FRC FUTURE OF CORPORATE REPORTING CONSULTATION: NESTOR ADVISORS RESPONSE

Nestor Advisors is a London-based advisory firm specialising in corporate governance and organisational design. We work with the boards and senior management of financial institutions, companies and not-for-profit organisations to improve decision making, organisational structures, controls and incentives. We maintain a high degree of independence by focusing exclusively corporate governance advice and avoid the conflicts of interest that can occur by offering competing corporate services to our clients.

We welcome this review of corporate reporting, and entirely agree with the FRC that the annual report "has been pushed and pulled to meet increasing demands from traditional and new users… [and that] the result is a document that is confused about its intended audience and purpose". We also agree that both companies and users would benefit from a more holistic approach to corporate reporting.

However, we are not persuaded that in order to achieve this objective it is either necessary or desirable to scrap the annual report and accounts altogether. We are also concerned that the proposals could result in a significant increase in the overall volume of reporting which could undermine the benefit of an improved structure by making it harder for users to find relevant information.

In our view there is still value in having a summary report bringing together most important information about a company's performance, albeit one that is much shorter and focused than at present.

If part of the rationale behind the restructuring of reporting is to make it easier for users to find the information relevant to them, it is not clear how requiring them to look through three or possibly more separate reports to find it achieves that.

There also seems to be an implicit assumption that the audiences for, for example, financial and ESG information are different ones; this runs counter to the FRC's admirable efforts to encourage investors in particular to take a more rounded view of a company's performance and prospects, such as the 2020 Stewardship Code.

In our view, there is benefit to be had from requiring companies to produce a 'highlights' report bringing together key financial and non-financial information in an integrated way. Whether this would need to be a physical or web-based report would be a matter for further consideration but – particular in the latter case – it is not inconsistent with the proposed network approach.

Such a report might perhaps sit on top of the structure that is proposed and act as an access point as well as a summary. This is what many of the better annual reports already do when viewed online, incorporating links to more detailed information elsewhere on the website for those who are interested.

103 Wigmore Street
London W1U 1QS
United Kingdom

+44 (0)20 7628 3497
info@nestoradvisors.com

Nestor Advisors Ltd
Registered in England number: 04493428
VAT: GB 805 6770 21

nestoradvisors.com

As noted, our other concern about the proposals is the potential increase in the volume of information to be provided, increasing the cost to companies and decreasing the ability of users to find the information they seek.

This would seem to us to be the almost inevitable consequence of a requirement for companies to produce multiple reports. It could be the reporting equivalent of adding another lane to the M25; creating more capacity results in greater demand for information, not better management of existing demand.

Combined with the related proposal that there should no longer be a single materiality test it could be viewed as a signal to users – and perhaps even more so regulators – that the thresholds in terms of the level of information they can reasonably expect companies to provide have been lowered. This is a particular concern in relation to the public interest report. The consultation paper is not all that clear about what would be included in such a report other than that it would go into greater detail than the annual report does at present.

While we welcome the FRC's proposed reporting principles of brevity and relevance, we would note that companies are encouraged to apply similar principles already (for example, in your guidance on the Strategic Report). This has not prevented annual reports increasing exponentially in length. In most cases this has not been the result of a lack of discipline on the part of companies but additional regulation and external pressure from investors and other stakeholders. On their own, we think these principles are unlikely to be an effective counter measure.

As far as materiality is concerned, we accept that the current materiality test may be flawed but, similarly to the annual report, we consider the answer is to reform the test rather than replace it with multiple tests.

Bringing these issues together, we would suggest that recalibrating the existing reporting framework might be more suitable than reinvention. At its simplest, this would have three levels: mandatory information that must be provided in the annual report, which would be greatly stripped back; mandatory information that must be provided on the website; and voluntary information. As a starting point, the different topics currently covered by the annual report – business model, risk and so on – could be mapped against these levels.

As an illustration of how this might work in practice, the corporate governance statement in the annual report might be limited only to any changes in the composition of the board and committees, a summary of the board and committee's activities during the year and, if relevant, a statement on what the board has done in response to any significant votes against at the previous AGM and an explanation of any non-compliance with provisions of the UK Corporate Governance Code. All other disclosures currently required by law, Listing Rules of the Code would be provided on the website only.

We hope that these views are helpful and would be very happy to discuss them in more depth with the FRC if requested.

CONTACT INFORMATION:

Lisa Willmott
Marketing Manager
Nestor Advisors
103 Wigmore Street, LondonW1U 1QS
Tel: +44 (0)20 7628 3497
lwillmott@nestoradvisors.com