

Deepa Raval
Financial Reporting Council
Aldwych House
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WC2 B4HN

Wednesday 13th October 2013

Dear Ms Raval

We welcome this opportunity to provide feedback on the Financial Reporting Council's Draft Guidance on the Strategic Report.

About ShareAction

ShareAction (formerly FairPensions) is a registered charity established to promote Responsible Investment practices by pension funds and other institutional investors. In particular, we work to encourage active stewardship of listed companies through the informed exercise of shareholder rights. ShareAction also champions greater transparency and accountability to the millions of people whose long-term savings are entrusted to the capital markets.

We are a member organisation and count amongst our members a growing number of globally recognised NGOs and trade unions, as well as over 8000 individual supporters.

Overview

The Coalition Agreement committed to 'ensure that directors' social and environmental duties have to be covered in company reporting, and investigate further ways of improving corporate accountability and transparency'. Share Action welcomes that commitment.

But we believe that the FRC's draft guidance does nothing to advance this commitment to higher standards of environmental and social reporting. At present, many investors tell us that they cannot assess and act on companies' social and environmental reporting with the same confidence that they would financial information. Better guidance could help to address this problem, and this draft represents a missed opportunity to provide that guidance.

Our recommendations

- We seek clarity that social and environmental reporting must be forward-looking and strategic. In particular, a specific link should be made between environmental and social reporting and strategic risk. It should be made clear that it is not sufficient for companies to



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confine environmental and social reporting to peripheral ‘CSR’ activities such as volunteering, but that they should ensure they address the key environmental and social risks associated with their core business. The draft guidance states that part of ‘the overriding objective of narrative reporting’ is to address ‘the principle risks that the entity faces’. But guidance on reporting strategic environmental and social risk is absent. Full integration of environmental and social information into strategic reporting is a key component of emerging best practice (as evidenced by the ‘integrated reporting’ movement) and the guidance will quickly become outdated if it does not reflect this.

- The guidance advises that ‘the strategic report should include a description of the principal risks and uncertainties facing the entity, together with an explanation of how they are managed or mitigated’. Whilst we do not suggest the guidance should incorporate a prescriptive ‘tick list’ of issues to report against, we do believe that clarity would be provided by guidance as to some of the key environmental and social risks likely to be material to companies in certain sectors, and to the markets in which they operate. For example, climate change poses particular risks to energy companies, and retail companies may be at risk from poor oversight of labour standards in supply chains.
- In promoting meaningful social and environmental reporting, the FRC could also refer to existing reporting frameworks, for example published by the Global Reporting Initiative and International Integrated Reporting Committee. In addition to these resources, the FRC could improve its own guidance by seeking expertise from civil society organisations. We have been somewhat disappointed by the FRC’s reluctance to engage with civil society whilst developing the draft guidance.
- More guidance is required on implementing the new reporting legislation. As per the Companies Act, paragraph 6.64 states that the strategic report should include information about ‘environmental matters; the entity’s employees; and social, community and human rights issues’. The inclusion of human rights in this list is one of the few substantive changes made by the new reporting regulations, and is cited in the UK Government’s human rights action plan, ‘Good Business: Implementing the UN Guiding Principles on Business and Human Rights’, as one of the key steps taken by the government to promote respect for human rights by UK businesses. The absence of any guidance about how to meet these new requirements is therefore concerning.
- The guidance should provide more detail on how the quality of information can be improved. To be helpful to investors, reporting must meet a clear standard of objectivity. We welcome paragraph 6.7 which states that ‘the strategic report should ... address positive and negative aspects of the entity’s development, performance, position and future prospects’. Narrative information must be fair, balanced and comprehensive, with investors and regulators able to challenge reports where they are inconsistent with what a reasonable director could be expected to report. Assumptions underlying key statements and projections must be disclosed.
- Non-financial KPIs are the single largest area of non-compliance with the law identified by the Accounting Standards Board, so it is vital that stronger guidance is provided on this matter.

In addition to these recommendations, it is critical that steps be taken to improve the effectiveness of enforcement. Accounting Standards Board research shows high levels of non-compliance with reporting obligations. Unless this is addressed, the FRC will not succeed in its objective to promote high quality reporting to foster investment. In particular, we believe that the Financial Reporting Review Panel must recruit specialists with expertise on social and environmental reporting, and should seek to improve the transparency of its practices when reviewing company reports, in order that FRRP decisions can advance the market’s understanding of what constitutes acceptable reporting.

We would welcome the opportunity to meet with you to discuss the issues raised in this response. Should you have any queries, please do not hesitate to contact me.

Yours sincerely,

A handwritten signature in black ink that reads "Catherine Howarth". The signature is written in a cursive style with a large initial 'C' and a distinct 'H'.

Catherine Howarth
Chief Executive, Share Action