Response and comments from Black Sun

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Corporate Governance and Stewardship
Financial Reporting Council
8th Floor
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RE: Future of Corporate Reporting

Dear Sir/Madam

Black Sun welcomes the opportunity to respond to the *FRC Discussion paper "Future of Corporate Reporting"* and commends the FRC for looking to the future.

Black Sun is an internationally recognised, market leading stakeholder communications company. We help businesses articulate their purpose and communicate how they deliver value by developing inspiring communications that reach, engage and influence important stakeholders. We encourage best practice in communications and corporate reporting and believe that transparency and clear communication are pre-requisites for effective engagement between companies, investors and wider stakeholders.

We regularly work with over eighty FTSE 350 companies, including some of the UK's biggest names such as Burberry, Coca-Cola HBC, DS Smith, G4S, Schroders, Taylor Wimpey, Tesco, Schroders, Rio Tinto and Vodafone We are passionate about demonstrating thought leadership within the industry and published the 15th edition of our flagship Complete 100 research - which assesses corporate reporting trends among the FTSE 100 in June 2020. We also held many events with the FRC and other organisations last year, engaging over 1,000 corporates, to discuss the changes in the governance and reporting landscape.

We occupy a unique market position, working with corporates to help them create, develop and produce best practice communications and reporting, while maintaining open and honest dialogue with framework setters, regulators and industry bodies. The ability to advise on principles and approaches to business, while providing practical implementation insights to industry bodies allows for a win-win approach, supporting progress for all.

We recognise that this is a thought leadership paper and commend the FRC for stimulating the debate. In summary, we support aspects of the proposals and principles and encourage continued engagement with preparers, advisors, investors and other stakeholders to develop this thinking.

To compile our response, we have attended many of the FRC's engagement workshops, listened to our clients day to day and conducted a specific client workshop to compile this response with representation from ten FTSE organisations (individuals from communications, investor relations, co-sec and finance)

We recognise that many of these ideas are conceptual at the moment and much will need to be done to address the practicalities. However; there were a number of questions that underpinned many of the discussions with corporates which we believe need further consideration and clarification: what problem are we trying to solve? What is the FRC's role as a regulator? Are we losing focus on the primary audience for corporate's reporting – the 'investor'?

We are thankful for the opportunity to provide our comments and we will be happy to discuss any of the issues raised.

Yours sincerely,

Sallie Pilot, Chief Insight and Engagement Officer

Q1. What are your views on our proposals as a whole? Are there elements that you prefer over others?

We support aspects of the 'Future of Corporate Reporting' paper, welcoming the concept of a 'networked system of communications' reinforcing the direction many companies are moving towards. We have found companies are pursuing a networked communications strategy, communicating and disclosing broader information to meet the disclosure needs of the market and their wider stakeholders, and leveraging the use of digital channels and technology.

Each year, for the past 15 years, we have been tracking corporate reporting trends of the FTSE100 through our Horizon Series Research programme. Over that time reporting has changed profoundly – from a compliance driven tick-box record of past performance to one of challenging mindsets and behaviours internally, setting out effectiveness of decision making and demonstrating sustainable benefits for shareholders, employees and wider stakeholders. There is clear evidence of increasing transparency and improving engagement between businesses and their key stakeholders.

Through our research and day to day work we have also found companies are naturally widening and deepening their communications; providing information in more accessible, transparent and connected ways, leveraging their communication channels in order to meet the market needs and increasing stakeholder demands for information, and communicating and engaging more consistently on their value creation story. All without regulatory intervention.

We broadly agree that the traditional annual report is increasingly trying to serve multiple purposes and audiences and becoming too long and unwieldy. However, it is our view that the primary focus should be on streamlining and improving the existing annual report, rather than pursuing a wholesale change in format to force a network of reports, because we feel in many cases this is naturally happening, without regulatory intervention as articulated above.

Many companies have achieved a great deal within the existing reporting framework: embracing concepts such as purpose, culture and values which drive behaviour change, successfully considering a wider group of stakeholders, as required under Section 172, and integrating environmental, social and governance (ESG) factors into their businesses and reporting. Many are adopting frameworks for non-financial reporting that are gaining global recognition such as the Task Force on Climate-related Financial Disclosures (TCFD) and Sustainable Accounting Board Standards (SASB). It is our expectation that annual reporting will continue to develop and build upon these elements still further.

> “Overall the vision seems interesting, searchable reporting could be attractive to investors but the question is this the right format to do that? Have the sense that the FRC doesn’t appreciate the practicalities around this, getting the sign off on a more frequent basis and additional burden created is very complex. The devil will be in the detail.”

We have provided further details of the benefits and concerns of the proposals in the responses to the questions below.

Q2. What do you see as the key practical challenges of implementing our proposals? Do you have suggestions on how these could be overcome? What do you see as the costs and benefits of the new model?

The following are a summary of the challenges and concerns of the proposed reporting framework:

Fear of loss of integration efforts

Within most organisations, the planning and preparation of the annual report is usually a team effort, bringing together some or all of finance, company secretariat, investor relations, communications, sustainability. The strength of the reporting process is the ability to bring different parts of the organisation together to think in a more holistic and integrated way about the business and communicate in a consistent and connected way. The ‘value and the challenge’ in the annual report process is that in the majority of cases it is ‘no-one’s day job’. It is a part of everyone’s job, ensuring that the participants in the process are knowledgeable and connected to both the strategic and the operational aspects of the business.

Creating a network of reports may result in the fragmentation of that team effort, the overall focus on the holistic value creation story, and the quality of the information - with individuals and teams forced to focus on specific content. This may impact the quality of joined up thinking and the flow of information within organisations as well as marginalise employees, or teams, that are given the task of working on aspects of the reporting network that might be considered ‘non-core’.

Pressure on resourcing and timing

A number of companies raised their concerns of how the reporting network will work in practice. In particular, annual report owners noted there already are strains on resources at companies with communications often delivered by small teams. It is also likely that companies would need more resources to produce multiple reports and a risk that, over time, these separate reports may grow rapidly in size. In addition, companies felt it will be challenging delivering the different reports across different timelines while maintaining timely information. The extra resource required for multiple reporting may lead to the reporting function in large companies becoming too separate from the operational business, and therefore losing the integration benefits. In smaller companies the resource requirement will simply be unmanageable.

Furthermore, concerns have been raised about the challenges in obtaining the same level of attention from senior management and the board to review a network of reports instead of a single annual report, leading to potential governance challenges.

The following practicalities warrant further detailed considered in the development of these proposals:

Loss of focus on key target audience – We recognise the concept of stakeholder capitalism is gaining momentum and welcome the ongoing progress towards corporate reporting becoming focused on a wider group of stakeholders. However, the reporting network may inadvertently make it harder for investors to find the information that they need. A ‘business report’ as a stakeholder-neutral document and the separation of the financial statements causes confusion as to what investors will hold companies to account with. Splitting the financial half with management commentary could reduce coherence, consistency and connectivity between the two.

Challenge of duplication – Every report requires wider context for its content which presents the challenge of duplication. With multiple networked reports and lack of clarity of non-financial information required to be reported in the business report and public interest report, there may be significant duplication in reporting on issues among companies.

Focus on reporting on business rather than running businesses - The current annual report process is a tremendous burden on a corporates in terms of the time, cost and resourcing and these proposals will exacerbate that. "Instead of 3 or 4 months for doing an annual report, we will have to do the annual report throughout the year" with new additional network repots with their own objectives.

Devil is in the detail – The proposals outline how the network could work, but further information will be needed on how everything will work in practice. "The annual report is a very retrospective document. There was a feeling that the FRC could have looked at a broader format e.g. on a corporate website. Devil is in the detail e.g. how this will be connected from technology perspective".

Increase the communications divide – Our research and engagement shows gaps in the level of disclosure, transparency and communications between companies that have larger dedicated teams and individuals compared to companies with limited resources. The proposals will likely increase the divide further.

Encourage siloed thinking: A network of reports may result in companies moving from bringing together people across the business and helping to think in a more holistic and integrated way when preparing the annual report, to siloed thinking as individuals and teams will be focused on specific content.

Additional board sign offs – In many cases, the annual report can be challenging for companies to get the attention of the board and could be even more challenging with multiple documents with multiple objectives to get clear and appropriate governance and oversight within organisations

Pressure on Resource : Additional Board Reporting - This will also increase burden on NEDs (who typically have multiple Boards) to review a series of reports over the course of the year. Could impact time commitments resulting in having to give up some positions.

Q3. Should corporate reporting focus on a wider group of stakeholders through multiple objective-driven reports, instead of a primary user focused approach?

The concept of stakeholder capitalism is gaining momentum, and we welcome the ongoing progress towards corporate reporting becoming focused on a wider group of stakeholders. We firmly believe that the annual report must not lose sight of the primary intended purpose of the annual report, which is to communicate the financial position and performance of a company to its shareholders, whilst also meeting the requirements of Section 172 and reflecting how boards are engaging with and considering a wider group of stakeholders in their decision-making. It is important that the FRC considers the views and needs of this primary user group in any proposed changes. The investor lens has a broad focus on all factors that may impact the long-term success of the company spanning many issues. Therefore using an investor lens is most likely to fulfil the needs of many stakeholders over the often singular issue interests of individual stakeholders.

Wider interest in reporting has grown and the annual report has, for many years, been used by a wider group of stakeholders (for example existing and prospective employees, customers and suppliers) to gain a better understanding of the business, its performance and prospects. We believe that the concept of objective-driven reporting could help companies to filter information and lead to more focused and detailed reporting on specific areas, however we feel more thought needs to be given to what we are trying to achieve.

> "Without clear guidance, would have concern on whether the board would be able to assess the completeness of the documents if it wasn't clear who they were for – whose stakeholder perspective should they consider? Do the documents complete the view of x?"
>
> "What companies think an audience wants may not be what an audience wants." – FTSE 100 Company

In addition, the approach needs to be considered alongside achieving the principles set out in the paper - if each report is driven by different objectives, this may make the reports less comparable within and between companies.

Q4. Do you consider the set of principles (system level attributes, report level attributes and content communication principles) in section 2 would be helpful in improving the quality of corporate reporting today and in the future?

We welcome the proposed set of principles set out in Section 2 to establish coherence across all company reporting. We note that a number of these principles have already been established in guidance and practice within the current reporting framework.

Q5. Do you agree with our proposals to improve the relevance and accessibility of information, involving more concise reports distributed across a reporting network?

We are strongly in favour of steps to improve the relevance and accessibility of information and we agree that more concise reporting is required. As noted in Q1, we have found companies are already naturally moving in this direction. As such we encourage the FRC to focus on ways to streamline and improve the existing annual report rather than create new requirements.

Recently, we have seen a growing number of companies delivering core annual reports supported by additional detailed information which communicates in more engaging, accessible formats, designs and channels – through a well-designed website that is rich in content and kept regularly updated. This approach can be very powerful, enabling companies to focus on different needs for information – from data rich to engaging story telling.

It is our view that companies must embrace digital communications across all aspects of their reporting, and we would urge the FRC to ensure this is embedded in any proposed changes to the current annual reporting system.

Q6. We are proposing that there should no longer be a single test for materiality that is based on accounting standards but instead materiality will be dependent on the objective of a report. Do you agree with this approach, please explain why?

Currently it is not quite clear how this proposal might work in practice. We would like more detail on the proposal for materiality to be dependent on the objective of a report, including how materiality could be defined in non-financial terms and fit with the principle of 'true and fair' reporting. Some specific points to be addressed:

> "Having potentially three different materiality lenses for the three different core reports may not be helpful for a reader that might want to search historical information e.g. 10 years looking back across three different reports, that person may not appreciate a different materiality lens on the information they are reading and the fact the materiality lens is determined by the company means you have to determine the materiality lens used by the company in order to understand the context you are reading."
>
> "The financial materiality concept set out by IASB is a good one – but even applying that with financial statements is not straightforward and can lead to frequent discussions within the finance community as to whether something that is/isn't material. As you start to apply this to different reports and with different users and think about the principle [whether omission/inclusion of content will] impact the decision of investors, if you have a different user and a different type of report you could end up having an extremely complex understanding of materiality. As it stands it's pretty impractical"

In addition, some companies felt the proposals will add additional work behind the scenes at board and management levels to understand implications materiality concepts on reporting. Another company commented

> "Might be material for one stakeholder, coming back to s.172, this just yet more evidence we've lost sight of the core document and what it's trying to do and it's trying to be all things for all people which could end up diluting what's good about it.'

Finally, there will be an impact to Audit profession on having consider different sets of materiality in the same year for different part of the Annual Report. Making it even more complicated that what they are having to endure currently with so much focus on their quality of work.

Q7. Do you believe that there is a need for regulatory standards for non-financial reporting? If so, what do you consider the scope of the information that should be covered by these standards?

Black Sun believe a more standardised framework for reporting would not only be beneficial to preparers of reports and the materiality processes they conduct to create them, but also to wider stakeholders such as investors and civil society. The ability to compare organisational performance and impact – with sufficient context – across industries and activities, would provide invaluable knowledge to all stakeholders, but specifically to capital markets, investors, regulators and businesses themselves. In this regard, the majority of our clients have begun to report on the TCFD framework ahead of the new listing rule requirements.

As already noted, we have seen excellent progress over the past 15 years in non-financial reporting and this focus has been accelerated by the pandemic. A number of our clients and corporates (67% FTSE100) have already adopted, or are beginning to use, the TCFD framework on a voluntary basis, ahead of new 'comply or explain' Listing Rule and expected mandatory disclosure requirements that have been announced by the government. SASB is also received widespread recognition by regulators such as yourself, investors and inadvertently corporates.

We have been hearing for quite some time the challenge of the confusion in the market with the multitude of different actors and frameworks. In addition, many corporates are at different stages of their ESG journey.

As such, we welcome the development of globally recognised standards for non-financial reporting to enhance the consistency and comparability of data, whilst avoiding the creation of a 'one size fits all' model. In our view, these global standards must provide sufficient flexibility for companies across different sectors and of different sizes and complexity to tell their sustainability story in their own terms

We hope that future standards will be developed based upon the existing frameworks that are being widely adopted and endorsed by corporates, investors and wider stakeholders and align with work the work at International level by the IFRS Foundation and EU Commission and avoid inadvertently creating additional non-financial standards/ reporting systems.

We would also expect the development of global standards to build upon existing legal and regulatory requirements for UK listed companies, such as those set out in the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013.

Q8. Do you agree with the need for companies to provide information about how they view their obligations in respect of the public interest?

We agree and based on our annual research of annual reports have found that many companies are already considering their obligations through reporting on the requirements set out in Section 172 as well as how they are delivering on their societal purpose.

Q9. Do you agree with the introduction of a Public Interest Report and the suggested content as set out in Section 6?

We note the proposals are in line with the recommendations of the Brydon review, namely "The directors present an annual Public Interest Statement, which explains the company's view of its obligations to the public interest, whether arising from statutory, self-determined or other obligations, and how the company has acted to meet this public interest over the previous year."

We believe matters relating to the public interest should be part of the company's DNA and purpose, strategy and business model, and integrated into every aspect of the business. As noted, this has become more evident prior to the Covid-19 crisis but we have seen a rapid acceleration in this trend over the past year, as a result of the pandemic. This is also reinforced by S172.

In our view, splitting this information into a separate report contradicts the wider direction of travel for integrated thinking and reporting and how companies think about purpose, ESG and their holistic value creation story. It could lead to overlap and repetition in content between the key Business Report and Public Interest Report, causing potential confusion and frustration for the reader.

There is also the worry of scope creep in trying to determine the stakeholders that could be captured under this – especially for asset management firms having to consider same for their portfolio companies. Clarity and relationship or differentiation to obligations under S172 would be welcome.

We acknowledge that the need to define businesses role in society is changing, and demands and requirements for non-financial information will continue to increase. We believe it is important to provide companies with clear guidance on their legal and best practice disclosure requirements in the annual report, as part of a wider initiative to streamline and improve the document. Where appropriate, companies may wish to continue expanding upon their sustainability credentials, activities, accomplishments and impacts in separate reports, communications channels or corporate website, dependant on their needs and the needs of their stakeholders. In our view, this should not be prescriptive.

Some critical and practical questions to be answered at the next stage of thinking:

> "How different will this be compared to what companies currently produce through sustainable business report? Those have evolved over the years and are fairly comprehensive."

> "I find it quite difficult to understand what content will be left to put in here, given I would have thought most reporters will probably pull on elements of those kind of subject matter areas in the business report, and then how will it sit as a standalone report without the context of value creation and the business model and general performance overview. How will the pieces that are left, be enough for it to be standalone? And then it comes back to practicalities, there will be different project owners and how do you get consistent messaging across the workstreams."

10. Do you see any other ways that current and new technology could be used to facilitate the proposed model, and support the system level attributes of corporate reporting identified in section 2?

There is a clear and important opportunity to develop the role of digital, and in particular the role of the corporate website, in the annual reporting process. In our experience with clients well-designed corporate websites should be rich in content, setting out the company's strategy, business model, key markets, corporate purpose and so forth, and kept regularly updated. It also provides a platform to share presentations and other materials with stakeholders, and bring communications to life through the use of images and videos.

We see tagging to provide extra functionality as a positive step forward for users. We welcome the proposed tagging model and agree XBRL is best placed to support the attributes the proposal is trying to achieve. The ability to leverage technology in order to analyse information and gain insights would help ensure that any business, regulatory, investor or customer decisions and approaches would be more holistic going forward. In addition, the technology would enable users to choose topics they are interested in.

However, we note some companies are further behind in their technology journey and some consideration must be given to the potential increase in time and cost to investor relations teams, in particular within small cap companies.

> "This is a thing we should think about as a positive to the extent we have the resources to do this. My team struggles each year between signing the accounts and the AGM to print these things and send them to shareholders, this is where the world should go".

> "Maybe there does need to be regulation for companies to do get on board and do it appropriately, my concern especially for those companies that are least able to do it this will become yet another burden for an overstretched team at a time when were still struggling with the impacts of MFID II and direct communication impacts as a result of Covid and real reluctance to invest in the investor relations function."

In addition, others note the developments of future technology could be very different in the future.

> "Not completely clear this was a driver of technology, most of the opportunities referred to could be done in any case. And given the extended timelines of the proposals the technology that would be used would be completely different in 10 years' time".

11. Do you agree that the model we propose will achieve a proportionate reporting regime for companies of different sizes and complexity?

Whilst we are in support of the ambition presented, we are concerned that the proposals may not achieve a proportionate reporting regime for companies of different sizes and complexity and could widen the gap between leading and lagging practice. The separation of the annual report and the focus on a network of reports will undoubtedly lead to an increase in the resources required across an organisation to produce, approve and provide oversight on multiple documents and communications. This could also as noted in Q2, lead to the fragmentation of teams, jeopardising all the years of recent efforts to break down silos within organisations to think, report and communicate in a more holistic, joined up and connected way.

The consultation paper does not set out in sufficient detail how the proposed network of reports would be adapted / flexed to accommodate companies in different sectors, and of varying sizes and levels of complexity.

A specific example shared was - whilst we agree the preparation of the Public Interest Report should initially apply to larger companies, some companies are concerned that as proxies become used to larger companies publishing a Public Interest Report, smaller companies will be targeted and could be penalised for not publishing one.

12. What other areas do you see being necessary or relevant to the development of a model for corporate reporting that is fit for the future?

We believe it is essential to engage with the users of annual reports more deeply to determine their views and requirements, and the extent to which the current system is meeting their needs. As noted in Q1, many companies have already made significant progress within the current reporting framework and that momentum has only been accelerated through the pandemic.

In addition, we believe that it is imperative that the preparers of reporting are engaged more deeply moving forward, to help address not just the practicalities but the usefulness of this from an organisational, decision-making and governance perspective.

There is already a great deal of momentum for change, significant steps forward have been taken since this report was researched and written and a number of positive attributes which can be built upon to develop and improve the existing annual report.