overlap between the Companies Act 2006 requirements for the disclosure of directors' emoluments, and the requirements of the Listing Rules. Appropriate deregulation in this area would be welcome, and is overdue.

28. In addition, we believe that 'essential' in section 417(5)(c) (CA 2006) is subject to some subjectivity in its interpretation. Perhaps additional guidance on this limited point could be helpful, although this does not require any change in regulatory requirements.

8. Is there scope to arrange the information in a more useful way?

29. Notwithstanding our answer to question 7 above, we would reiterate that coherence and clarity in corporate reporting is an important issue and one on which we feel some progress could be made. Currently the various requirements relating to narrative reporting are distributed across a variety of sources (i.e. accounting standards, the law and the Listing Rules). This inevitably leads to fragmentary and duplicated disclosures that impair the annual report's ability to articulate a coherent message. A greater level of coherence between the various requirements, and in particular the mitigation of duplication, would be welcome. One example of duplication between different sets of regulations is the directors' emoluments disclosures, as noted in paragraph 27.

30. Further, we agree with the third bullet point of paragraph 30 in the consultation document which suggests that narrative reports could be condensed into a summary of strategic issues with detailed supporting information provided in the form of a separate document. Given the growth of electronic communication it is now considerably more feasible to publish such information with the same level of prominence as the annual report, for example by attaching it alongside on the company website. This may also be suited to the disclosure of environmental, social, community and employee matters, which can only be imperfectly addressed in corporate reports produced primarily as an aid to shareholder decision making. We note that paragraph 21 of the consultation document addresses social and environmental reports. As set out above, while we are supportive of the publication of this information if public policy demands it, we do not believe such information belongs in the annual report, which is published for a specific purpose.

Business Review

9. 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?

31. The information disclosed by companies to comply with the requirements of the Business Review (at least for quoted companies) is effectively equivalent with that which would be contained in an operating and financial review. Therefore, reintroducing the requirement for a mandatory OFR is likely to have little impact in practice. There is even a risk that increasing prescription in this area could be met with generic 'boiler-plate' disclosures that add no value for users of the financial statements.

32. The only operational difference we see between the two is in the nature of the audit report, which would have been more extensive for a statutory OFR. This is a separate issue beyond the scope of the current consultation. However, we do note that were our suggestions in paragraph 27 for the publication of a supplementary report to be heeded, it may be easier in

the context of this stand-alone document to address a more appropriate form and extent of assurance for a separate CSR report.

33. From a financial reporting perspective, increasing the auditor's involvement in narrative information might potentially have the value of increasing the credibility of the information.

34. However, we note the challenges that auditors might face if there is a lack of clarity as to what their responsibility would be in relation to different aspects of narrative information. In some areas, it may be sufficient to meet the needs of users by checking consistency, but in other areas, users may expect auditors to carry out more work that would give them positive assurance. For example, we observe that users are increasingly interested in sustainability and carbon emission related matters and expect auditors to carry out more work than required under the current business review. This appears to indicate that specific aspects of narrative reporting merit further auditor involvement (such as carbon emission) rather than there being a demand for a general, increased responsibility. We therefore expect more debate over what work by auditors is required on what aspect of narrative information, and whether it should be carried out within a statutory audit or should be best dealt with as a separate engagement. It is possible that auditor involvement in some areas might have the perverse consequence of inhibiting disclosures given the safe harbour provisions that are available to directors but not to auditors.

35. The consultation paper notes in paragraphs 22 and 23 the differences in the audit requirement between the proposed statutory OFR and the current business review. In practice, this does not appear to have resulted in much difference between what auditors currently do on the business review and what they would be expected to do to meet the requirements for the OFR.

10 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?

36. We are not responding to this consultation as a user of financial statements. However, in general we believe that the information contained in the business review is useful to users.

ii) Could disclosure be improved? If so, how?

37. We believe that narrative reporting in the UK currently represents a 'gold standard' that is in fact a source of comparative advantage to the UK. Therefore we feel strongly that changes should not be made to the current regime that may endanger this. Although we believe that further improvements could be made, and our views in this regard are set out in paragraphs 9 – 15 above, we do note that the standard of narrative reporting has been continuously improving in recent years. Peer based incentives such as recognition and award schemes are in our view the best solution for continuing to promote improvement. Increasing the level of regulation is likely to be counterproductive.

iii) Are there key issues which are missing? If so, please explain?

38. We do not believe that there are currently any issues missing from the Business Review requirements in the Companies Act. The requirements are far reaching and are articulated in terms that facilitate disclosure of those issues that are of particular relevance to the entity reporting. An extension of the requirements to explicitly include items that may not be of

relevance to all entities is likely to result in 'boiler-plate' type disclosures that are of little value to users.

11. Would more guidance be helpful? If so, what form should this take? For example: best practice example, sample Key Performance Indicators, etc?

39. No; increasing the amount of published guidance is unlikely to be helpful. As set out in our response to question 8 above, it is the coherence of the published materials that is key. We are particularly opposed to the publication of sample key performance indicators, which in our opinion would simply encourage generic 'boiler-plate' disclosure.

12. Should there be a shareholder's advisory vote on the Business Review?

40. No; it is unnecessary for shareholders to vote on the Business Review as they already vote on the annual report as a whole. It should be noted that although an advisory vote is required on remuneration strategy, this is an area of unique significance to shareholders as it represents their opportunity to voice their opinion on the reward that the Directors have recommended for themselves. This principle should not be extended to other areas.

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

41. We agree that championing excellence in reporting is an effective way of improving quality; a number of such award schemes are already in existence and we applaud their efforts in this area.

42. We would find it useful if BIS were to publish a list of the reports and research it reviewed in preparing this consultation. This would enable us to comment in more detail on these and to highlight any omissions.

Directors' Remuneration Report

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?**

If not, please explain including any views on how this might be improved

43. Generally we feel that standards are high in the reporting of Directors' remuneration. Certainly each of the points above is commonly adequately addressed by the information provided. The reports do suffer however from being unduly lengthy. In particular a great deal of information is required to be included on long-term incentive plans and share options. Although we agree that all of this information is useful, and would not advocate its omission, the clarity of the remuneration report could be improved were this detailed information to be contained in a separate document, leaving an overall summary in the annual report. As discussed in paragraph 27, electronic publication now makes it much more feasible to present detailed breakdowns of information in a discrete document. Were this suggestion to be taken forwards, it would need to be considered whether there were any implications for the shareholders' advisory vote on remuneration strategy.

Potential Costs

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.

44. Companies invest significant amounts both in complying with the existing narrative reporting requirements and also in providing additional voluntary information. However, it should also be noted that there are costs to shareholders too, not only in terms of the use of company money to fund these reports, but also in the time taken to analyse the annual report. A lack of coherence and excessive volume in disclosure increases these costs.

45. We have based our comments in this letter on the assumption that the proposals are intended to apply only to listed companies, although we note that the consultation document does not make this clear. Private companies, particularly those at the smaller end of the spectrum, are likely to find any change to the current regime particularly onerous and we would question whether there is any benefit to be gained by any extension of narrative reporting requirements for the shareholders in such companies.

E john.boulton@icaew.com

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17 September 2010

Our ref: ICAEW Rep 94/10

Mr Tony Manwaring
CEO
Tomorrow's Company
4th Floor, Samuel House
6 St Albans Street
London SW1Y 4SQ

By email: evidence@tomorrowscompany.com

Dear Mr Manwaring

Tomorrow's Corporate Reporting

ICAEW welcomes the opportunity to submit evidence to the Tomorrow's Company project on Tomorrow's Corporate Reporting.

ICAEW operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, we provide leadership and practical support to over 134,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. We are a founding member of the Global Accounting Alliance, which has over 775,000 members worldwide.

Our responses to the eight questions posed in the Tomorrow's Corporate Reporting call for evidence are to a large extent based on our report, *Developments in New Reporting Models*, published in 2009, of which we attach a copy. This builds on the work in our earlier report, *New Reporting Models for Business* (2003).

What are the weaknesses and strengths in the current system?

There is a statement at the start of the call for evidence that 'Corporate reporting is no longer working'. We do not believe that this claim is supported by the facts.

No doubt corporate reporting constantly needs to change to respond to changing circumstances, and no single approach to corporate reporting will be able to meet all the different needs of diverse groups of users. So it could be said that corporate reporting never has been perfect, is not now, and never will be. But the premise for Tomorrow's Corporate Reporting seems to be that the position at the moment is particularly bad – in a way that was not true, presumably, in the past. We do not see that this is the case. On the contrary, corporate reporting gives users more information, and major companies are more open now than at any time in the past. This seems to us to be progress, rather than a failure.

This state of affairs reflects a combination of market and non-market forces that contribute to the strength of the current system. While we often disagree with governments, regulators and standard setters on particular issues, we believe that in general the regulatory framework for corporate reporting is more effective at present than in the past. At the same time, the incentives for company

The Institute of Chartered Accountants in England and Wales
Chartered Accountants' Hall
Moorgate Place London EC2R 6EA UK
icaew.com

T +44 (0)20 7920 8100
F +44 (0)20 7920 0547
DX 877 London/City

managements and third parties (such as investment analysts) to provide information for investors are stronger than in the past. This in turn reflects growth in the volume and value of global capital markets, the growing number of sophisticated users, and falling costs of information production, transmission and analysis.

Some people do indeed portray this growth in information as a defect and say that it has become impossible to see the wood for the trees. While we accept that companies' communication of corporate reporting information could often be improved, we do not regard the growth in the total information available as a problem per se. Those who only want summary information are always free to restrict their reading to this. They are not obliged, for example, to read the full annual report if they find it unhelpful to do so, let alone all the other information that companies disclose. Indeed, the idea that there was once a golden age when all shareholders would happily read their way through 20, 50 or 100 page annual reports is, we suspect, a complete myth.

What are the barriers obstructing the evolution of corporate reporting?

At the moment we do not believe that there are significant barriers to the evolution of corporate reporting. It is possible to envisage a situation in which comprehensive and rigid global regulation could constitute a serious barrier to evolutionary change, but we are still some distance from that.

What solutions would you propose to rectify these weaknesses?

Governments, regulators, standard setters, and all those with a stake in the corporate reporting process need to maintain their readiness to respond to change. We do not see that any radical institutional changes are required.

To what extent is there a shared understanding about the purpose of corporate reporting and the overriding objective of reporting standards?

In our view, the key purpose of corporate reporting and of reporting standards is to provide information for investors (including creditors), to assist them both in monitoring managers' stewardship of the company and in making decisions on their investments. We believe that this priority is widely shared – for example, among the most important financial reporting standard setters. However, it is certainly not universally accepted. Some, for example, believe that promoting financial stability should be a priority of financial reporting – at any rate for banks and other financial institutions. Others believe that social and environmental reporting should be a priority or at least rank equally with the claims of investors. We do not think that it can be expected that there will ever be universal agreement on such issues.

We recognise that there may be cost savings in having a single annual report aimed at all kinds of users and that some users find it convenient to have everything in a single document. But subject to this, we believe that different information needs are best met by the provision of different reports, focused on the needs of relevant users. Financial reporting is effective as a means of meeting investors' information needs. Financial stability regulators may need rather different information. And those who are interested in social and environmental issues for their own sake, rather than from an investor perspective, may also be best catered for in separate reports. However reporting focused on the needs of different user groups evolves, it may also need to be accompanied by appropriate forms of assurance reporting, which will add to its value.

To what degree are investors, accountants, standard setters and management incentivised to engage in any dialogue about changing the reporting model?

As noted earlier, corporate reporting is constantly changing, through the actions of governments, regulators and standard setters, and as companies adjust their reporting to changing circumstances. This is an evolutionary process. The number of people who engage in discussion on this process is relatively small by comparison with the number of those affected by it, who include intermediaries in the

information chain, such as analysts and journalists. We regard this as inevitable and indeed healthy. It would not be appropriate for everybody to be incentivised to spend a lot of their time discussing 'the reporting model'. However, those who do engage in the debate, such as professional bodies and industry associations, are often speaking for larger constituencies, and there are usually plenty of opportunities for those who do have strong views to contribute to the debate.

We would also question how far it is helpful to think in terms of 'the reporting model'. The language of 'models' may be a useful shorthand to refer to how people do things, but it can also be misleading. It gives the impression that there is a single way in which businesses report information and that this is designed by someone who is responsible for 'the model'. The reality of corporate reporting is a lot more complex. We believe that corporate reporting is best seen as an evolving social institution. It evolves, as we have indicated, in response to a range of market and non-market forces. At any given time, certain aspects of it are governed by relevant laws, regulations and standards, which vary according to jurisdiction and the company's size, ownership structure, and activities. But the manner in which companies comply with these requirements differs widely, and it is important to bear in mind that a significant amount of reporting – both in the annual report and elsewhere – is in effect voluntary. There is no single template for reporting that all companies follow.

Is the level of technical knowledge and understanding of financial and non-financial information and metrics a barrier?

Different industries require different types and degrees of skill from the readers of their reporting. For example, the detailed financial instruments disclosures of a major bank would be a challenge to many users of corporate reports, as would the extensive non-financial disclosures typically made by a company developing new pharmaceutical products. This is a reflection of the inherent difficulties in understanding such businesses, not a failure of the reporting system.

But although users have different levels of expertise, the information provided to them is usually tailored to reflect this. Tomorrow's Corporate Reporting is quite rightly not focusing exclusively on the annual report as for many large listed companies this is only a fraction of their total reporting. But it may be useful to consider the annual report for a moment to illustrate our point. A relatively unsophisticated user may have no need to go beyond the highlights page and chairman's statement and to read the press coverage. A more sophisticated user may well regard 15 pages of notes on financial instruments as barely adequate. We do not see that this is a significant barrier to effective reporting. It just means that different users will look at rather different information within what is reported by the company and in terms of what is provided by third parties (the media, analysts' reports and so on). Going beyond the annual report to the full range of corporate reporting, these differences are likely to be accentuated as more sophisticated users are more likely to monitor information such as preliminary announcements and press releases and to explore the more detailed information that many companies provide on their websites.

Are the transactional, regulatory, technological and other changes as a result of globalisation creating too much complexity and change for the system to deal with?

Increases in complexity and constant change do impose costs and create difficulties, but we do not know of any evidence that the corporate reporting system is unable to cope.

Who is best placed to change the system and what is needed to help them do this?

As we noted earlier, the system is constantly changing, partly through numerous incremental developments in reporting at the level of individual companies, and we expect this to continue. We do not see that there is a need to provide additional resources or other forms of help to ensure that this process of change continues.

Please contact me should you wish to discuss any of the points raised in this submission.

Yours sincerely

Dr Nigel Sleigh-Johnson
Head of Financial Reporting Faculty