Dear Investor

**The annual reporting season**

I am writing ahead of the 2016 shareholder meeting season to highlight some recent changes in reporting. I hope this will be helpful during the forthcoming shareholder meeting season.

**Overall aim of the annual report**

The purpose of the annual report is to communicate relevant information to investors, and the annual report as a whole should be fair, balanced and understandable. This means avoiding boilerplate disclosures and ensuring that the report and accounts only contain material information, which is presented clearly and concisely. [1]

We encourage investors to engage with companies to provide a steer on what information they believe is relevant and to challenge where reporting falls short of these expectations.

**Risk, internal control and viability**

For those companies that apply the UK Corporate Governance Code, this is the first year of enhanced reporting on risk and internal control and the inclusion of a viability statement. These changes were designed to strengthen the focus of companies and investors on the longer term and sustainable value creation.[2] Companies may choose the appropriate time period for their viability statements, although the period assessed should be significantly longer than 12 months. You should see an explanation of the period chosen, taking into account the circumstances of the company, and avoiding 'boiler plate' statements.

The strategic report is intended to be an important source of forward-looking information about strategy and risk.[3] It should provide the most current view of the company's prospects. You may find our recent letter to audit committee chairs helpful, in which we provided guidance on reporting during a period of significant market volatility.[4]

Companies are required to consider materiality in the reporting of their 'principal' risks and uncertainties as part of their strategic report. We encourage companies to disclose how those risks specifically affect them, the range of potential outcomes and any mitigating actions. Where key risks do not seem to be included then you may wish to raise this with companies. For example, we have recently heard some investors express surprise that cyber risk and climate-change related risks are not reported more often as principal risks.

**Brexit**

Companies may well be currently considering the risks and uncertainties associated with the UK's renegotiation of its EU position and potential exit. If the board considers this to be a principal risk they should disclose that to their shareholders.

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**Alternative Performance Measures**

We continue to monitor how non-GAAP and alternative performance measures are used to report performance. As a reminder, where companies elect to use these, they should be clearly defined, consistent and include reconciliations to, and explanations of, how they relate to GAAP measures.

**Audit reporting**

Extended audit committee and auditor reporting requirements were introduced in 2013. As a result, you should expect these to be consistent with the financial statements and for sufficient information to be provided about the audit to allow for an informed discussion with the company. We have recently published a guide on the impact of extended auditor reports.[5]

**Dividend disclosures**

We know that dividend disclosure is important to many investors. The Financial Reporting Lab's recent report *Disclosure of dividends – policy and practice* [6] encourages companies to ensure clear disclosure and suggests areas for improvement. You may wish to challenge companies that provide insufficient information in this area.

**Governance reporting**

The FRC recognises that not all parts of the Corporate Governance Code are relevant to all companies at all times. However, where boards elect not to comply with key provisions of the Code, they should provide specific, meaningful explanations to investors.

As a reminder, companies should set out the background to the matter, provide a clear rationale for the action being taken and describe any mitigating activities. If the non-compliance is intended to be temporary then the company should indicate when it expects to conform with the provision. We encourage investors to challenge companies where they do not believe that explanations given are sufficiently persuasive.

**Accounting policies and impact of new standards**

It is important that companies explain critical judgements and accounting policy choices, particularly where there is diversity of treatment, in pension reporting, for example. You should expect companies to identify the precise nature of the judgements they made rather than merely repeat what the standards require.

In the last two years, the International Accounting Standards Board has published three major standards; IFRS 15, 'Revenue', IFRS 9, 'Financial Instruments' and IFRS 16 'Leases'. The effective date for IFRS 15 has been deferred to 1 January 2018 and IFRSs 9 and 16 have not yet been endorsed for use in the EU. We will write again to explain how we see the potential impact of these standards in due course but in the meantime, you may wish to look out for indications by companies of their likely impact, which should be disclosed once it can be reasonably estimated.

**FRC transparency**

We are committed to improving our own effectiveness in raising the quality of corporate reporting in the UK. During 2016 we plan to increase the transparency of reporting our conclusions on individual company reports and audits; letting companies know when we have reviewed their report and accounts and have no substantive points to raise; and, from 2017, naming the companies whose reports have been subject to our corporate reporting or audit quality reviews.

**Your feedback**

Finally, we would welcome any general or specific comments you may have on the quality of corporate reporting, positive or negative. For serious concerns, the FRC also has a formal complaints mechanism via our Corporate Reporting Review team. [7]

I hope that you find this letter useful and look forward to your feedback.

Yours sincerely

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[1] Further information on the FRC's Clear & Concise initiative is available at https://www.frc.org.uk/Our-Work/Key-projects/Clear-Concise.aspx including the publication Clear & Concise: Developments in Narrative Reporting.

Corporate Reporting Review Annual Report 2015 – including Clear & Concise case study (pages 15-17). https://www.frc.org.uk/Our-Work/Publications/Corporate-Reporting-Review/Corporate-Reporting-Review-Annual-Report-2015.aspx

[2] Guidance on Risk Management, Internal Control and Related Financial and Business Reporting – including implementation of the Code requirements for a viability statement. https://www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Guidance-on-Risk-Management,-Internal-Control-and.pdf

[3] Guidance on the Strategic Report – including principles for good communication, placement of information and materiality. https://www.frc.org.uk/Our-Work/Corporate-Governance-Reporting/Accounting-and-Reporting-Policy/Clear-and-Concise-Reporting/Narrative-Reporting/Guidance-on-the-Strategic-Report.aspx

[4] Letter to audit committee chairs https://www.frc.org.uk/FRC-Documents/Audit-and-Assurance-Council/Letter-to-ACC-on-relevant-reporting-considerations.pdf

[5] A summary of the key findings in our recent report on extended auditor's reports can be found at: https://frc.org.uk/Our-Work/Publications/FRC-Board/Summary-for-Investors-Extended-Auditor-Reporting.pdf

[6] Financial Reporting Lab reports: *Disclosure of dividends – policy and practice*, *Accounting policies and integration of related financial information* and *Digital present* can be found here https://frc.org.uk/lab/reports

[7] https://www.frc.org.uk/About-the-FRC/Making-a-complaint-to-the-Financial-Reporting-Coun.aspx