

FRC: The Future of Corporate Reporting

2nd February 2021

Dear Sir John,

The FRC has an important role in serving the public interest by setting high standards of corporate reporting and by holding to account those responsible for delivering them. It is therefore only right and proper that this initiative should invite input from a variety of stakeholder groups on the proposed way forward on this increasingly important topic.

I personally welcome this opportunity to comment on the FRC discussion paper entitled A Matter of Principles: The Future of Corporate Reporting. Please find attached my comments in relation to suggested amendments to the FRC discussion paper which I hope will be of interest.

I would like to thank the FRC for providing this opportunity and should you require any additional information or wish to discuss any of the issues raised in more detail please do not hesitate to contact me.

Yours sincerely

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Response to FRC Invitation to Comment

A Healthy Balance Between the Focus on Value Creation and Value Preservation

The delivery of sustainable long-term stakeholder value requires a healthy focus on both value creation and on value preservation. Historically organisations have explicitly addressed the value creation imperative at a strategic level through their vision, mission statement, corporate strategy, and business model. The value preservation imperative however while perhaps sometimes implied has rarely been explicitly addressed in the same manner at a strategic level. The value preservation imperative in this context refers to the moral obligation to preserve, protect, and defend stakeholder value against value erosion, reduction, and destruction. The difference between explicitly addressing the value creation obligation and implicitly addressing the value preservation obligation is considerable, and its impact has already had a profound effect on corporate culture and resulting corporate behaviour. Unfortunately, in the 21st century there are already far too many examples of where a focus solely on value creation is typically associated with short-term financial rewards, often at the expense of, and/or neglect of, longer-term value preservation.

In recent times the FRC has been one of as a growing number of regulators, standard setters, and other governance bodies¹ who have been addressing this issue by explicitly referring to the value preservation imperative in its updated UK Corporate Governance Code in 2018. In the press release entitled A UK Corporate Governance Code that is fit for the future, the FRC identified the following change in relation to corporate culture:

“Culture: Boards are asked to create a culture which aligns company values with strategy and to assess how they preserve value over the long-term.”

In the document itself, in section 1 of the publication entitled Board Leadership and Company Purpose, the FRC stated the following:

¹ For example, the ICGN hold a position that companies and investors share a mutual responsibility to preserve and enhance long-term corporate value, thus contributing to sustainable capital markets and societal prosperity. This has been reflected in the publication of their Global Stewardship Principles (2016 & 2020), Global Governance Principles (2017), and Guidance on Investor Fiduciary Duties (2018).

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“Provisions

1. The board should assess the basis on which the company generates and preserves value over the long-term. It should describe in the annual report how opportunities and risks to the future success of the business have been considered and addressed, the sustainability of the company’s business model and how its governance contributes to the delivery of its strategy.”

In terms of corporate culture, board leadership, and company purpose, in this publication the FRC explicitly requires the board to assess upfront the basis on which their organization preserves value over the long-term.

In order to help ensure that organisations adopt a healthy balance between their focus on value creation and value preservation it is important that there is a balanced approach to both of these obligations within any future Corporate Reporting Principles.² With this in mind I have noted the following:

The discussion paper states that it is focused on the longer term and a wider stakeholder perspective. The desired more holistic approach to corporate reporting should therefore include reporting on both value creation and value preservation.

To help achieve this desired objective, I would suggest the following amendments:

- The Business Report would provide information that enables users to understand how the company creates and preserves long-term value in accordance with its stated purpose. We envisage this being similar to a concise Strategic Report, including financial and non-financial information (Executive Summary – page 3).
- We propose that the reporting network has a mandatory core, the Business Report, which brings together different aspects of value creation and preservation in a single, stakeholder-neutral document (An overview of the reporting network – page 14).

² In the January 2021 publication of the Revised International <IR> Framework, the IIRC now explicitly refers to value creation, preservation, or erosion in many areas throughout its Integrated Reporting document where its predecessor the 2013 publication previously only referred to value creation.

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- We believe that providing information that enables users to understand how a business generates and sustains value creation and preservation over the longer term is in the public interest and is a theme that should run through the Business Report (Business Report 3.7 – page 14).
- To provide information that enables users to understand how the company creates and preserves long-term value in accordance with its stated purpose (Objective for Business Report – page 14).
- demonstrate greater alignment between items that are currently reported elsewhere in annual reports, such as information on directors remuneration, to value creation and preservation (Business Report 5.7 – page 21).
- OBJECTIVE: To provide information that enables users to understand how the company creates and preserves long-term value in accordance with its stated purpose (5.8 Business Report – page 21).
- CONTENT THEMES: Performance (financial and non-financial), value creation and preservation (5.8 Business Report – page 21)
- MINIMUM CONTENT: Business Model (how it creates and preserves value) (5.8 Business Report– page 21)
- MINIMUM CONTENT: Explanation of how value is distributed to other stakeholders to sustain value creation and preservation, such as employees, local communities, and the natural environment, and how this contributes to sustaining value creation and preservation (5.8 Business Report – page 21)
- We would expect non-financial information to be included in the Business Report where it is material to meeting the report’s objective, which is to provide information that enables users to understand how the company creates and preserves long-term value in accordance with its stated purpose (6.12 – page 26).

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- Some of this information may be relevant to how the company creates, preserves and distributes value over the longer term. Therefore, there may be some overlap between the content of the Public Interest Report and Business Report (6.20 – page 27).
- The Business Report provides a mechanism for management to communicate information about how the company creates and preserves long-term value in accordance with its stated purpose. In a smaller company, where the communication channels with stakeholders are ‘close’, we would expect stakeholders to gather this information by interacting with the company itself, instead of through a separately prepared periodic report (8.3 – page 31).