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Dear Ms Raval

### Exposure Draft – Guidance on the Strategic Report

Thank you for allowing Legal & General Investment Management (LGIM) the opportunity to provide feedback on the guidance paper that has been produced. LGIM has £433bn of asset under management as at 30 June 2013. Of this, £71bn is invested in UK equities and a holding in all companies in the FTSE All-Share. As such, we consider the Annual Report as the single most important source of for us as shareholders.

We welcome the proposed changes to the reporting structure of the Annual Report to create a more focused document. We would like companies to take this opportunity to have an extensive review of their Annual Report which has grown in content and size over the years and build on the current business review. It is also an ideal opportunity for those companies that are undergoing significant changes, e.g. Vodafone plc.

We believe that the proposed guidance document has generally been well drafted, is comprehensive and clear. We hope the feedback below will be helpful to further improve the current draft.

#### Section 3 - The annual report

Section 3 of this draft guidance includes an illustration (Illustration 1) which is intended to clarify the purpose of each part of the annual report and help those that prepare annual reports to make judgements regarding where information would be best presented.

##### Question 1

Do you think that Illustration 1 is helpful in achieving this objective?

##### Question 2

Do you agree with the objectives of each component and section of the annual report which are included in Illustration 1?

Q1. – LGIM agree that the Illustration 1 is helpful.

Q2. – LGIM agrees with the objectives of each component and section of the Annual Report and having 3 distinct sections. We would like to request that the current box on the Corporate

Governance Report be expanded to include a separate bullet to highlight the various useful reports such as the Audit Committee and Nominations Committee reports.

### Question 3

Do you think the guidance on the placement of information in the annual report in paragraphs 3.10 to 3.14 will have a positive influence in making the annual report more understandable and relevant to shareholders?

Although this question refers to parts 3.10 to 3.14 of the document, we would like to make a comment about 3.7. This paragraph contradicts the rest of the document that emphasises the fact the Annual Report is for investors. We acknowledge that there are other people that may be interested in the annual report; but essentially, the Annual Report should be for investors. Over the years, the annual report has been adapted by companies to be useful to a range of readers. Historically this was because there was no corporate website and the Annual Report was seen as a good place to reach out to many readers. The result of this was that the size of the Annual Report grew in size and matters of importance became more obscure.

Companies' now have a corporate website and they should be encouraged to source more information for all users on their corporate website. We would therefore request a re-drafting of this paragraph to remove the current wording that encourages information for other stakeholders to be included in the Annual Report.

The wording in para 3.10 to 3.14 should encourage clearer and more objective reporting. A minor concern surrounds the use of "core" information and "supplemental". It may be helpful to give an example of what is meant as "core" and "supplemental" and require an explanation from whose perspective it is "core".

We believe that duplication of information can add value if it will facilitate the comprehension of information being presented and will remove the need to flick between several pages of text.

### Section 5 Strategic reports and materiality

Section 5 of this draft guidance addresses the application of the concept of materiality to the strategic report, remaining as faithful as possible to the definition of materiality used in International Financial Reporting Standards (IFRSs).

### Question 4

Do you agree with this approach? Is the level of guidance provided on the subject of materiality appropriate?

The guidance provides a good explanation of materiality. However, companies should be required to explain how they arrived at what is material to their business.

5.4 It may be useful to extend this section to require companies to integrate their material non financial KPIs with their financial KPIs. Some non-financial KPIs can be very important for the future prospects of the company. Linking the two types of KPIs will re-emphasise their importance for the future success of the business.

5.5 We would like to propose some *additional text* to be inserted at the end of 5.5. So that the paragraph reads as follows:

"...affecting the entity". *Items should be limited to those that are considered key in promoting the future success of the business.*

## Section 6 - The strategic report

### Question 5

Do you agree with the proposed 'communication principles', set out in paragraphs 6.5 to 6.27 of the draft guidance, which describe the desired qualitative characteristics of information presented in the strategic report? Do you think that any other principles should be included?

LGIM agrees with the suggested guidance. Clear linkage between relevant information would be very useful to us as readers of Annual Reports as searching for information can be time consuming.

We would like to request a change to the sentence structure at 6.20 by taking the first sentence and adding it to the end. This will make the paragraph more positive. In our view, the paragraph should read as follows:

Information on how a particular fact ... entity's future prospects. Therefore the use of generic or boiler plate information ... is of limited use to shareholders".

### Question 6

In this draft guidance, we have aimed to strike a balance between the need to ensure that the structure and presentation of the strategic report is sufficiently tailored to the entity's current circumstances and the need to facilitate comparison of the strategic report from year to year. Do you think the guidance in paragraphs 6.26 and 6.27 achieves the correct balance?

6.26 is very clear and provides appropriate balance, we are slightly unsure of the need for 6.27.

### Question 7

The 'content elements' in bold type described in paragraphs 6.28 to 6.73 do not go beyond the requirements set out in the Act, although the precise wording may have been expanded to make them more understandable. Do you think this is appropriate? If not, what other 'content elements' should be included in this draft guidance?

The purpose of the guidance is to provide clarity to the requirements of the Act. Therefore, it would be appropriate for the content elements to be expanded so long as it continues to give effect to the requirements of the Act.

6.59 – Some companies use two definitions of adjusted financials measures. Earnings per share (EPS) is a classic example. A company may have one adjusted EPS figure in the financials part of the strategic report and a completely different figure for adjusted EPS under executive remuneration. Therefore, we would request the following expansion to the example text as follows: "where an adjusted performance measure i.e. adjusted EPS, is used for the purpose of executive remuneration that a clear linkage is also highlighted".

6.65 – The guidance has used the words material throughout the documentation. Therefore we question the need to introduce a new word of "magnitude" in this paragraph. We would like to request that this word is removed and replaced with material. The wording would therefore be "The strategic report should include ...is of such a nature or *material* that they are relevant to shareholders.

**Question 8**

Appendix I 'Glossary' uses the same definition of a business model as the Code ('how the entity generates or preserves value'). Is the level of guidance provided on the business model description in paragraphs 6.38 to 6.41 sufficient?

LGIM considers the level of guidance what is meant by a business model is sufficient.

**Question 9**

Do you think that this draft guidance differentiates sufficiently between the concepts of business model, objectives and strategies? If not, why not and how might the guidance be improved?

We believe that the guidance has been fairly well set out with each section divided. It is possible to enhance it further by having the sections more clearly headed as demonstrated below.

For Example taking section 6.30 of the guidance.

6.30 Objectives, strategy and business model are inter-related concepts. An entity will decide on its objectives and select strategies to achieve those objectives. An entity will then apply its business model to its activities in pursuit of its objectives and strategies. The disclosure of an entity's objectives, strategy and business model should together explain what an entity does and how and why it does it.

**Objectives**

**What the business wants to achieve**

The strategic report should include a description of the entity's principal objectives and its strategies for achieving those objectives<sup>16</sup>.

6.31 An entity will normally have set a number of formal objectives describing what it intends to achieve. In addition, the entity will also have developed explicit strategies that describe the means by which it intends to achieve its objectives.

Having a number next to the box with the principle can be a little confusing a different numbering system for the principles or not having a numbering would be better in our view.

**Question 10**

This draft guidance includes illustrative guidance (the 'linkage examples') on how the content elements might be approached in order to highlight relationships and interdependencies in the information presented. Are these linkage examples useful? If not, what alternative examples or approach should be used?

Examples are always useful as they add colour to the definitions. They should be kept.

I hope the above comments are useful. Should you require any clarification please do not hesitate to contact me? We look forward to reading the final guidance document.

As this is a new approach to reporting, we wondered whether the FRC would consider over the course of the next year making note of companies that have produced good, well thought through strategic reports and publish these somewhere on their website as a useful guide to other companies. We believe that this will help to enhance better reporting standards. We look forward to hearing your comments regarding this proposal.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'AB', is positioned above the typed name.

**Angeli Benham**  
Corporate Governance Manager