



Corporate Reporting Services

Breakfast Briefing

Corporate reporting 2013: is your company really ready to innovate?

October 2013

Who are FutureValue?

- **Our purpose**

- We exist to help companies and their stakeholders benefit from effective narrative reporting

- **Our mission**

- We aim to make the market value of listed companies a less risky and more certain proposition

- **Our aspiration**

- We aspire to establish a standard for the effective and comparable reporting of strategy and governance

- **Our strategy**

- Unimpeachable, authoritative and unique research of narrative reporting
- Professional services to help companies achieve the highest standards at lower cost

Why our perspective is different and particularly relevant

- Experienced in strategy, risk and governance
- Fluent in corporate and investor communications
- Independent, authoritative and objective
- We work with report designers and with listed companies
- Narrative reporting is our business

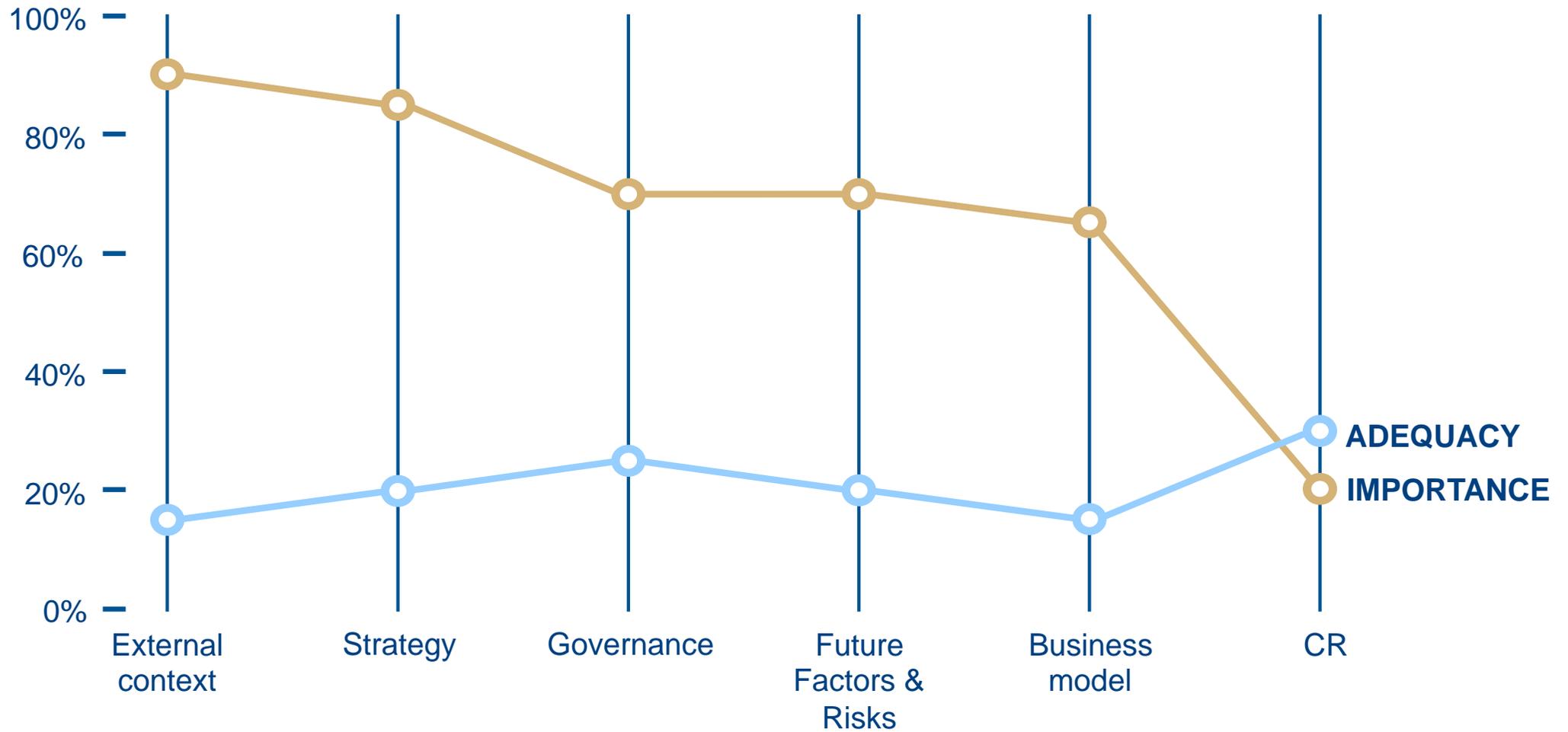
The Perfect Storm

An overview of imminent change: statutory, regulatory and voluntary

The main Annual Reporting narrative train set

- Companies Act 2006
- Large and Medium-sized Companies and Groups Accounts and Reports Regulations 2008
- Large and Medium-sized Companies and Groups Accounts and Reports (Amendment) Regulations 2013 + GC100 guidance
- Strategic Report and Directors' Report Regulations 2013 + FRC (draft) guidance
- Enterprise and Regulatory Reform Act 2013
- UK Corporate Governance Code 2012
- Listing Rules (LR) 9.8
- Disclosure Rules and Transparency Rules (DTR) 4.1
- DTR 7.1
- DTR 7.2
- Endless guidance from other interested parties

Mind the gap ...



Harmony or cacophony?

- Lack of co-ordination and orchestration
- Plenty of haste, not much speed
- Clash between commercial and political motivations
- IIRC and GRI want influence
- Government and regulators keen to see results
- Increasing pressure for regulators to get tough
- Auditor land-grab
- Business model, strategy, risk, CR disclosures and governance are “hot”

Is the regulator at odds with the aspiring global standard setter and its UK policy makers?

FRC declares <IR> draft framework has maybe *“lost its way”* on providing relevant information to investors

FRC also suggests: *“There are big challenges because there are policy makers who would suggest that the annual report and accounts are to further their policy thinking rather than serve the needs of investors”*

Business models and the Strategic Report

Ian McDonald Wood

FRC Draft Guidance to the Strategic Report

- *“The content elements for the strategic report [...] include a description of the entity’s objectives, strategies and business model ... ”*
- *“the strategic report should include an explanation of*
 - *the main trends and factors affecting the entity*
 - *a description of its principal risks and uncertainties*
 - *an analysis using key performance indicators*
 - *and an analysis of the development and performance of the business*
 - *Disclosures around the environment, employees, social issues; and diversity are also incorporated.”*

Business model – what's its purpose?

- to tell investors and other stakeholders the 'why'
- to help make investors 'more active stewards of the companies they own'
- to clarify, inspire confidence in a company's potential
- to project the quality of underlying analysis, not just present a graphic

Whose business model is it anyway?

- Strategic
 - Why entities exist and why they will continue to be profitable
- Operational
 - How businesses implement strategy; focused on outputs
- Capitals-based
 - Comprehensive economic, social and environmental overview; 'soft' outputs

Mapping the value system is the first step in the articulation of a strategic business model

Principal players

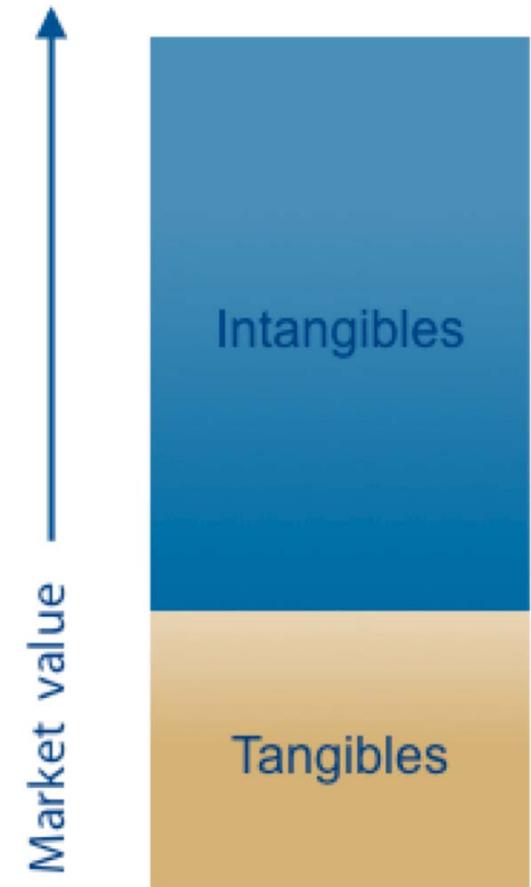


Principal processes



Why it is truly worth getting your Company's business model right

- The secret to communicating the intangible value of the company
- The key to presenting a truly cohesive story
- The foundation of an 'integrated report'
- Persuasive indicator of effective collective strategic thinking



Principal risks, uncertainties and the Strategic Report

Professor Garry Honey

Regulatory history of risk and the FRC

- 2006 Companies Act:
 - Enhanced Business Review (EBR) '... a description of principal risks'
- 2010 Corporate Governance code update:
 - 'the board is responsible for determining the nature and extent of the significant risks it is willing to take in achieving its strategic objectives.'
- 2011 Boards & Risk
 - FRC report into key reasons for inadequate risk reporting
- 2012 Corporate Governance code update:
 - 'the directors should include an explanation of the basis on which the company generates or preserves value over the longer term (the business model) and the strategy for delivering the objectives of the company.'
- 2013 Companies Act amendment - New Strategic Report:
 - 'to provide insight into the entity's main objectives and strategies, and the principal risks it faces and how they might affect future prospects.'

FRC criticism of risk reporting (2011)

- Approach to risk
 - The Board is responsible for determining the approach to risk, setting its culture, risk identification, oversight of risk management, and crisis management. It is a shared responsibility.
- Interpretation of risk
 - The Board needs to agree its appetite or tolerance for key individual risks; to understand the company's exposure to risk and how this might change..... Companies should indicate to shareholders when and to what extent they believed their exposure to risk was changing.
- Information about risk
 - Qualify why the reported risk is significant, why it represents a threat and what the organisation is doing to control this. Explain how readers will know when a risk ceases to exist and explain contingent factors that increase or decrease this risk.

Three key changes

- **Context**

- Business Model to be explained specifically linking strategy and risk

- **Category**

- Strategic risk to be reported not just operational risk

- **Control**

- Risk governance to be reported not just risk management

Context

- Risk is about future uncertainty...the probability of events occurring which impact business continuity
- Strategy is about future direction and the route chosen to achieve pre-determined goals or business objectives
- As future forecasts strategy & risk are linked ... why then have they traditionally been separated in corporate reporting?
 - Possibly because strategy copywriting talks of future positives whereas risk copywriting talks of future negatives?
 - Nevertheless, as future unknowns, how can regulators, accountants and auditors police 'estimates' which are not evidence-based?
- Strategy & risk are to be explained in tandem and within the context of the business model.

Category

Risk Type	Reporting Frequency	Control & Predict	Strategy	Examples
Market Risk	Occasional	Hardest	Mitigate	marketplace - exchange or interest rates, taxation, government policy, competitor activity, pricing, product demand etc.
Operational Risk	Regularly	Easiest	Retain & manage	business - financial, insurance, liquidity, credit, capital, project, ERM, corporate responsibility, brand activity etc.
Strategic Risk	Rarely	Difficult	Avoid or mitigate	direction - impact on chosen strategy, sustainability, <i>reputation</i> , culture & corporate behaviour, value alignments.

Principal Risk Significant Risk	Statutory requirement	Difficult	Manage	realisable value - ROI, significant to investors - share price, <i>reputation</i> etc.
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Control

- Risk governance is not the same as risk management
- Governance is setting risk appetite, tolerance & culture
- It also includes oversight of risk management function
- Approach to risk: literacy in boardroom, maturity of operation
- Risk Governance standards
 - NOS Feb 2013
 - BSI Sep 2013

Governance paradigm: shift or paralysis?

Neville Wells

Governance

- Much more change than Strategic Report
- Governance Statement (UKCGC, LAMSCAGARR 08, DTR and LR)
 - Content revisions
 - Framework
 - Disclosure style
 - Inconsistency and conflict of requirements
- Remuneration Report (LAMSCAGAR(A)R13, ERRA 13, UKCGC, DTR and LR)
 - New requirements, with prescriptive detail and voting
 - Lots of tinkering over past 12 months

Tensions – the paralysis

- Regulatory level
 - UKCGC – Comply or explain, plus 18 specific Provisions (out of 52)
 - LR 9.8.6 R – all of the above, plus how company has applied 18 Main Principles set out in UK Corporate Governance Code, “in a manner that would enable shareholders to evaluate how the principles have been applied” ie fungus
 - Also inconsistencies within UKCGC
- Company level
 - External – commercial confidentiality
 - Internal – personally/collectively awkward
 - Siloed nature of production
 - “What are others doing?”
 - Increased onus on committee chairmen (and CoSec)

Flexibility, discretion and judgement – the shift

- Change style from boilerplate to year-on-year reporting
- Report key decisions taken, judgements made and outcomes
 - roles, remits, authorities delegated, and what was considered often covered
 - how responsibilities were actually discharged is not
- Give full explanations for non-compliance and use of discretion
- Show how strategy is governed and incentivised
- Establish clear linkages with Strategic Report content

Summary

Closing thoughts

- Focus on linkage and logic, with inter-related content throughout narrative
- Focus on granularity, transparency, relevance and purpose of disclosures
- Give explanations of judgements, decisions, actions and outcomes
- Quality, not quantity, of disclosures – materiality
- Demonstrate understanding of what primary audiences want to know
- Compliance is a start, not an achievement

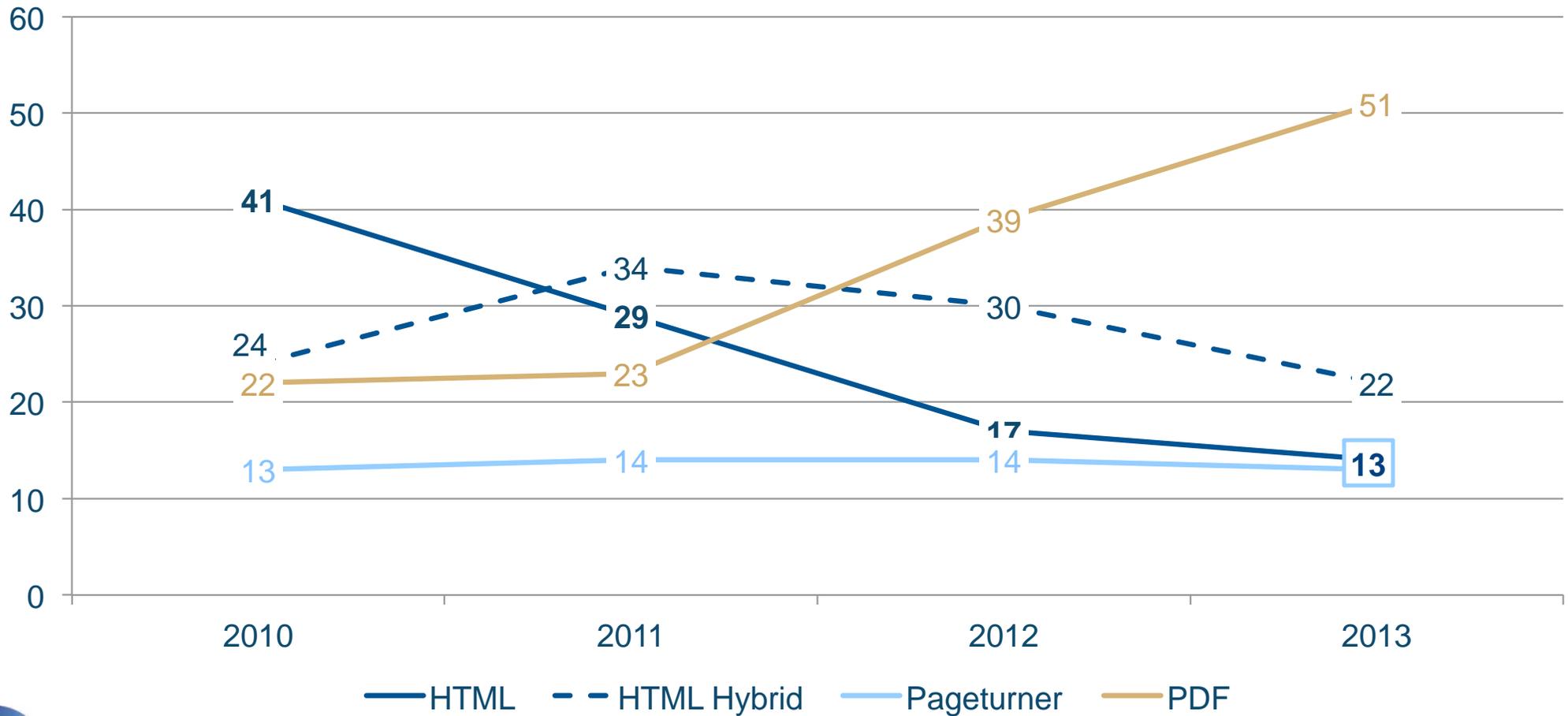
Thank you...

Q&A

Appendices

HTML Reports: what was being improved?

FTSE100 Statutory AR 2013 projection @ 18/9 – no further changes



Companies that have included largely strategic business models in their recent Annual Reports

- British American Tobacco
- Intercontinental Hotels Group
- International Airlines Group SA
- Lloyds Banking Group
- Tesco
- Unilever
- Domino Printing Sciences
- Ferrexpo
- Moneysupermarket.com Group
- Spirent Communications
- UBM

Continuing change expected

- Regulation, direction and guidance due:
 - Strategic Report and Directors' Report guidance (FRC)
 - Business model guidance (EFRAG, FRC guidance, IIRC, FRC Reporting Lab)
 - Revised Going Concern disclosure guidance consultation (Sharman) (FRC)
 - Turnbull (reporting on internal control) revision (FRC)
 - Kay (long-termism) direction and guidance (FRC)
 - UK government consulting on Corporate Responsibility, including CR reporting
 - EU Directive on CSR disclosures
 - Intended harmonisation of CA06, UKCGC, LR, DTR, EU Directives (starting with LR 9.8.8)
- UK election coming up, with band-wagons to be climbed on
- <IR> may become enshrined as “best practice” in any of its forms
- Increasing tension in international narrative and accounting standards
- Online genie may be let out of bottle (again)

FutureValue – the way forward



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