Swimming in words
Surveying narrative reporting in annual reports
## Contents

1. Executive summary 1
2. Regulatory overview 3
3. Survey objectives 11
4. Overview of the annual report 12
5. Summary information 16
6. The business review 19
7. Principal risks and uncertainties 23
8. Key performance indicators 27
9. Corporate governance – Compliance 32
10. Corporate governance – Audit committees 38
11. Corporate governance – Going concern 41
12. OFR-style information 45
13. Investment trusts 51
   Appendix 1 – The missing links 58
   Appendix 2 – Glossary of terms and abbreviations 59
   How can we help? 61
   Related publications 62
1. Executive summary

This 2010 Deloitte survey of narrative reporting is remarkable for two reasons. The first is that it is issued at a time of political interest in the topic, more of which below. Political interest in narrative reporting is not unprecedented but the second reason is. The corporate reports equivalent of the four minute mile record has now been smashed. Annual reports have broken the ton. Their average length is now over 100 pages.

When the first of these surveys was produced in 1996, the average length of the annual report of a listed company was 44 pages. By 2000 it was 56 pages. In 2005, the average was 71 pages, increasing to 85 in 2006. From there, it increased steadily to 99 pages in the 2009 survey. It is now 101 pages. So there are plenty of words to be read.

The main findings from this year’s survey are positive.

• 93%, 94% and 90% of corporates provided respectively the required information about the environment, employees, and social and community issues. These percentages were a significant improvement on the 2009 equivalents of 87%, 89% and 70%.

• 90% of companies clearly identified key performance indicators, an increase from 84% in 2009. The average number of KPIs was seven.

• 4% of companies (2009: 7%) received a modified audit opinion relating to going concern. While it is positive that this number has decreased, more companies named the state of the economy as a key business risk. Three quarters of companies did so in 2010 compared with 63% of companies in 2009.

• 35% (2009: 32%) of companies complied fully with the UK’s Combined Code on Corporate Governance.

What comes through from reviewing practice is that companies are now getting to grips with changes to the rules that have been made in recent years. The FRC Guidance on going concern, which was issued finally in October 2009, is now clearly taken on board by companies. Companies are disclosing their business risks and providing key performance indicators. All corporates provide the directors’ responsibility statement introduced in 2007 by the EU’s Transparency Obligations Directive.

So then comes the August 2010 consultation from the Department for Business, Innovation and Skills on the future of narrative reporting. The Minister has set three objectives for this:

1. to drive up quality of narrative reporting to the level of the best, including on social and environmental issues;

2. to empower shareholders to step up and act as effective owners in the long term interest of the companies; and

3. to achieve coherence without increasing the regulatory burden on business.

As these reports have illustrated over the years, the UK is not short of rules on narrative reporting disclosures. Indeed one of the difficulties for corporates is keeping track of the many rules which come from different authorities. These rules have led to longer and longer reports so that the ton has now been broken. But are companies communicating better or just more?

Annual reports have broken the ton. Their average length is now over 100 pages.
Deloitte has published in September 2010 a joint research international report on narrative reporting, called “Hitting the notes, but what’s the tune?”, with the Association of Chartered Certified Accountants. It asked preparers in nine countries, including the UK, for their views on narrative reporting and how might it be improved. What emerged was that companies are trying to serve two masters at the same time. They want to inform shareholders of what is happening in the business. They need to satisfy regulators by meeting all the disclosure rules. To achieve succinctly and simultaneously both outcomes in the same report is a major challenge. Preparers would welcome more discretion and less regulation.

The 2010 annual report from the Financial Reporting Review Panel set out nine things which make a good annual report. These are below.

These nine principles seem to say it all. Armed with these principles, do companies need all the detailed rules?

Putting all this evidence together, the main message for the Minister may be that deregulation is necessary to improve communication. Otherwise, all will continue to be swimming in words.

To achieve succinctly and simultaneously both outcomes in the same report is a major challenge.
2. Regulatory overview

Narrative reporting by UK listed companies is subject to a complex tapestry of requirements, which has evolved significantly over the last few years. This section provides an overview of the regulations and guidance which have shaped some of the ‘front half’ of annual reports during the survey period, as follows.

Also discussed here are changes that may be made to the narrative disclosure regime in the foreseeable future. This publication excludes the directors’ remuneration report, the regulatory requirements for which are covered in the Deloitte publication, ‘Know the ropes – the remuneration committee knowledge’. Two other Deloitte publications, ‘Your guide – Executive directors’ remuneration’ and ‘Your guide – Board structure and non-executive directors’ fees’, published in September 2010, provide survey data on the directors’ remuneration report.

Directors’ report, including the business review

The general requirement to produce a directors’ report is contained in section 415 of the CA06. All quoted and unquoted companies (except those qualifying as small) are required to include a business review in their directors’ report. This includes subsidiary companies which do not qualify as small, even if they are wholly-owned. The purpose of the business review is to inform members of the company and help them assess how the directors have performed their duty to promote the success of the company.

Under s417, a business review should include a fair review of the company’s business and a description of the principal risks and uncertainties facing the company. The review required is a balanced and comprehensive analysis, consistent with the size and complexity of the business, of:

- the development and performance of the business of the company during the financial year; and
- the position of the company at the end of the year.

The requirements include, to the extent necessary for an understanding of the development, performance or position of the business of the company:

- an analysis using financial key performance indicators (KPIs); and
- where appropriate, analysis using other KPIs, including information relating to environmental matters and employee matters.

In practice the interpretation of “necessary” and “appropriate” varies greatly depending on the size and nature of the company’s business.

In addition, a quoted company’s business review must disclose:

- the main trends and factors likely to affect the future development, performance and position of the company’s business;
- information about:
  - environmental matters (including the impact of the company’s business on the environment);
  - the company’s employees; and
  - social and community issues,
including information about any policies of the company on these matters and the effectiveness of these policies; and
• information about persons with whom the company has contractual or other arrangements which are essential to the business of the company. Disclosure about a person is not required if the disclosure would, in the opinion of the directors, be seriously prejudicial to that person and contrary to the public interest.

Although the above disclosures need to be included only “to the extent necessary” for an understanding of the business, a company not discussing each of the specific areas in the second and third bullets above has to state expressly that it has not done so.

Companies are not required to disclose information about impending developments or matters in the course of negotiation if the disclosure would, in the opinion of the directors, be seriously prejudicial to the interests of the company. The exemption from disclosing information about persons with whom the company has contractual arrangements is somewhat different. Disclosure of information about such a person may be omitted only if it would be seriously prejudicial to that person and contrary to the public interest. Non-disclosure is not permitted simply because it would be prejudicial to the company.

Compliance with the statutory requirements of the business review is analysed in sections 6, 7 and 8 of this publication.

The Operating and Financial Review

The RS was originally issued in 1993 and subsequently revised in 2003 and 2006. While the Government had been planning to make compliance with the RS mandatory in 2005, this did not happen and thus adherence to the RS has remained voluntary throughout its existence. ‘On the horizon’ below provides details of the latest developments in this area.

If a narrative report is called an ‘Operating and Financial Review’ (OFR) there is an expectation that directors will have followed the RS and if this is not the case it would be useful to give the narrative report a different name, such as a ‘Business Review’. This publication refers to ‘OFR-style information’ which includes both formal OFRs and where companies have covered many of the items recommended by the RS within their chairman’s and/or chief executive’s statement, business review and financial review.

Corporate governance disclosures
Listed companies are required by the Listing Rules to make certain disclosures about corporate governance in their annual reports. At the heart of this requirement is the Code. A listed company incorporated in the UK is required to make a statement about how it has applied the main principles in the Code and a statement of compliance with the Code. The Code is supported by additional guidance on internal controls (the ‘Turnbull Guidance’) and audit committees (the ‘FRC Guidance on audit committees’). In addition, the Listing Rules state that there should be a statement by the directors that the business is a going concern with supporting assumptions or qualifications as necessary. These requirements are discussed in more detail in sections 9 to 11 of this publication.

Following amendments to the EU Fourth, Seventh and Eighth Directives, the Financial Services Authority (FSA) introduced new rules into the Disclosure and Transparency Rules (DTR) on corporate governance statements and audit committees. These rules apply to all UK companies, which have shares and/or debt admitted to trading on a regulated market in the EU, for periods commencing on or after 29 June 2008.

Listed companies must include a corporate governance statement in their directors’ report referring to:

• the corporate governance code that the company has decided to apply or is subject to under the law of the Member State in which it is incorporated (the Combined Code (now renamed) in the UK).
• an explanation as to whether, and to what extent the company complies with that code. To the extent that a company departs from the code, the company should explain the parts of the code from which it has departed and the reasons for doing so;

• a description of the main features of the company’s internal control and risk management systems in relation to the financial reporting process;

• major shareholdings and related matters already required by the Takeover Directive; and

• a description of the composition and operation of the company’s administrative, management and supervisory bodies and their committees.

For companies complying in full with the relevant provisions of the Code, many of these disclosures will already be in place. What is additional are the requirements to provide the information in a dedicated ‘corporate governance statement’ and to provide a description of the main features of the company’s internal control and risk management systems.

The company must ensure that, as a minimum, the relevant body should:

• monitor the financial reporting process;

• review and monitor the independence of the statutory auditor and in particular the provision of additional services to the company;

• monitor the effectiveness of the company’s internal control, internal audit function where applicable and risk management systems; and

• monitor the statutory audit of the annual and consolidated accounts.

The company must make a statement available to the public disclosing which body carries out the functions above and how it is composed. This statement can be included in any corporate governance statement.

The FRC Guidance on audit committees

In October 2008 the FRC issued a new edition of the Guidance on audit committees (formerly known as the Smith Guidance). The Guidance includes the following recommendations that the audit committee:

• explains to shareholders in the audit committee report how it reached its recommendation to the board on the appointment, re-appointment or removal of the external auditors;

• considers whether there might be any benefit in using firms from more than one network; and

• considers the need to include the risk of the withdrawal of their auditor from the market in their risk evaluation and planning.

The explanation to shareholders on how the audit committee reached its recommendation to the board on the appointment, re-appointment or removal of the external auditors should normally include supporting information on tendering frequency, the tenure of the incumbent auditor and any contractual obligations that acted to restrict the audit committee’s choice of external auditors.
**Going concern**

The Listing Rules and the Code require a statement by the directors that the business is a going concern, together with supporting assumptions or qualification as necessary. This requirement should be prepared in accordance with “Going Concern and Liquidity Risk: Guidance for Directors of UK Companies 2009” (the Guidance) published by the FRC in October 2009. This Guidance is effective for accounting periods ending on or after 31 December 2009.

The Guidance is based on three principles covering the process which directors should follow when assessing going concern, the period covered by the assessment and the disclosures on going concern and liquidity risk. The Guidance applies to all companies and in particular addresses the statement about going concern that must be made by directors of listed companies in their annual report and accounts.

The three key principles are:

1. **Assessing going concern:** directors should make and document a rigorous assessment of whether the company is a going concern when preparing annual and half-yearly financial statements. The process carried out by the directors should be proportionate in nature and depth depending upon the size, level of financial risk and complexity of the company and its operations.

2. **The review period:** directors should consider all available information about the future when concluding whether the company is a going concern at the date they approve the financial statements. Their review should usually cover a period of at least twelve months from the date of approval of annual and half-yearly financial statements.

3. **Disclosures:** directors should make balanced, proportionate and clear disclosures about going concern for the financial statements to give a true and fair view. Directors should disclose if the period that they have reviewed is less than twelve months from the date of approval of annual and half-yearly financial statements and explain their justification for limiting their review period.

The FRC believes that the impact of the new Guidance will be to support directors making high quality assessments of going concern and providing effective disclosures without increasing the costs for companies or users of financial statements. Section 11 of this publication considers how companies have adopted the new Guidance.

**Responsibility statement**

UK companies with shares and/or debt admitted to trading on a regulated market also have to comply with the requirements on periodic financial reporting in the DTR issued by the FSA. These rules are derived from the EU Transparency Obligations Directive. The DTR require most listed companies to prepare an annual management report. With one minor exception, these requirements duplicate the existing requirements within UK law for the directors’ report.

The responsibility statement required by the DTR must be made by the person(s) responsible within the company. This is usually the directors, but it is up to each company to decide which person(s) is (are) considered responsible. The responsibility statement must include the name and function of the person making the statement. Only one person is required physically to sign the responsibility statement.

Each person making a responsibility statement must confirm that to the best of his or her knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole; and

- the management report (the DTR term to describe the narrative part of the annual report) includes a fair review of the development and performance of the business and of the position of the company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.
The responsibility statement is discussed in section 6 of this publication.

ISA (UK and Ireland) 700 (revised) requires that the audit report contain a ‘statement that those charged with governance are responsible for the preparation of the financial statements’. Whilst this is not as strict as the previous ISA, which required that either the annual report or the audit report contain a description of those responsibilities, all of APB’s examples refer to a separate Directors’ Responsibilities Statement. The APB has not provided an example of a statement for a listed company, but market practice has generally been to continue preparing a similar statement to that used in previous years, combined with the statement required by DTR 4.1. This is presumably driven by a concern that removing the statement required under the old ISA could imply that directors were taking less responsibility for the accounts and reports.

**Directors’ liability for disclosures**

Section 463 of the Companies Act 2006 provides a level of protection for directors in respect of certain statements. It was introduced to encourage directors to provide more meaningful disclosures, particularly relating to the future. Under Section 463, a director may be held liable only to the company itself (although existing civil or criminal offences are unchanged) and not to individual shareholders or third parties. Such liability to the company would exist only if the director knowingly made a statement that was untrue or misleading, or was reckless as to whether this was the case. For an omission from the directors’ report, liability would arise only if he or she knew that the omission was ‘dishonest concealment of a material fact’.

This protection extends only to the directors’ report and directors’ remuneration report and any summary financial statement derived from those reports. Statements made outside these reports, such as within an OFR or corporate governance statement (whether under the Listing Rules or DTR 7.2), are not protected unless the OFR or other relevant statement has been scoped into the directors’ report by means of a clear cross reference.

**On the horizon**

This section provides an overview of the latest developments which will impact narrative reporting next year and beyond.

**Gender pay gap information**

The Equality Act 2010 gives the Government the power to make regulations requiring disclosure of gender pay gap information, defined as the size of the difference between men’s and women’s pay expressed as a percentage. This power will only be used if voluntary arrangements do not work. The Government’s aim is for employers regularly to publish such information on a voluntary basis. To give voluntary arrangements time to work, the Government does not intend to make regulations under this power before April 2013. The power would then be used only if sufficient progress on reporting had not been made by that time.

**Reporting greenhouse gas emissions**

In September 2009, the Department for Environment, Food and Rural Affairs (Defra), in partnership with the Department for Energy and Climate Change (DECC), published guidance for businesses and organisations on how to measure and report their greenhouse gas emissions. The guidance explains how businesses and organisations can measure and report their greenhouse gas emissions as well as set targets to reduce them. The guidance is aimed at all sizes of business as well as public and third sector organisations.

In addition, section 85 of the Climate Change Act 2008 commits the Government either to introduce regulation, under CA06 by April 2012, requiring corporate greenhouse gas reporting, or to explain why not.

The Government’s aim is for employers regularly to publish such information on a voluntary basis.
The new UK Corporate Governance Code
At the beginning of 2009 the Financial Reporting Council announced another review of the impact of the Combined Code on Corporate Governance. Views were invited on the following questions:

- Which parts of the Code have worked well? Do any of them need further reinforcement?
- Have any parts of the Code inadvertently reduced the effectiveness of the board?
- Are there any aspects of good governance practice not currently addressed by the Code or its related guidance that should be?
- Is the ‘comply or explain’ mechanism operating effectively and, if not, how might its operation be improved?

In addition Sir David Walker was asked by the Chancellor of the Exchequer to review the corporate governance arrangements of the UK banking industry. The terms of reference for this review included consideration of the following areas:

- the effectiveness of risk management at board level including the incentive in remuneration policy to manage risk effectively;
- the balance of skills, experience and independence required on the boards of UK banking institutions;
- the effectiveness of board practices and the performance of audit, risk, remuneration and nomination committees; and
- whether the UK approach is consistent with international practice and how national and international best practice can be promulgated.

Having considered the outcomes of its and Sir David Walker’s reviews, the FRC launched the new UK Corporate Governance Code in May 2010. The new Code aims to help company boards become more effective and more accountable to their shareholders.

Changes to the Code include:

- to improve risk management, the company’s business model should be explained and the board should be responsible for determining the nature and extent of the significant risks it is willing to take;
- performance-related pay should be aligned to the long-term interests of the company and its risk policy and systems;
- to increase accountability, all directors of FTSE 350 companies should be put forward for re-election every year;
- to promote proper debate in the boardroom, there are new principles on the leadership of the chairman, the responsibility of the non-executive directors to provide constructive challenge, and the time commitment expected of all directors;
- to encourage boards to be well balanced and avoid “group think”, there are new principles on the composition and selection of the board, including the need to appoint members on merit, against objective criteria, and with due regard for the benefits of diversity, including gender diversity; and
- to help enhance the board’s performance and awareness of its strengths and weaknesses, the chairman should hold regular development reviews with each director and FTSE 350 companies should have externally facilitated board effectiveness reviews at least every three years.

There are two key changes which will impact narrative reporting. Firstly, the preface to the new Code states that “chairmen are encouraged to report personally in their annual statements how the principles relating to the role and effectiveness of the board (in Sections A and B of the new Code) have been applied”. It is hoped that this will give investors a clearer picture of the steps taken by boards to operate effectively but also, by providing fuller context, it will make investors more willing to accept explanations when a company chooses to explain rather than to comply with one or more provisions.
Secondly, there is a new requirement (Code provision C.1.2) that there should be an explanation of the basis on which the company generates or preserves value over the longer term (the business model) and the strategy for delivery of the objectives of the company. The new Code states that it would be desirable if the explanation were located in the same part of the annual report as the business review required by section 417 of the CA06. It also refers preparers to the guidance contained in paragraphs 30 to 32 of the ASB’s Reporting Statement: Operating and Financial Review.

The new Code applies to all companies with a premium listing of equity shares with financial years beginning on or after 29 June 2010 but boards are encouraged to take positive and constructive early action. The Deloitte publication ‘Setting the tone – a new focus for governance’ provides suggested actions and questions to ask on a practical route to implementation.

The future of narrative reporting

Further to a commitment in the Coalition Agreement to “reinstate an Operating and Financial Review 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”, the Department for Business, Innovation and Skills (BIS) issued in August 2010 a consultation paper on the future of narrative reporting.

The objectives of the consultation are to look at ways to drive up the quality of company reporting to the level of the best and thereby to enable stronger and more effective shareholder engagement. The consultation paper is exploring a number of options, regulatory and non-regulatory, to achieve the objectives. The consultation focuses in particular on the business review provisions of the CA06 but also, as part of its exploration of wider narrative reporting, it looks at issues relating to the directors’ remuneration report. The consultation asks a number of questions including:

- are company directors providing useful and relevant information on the company’s forward-looking strategy and principal risks and uncertainties?
- does the information provided reflect the issues discussed by the directors in board meetings?
- would a statutory reporting standard help to improve the quality of reporting?
- should there be a shareholders’ advisory vote on the Business Review?
- are there non-regulatory solutions to increasing quality through better guidance or publicising excellence in business reports?
- do the current disclosure requirements provide clear and usable information about the process by which directors’ remuneration is decided?

The consultation period closed on 19 October 2010 and Deloitte provided the results of this survey to BIS to assist with the thinking in this area.

New disclosures for audit committees on the provision of non-audit services

The FRC has published for consultation updated guidance to audit committees on determining whether a company’s auditor should be permitted to provide particular non-audit services. The FRC believes that there is a perception that auditor objectivity and independence is adversely affected by the provision of non-audit services and that improved transparency and governance would address these concerns. Changes are proposed to the FRC’s Guidance on audit committees including the following:

- more prominence to be given to the importance of non-audit services in the assessment of the objectivity and independence of the company’s auditor;
- new policy and procedure guidance relating to the practice of seeking specific approval from audit committees for particular categories (and values) of non-audit services to be supplied by the auditor;
- additional guidance to help the audit committee distinguish between those non-audit services which are closely related to an audit and are a very low threat to auditor objectivity and those where the threats need more careful consideration;
• guidance to assist audit committees on the
  judgement as to the cost and efficiency benefits and
  the real or perceived threats to auditor independence
  which are associated with the auditor providing
  services which fall outside the audit and audit related
  services; and

• improved disclosures on the nature of services
  provided by the auditor and an outline of the reasons
  why the audit committee decided to purchase non-
  audit services, other than audit related services, from
  the auditor rather than from another party.

**IASB guidance on management commentary**

As noted in last year’s survey, the IASB is undertaking
a project on management commentary. The objective of
this project is to develop a model for a narrative report,
which would accompany but be presented outside of
the financial statements, setting out management’s
explanation of the enterprise’s financial condition,
changes in financial condition, results of operations,
and causes of changes in material items. The output of
the project will be a ‘best practice’ guidance document
rather than a standard.

An exposure draft of the guidance was published last
year and it is expected that the final document will
not be substantially different from the exposure draft.
The final document is expected to be published at the
end of October.

---

**The Turnbull Guidance on internal control**

The FRC has committed to another review of the
Turnbull Guidance on internal control, beginning later in
2010. This guidance has not been updated since 2005
and needs to reflect the revised Code’s principles on
risk. It will not be a back-to-basics review but there may
be some new disclosure requirements and some
consequential amendments to the Guidance on audit
committees.

---

**The objective of this project is to develop a model for a narrative report, which would accompany but be presented outside of the financial statements . . .**
3. Survey objectives

The main objectives of the survey were to discover:

- what narrative reporting listed companies have provided in their annual reports;
- how disclosures varied depending on the size of the company;
- how companies met the requirements of the Companies Act 2006 to provide a business review within the directors’ report;
- to what extent companies have adopted the recommendations in the ASB’s best practice Reporting Statement: Operating and Financial Review (RS); and
- how the results compared with similar surveys performed in previous years.

The annual reports of 130 listed companies were surveyed to determine current practice. Consistent with the approach adopted in Deloitte’s 2009 survey, the companies were split into two groups being 30 investment trusts and 100 other companies. Investment trusts are those companies classified by the London Stock Exchange as non-equity or equity investment instruments (this excludes real estate investment trusts). They have been treated as a separate population due to their specialised nature and the particular needs of their investors.

The sample is, as far as possible, consistent with that used in last year’s survey. As a result of takeovers and mergers over the last twelve months, the sample could not be identical. Replacements and additional reports were selected evenly and at random from three categories being those within the top 350 companies by market capitalisation at 30 June 2010, those in the smallest 350 by market capitalisation, and those that fall in between those categories (the ‘middle’ group). Furthermore, because of clustering within the top 350 companies’ category, five companies were replaced with the new ones chosen at random.

The comparatives for 2009 were then reworked to use the same companies in both years in that category.

The annual reports used were those most recently available and published in the period from 1 August 2009 to 31 July 2010.

As noted above the findings for investment trusts are analysed separately within this publication. Sections 4-12 summarise the results for the 100 companies excluding investment trusts and section 13 reviews the 30 investment trusts.
4. Overview of the annual report*

- Annual reports continue to increase in length and the average is now 101 pages.
- Narrative reporting makes up 51% of annual reports, a slight decrease from 52% in 2009.
- Companies are reporting quicker, taking an average (mean) of 75 days to approve their annual reports (2009: 76 days), with all companies achieving compliance with the DTR reporting requirements (2009: 99%).

Length of the annual report

Over recent years, it has been noted that the average length of annual reports has been on the increase. That trend has continued in 2010, with a mean average length of annual reports of 101 pages (2009: 99).

The median average (i.e. the middle value when the report lengths are ranked in numerical order – see below) length of annual reports is 90 pages (2009: 85) – an increase of 6% year on year. Figure 1 shows how the median average has changed over the past five years.

Not surprisingly, the longest average (median) reports are those of the top 350 companies (117 pages) whilst the shortest reports are produced by the smaller companies (88 pages for the middle companies compared with 60 pages for the smallest 350 companies) – see Figure 2.

The increase in the length of the annual report is due to the additional disclosure requirements introduced in recent years, with the new accounting standard IFRS 8 on operating segments and more information on going concern and risks likely to be the principal factors contributing to the increase from 2009 to 2010.

* This section analyses the findings for all companies other than investment trusts
The longest report (490 pages) came from the sample of top 350 companies by market capitalisation, while the shortest report (33 pages) came from the sample of the smallest 350 companies by market capitalisation. This was also the case in the prior year, when the longest report was 469 pages and the shortest was 32 pages.

**Balance of narrative and financial reporting**

For the purposes of this survey, the ‘narrative’ section (or ‘front half’) of the annual report is defined as all the pages in the annual report excluding the audited financial statements and independent auditors’ report. The narrative reporting typically includes some, or all, of the following sections:

- Summary information;
- Chairman’s statement;
- Chief executive’s statement;
- Business review;
- Financial review;
- Corporate social responsibility (CSR) statement;
- Directors’ report;
- Corporate governance statement;
- Directors’ remuneration report; and
- Statement of directors’ responsibilities.

When considering the length of the annual reports, median averages have been considered, in addition to arithmetic means. The reason for this is that the arithmetic mean could be considered misleading (see Fig. 3): the range of annual report lengths is not normally distributed, with a small number of lengthy outliers skewing the arithmetic mean upwards. The white boxes in the figure below indicate where the middle 50% of the sample are distributed, while the two ‘whiskers’, or tails, show the range of the upper quartile (longest 25% of reports) and the lower quartile (shortest 25% of reports). As shown in the box plots below, the majority (75%) of reports are in the range of 33 – 108 pages (2009: 32 – 102 pages), but the upper quartile (the upper 25% of the sample) are significantly longer, ranging from 108 pages to 490 pages (2009: 102 – 469 pages). It is these lengthy reports which skew the arithmetic mean upwards.

Given the relatively small size of our sample (100 companies), it is likely that the modal average (i.e. the most common report length) could also be relatively misleading, and therefore the median report lengths have been considered for the analysis within the remainder of this chapter.
The balance of narrative pages and financial statements has remained relatively consistent with the prior year. As shown in Figure 4 below, narrative reporting now constitutes 51% of the annual report (2009: 52%).

Figure 4. What is the balance of narrative and financial reporting in the annual report?

The length of the narrative reporting sections within the annual reports has thus increased roughly in line with the overall increase in the length of the annual reports discussed above. This is shown in Figure 5, above, which shows that the median length of narrative sections has remained flat (43 pages in both 2010 and 2009), while the inter-quartile range has increased from 31 – 54 pages in 2009 to 30 – 56 pages in 2010. The longest narrative section in the sample was 368 pages (2009: 351 pages) while the shortest was 11 pages (2009: 12 pages).

Figure 5. What is the range of narrative reporting length in 2010 and 2009?

### Speed of reporting

All companies included in the survey are required to comply with the DTR requirement to publish their annual report within four months of their year end. The potential impact of non-compliance with this rule is the suspension of shares.

Compliance with this requirement was good in the current year, with all of the companies in the sample meeting the deadline (compared with 99 out of 100 companies meeting the requirement in 2009).

The mean average time for report approval was 75 days which was slightly quicker than in 2009 where the mean average was 76 days. The profile of speed of approval is comparable with the prior year: 57% of companies approved their annual reports within 75 days of their year-end (2009: 57%), while 21% of companies took over 90 days to approve their annual reports (2009: 21%).
The top 350 companies were quickest, on average, while the smallest 350 companies were slowest (see Fig. 6). The quickest report was approved within 42 days of the year end (2009: 43 days), while the slowest report took 121 days to be approved (2009: 141 days). Middle sized companies were slightly quicker this year, taking 71 days on average (mean, 2009: 76), while larger companies were consistent with the prior year, taking 62 days on average (mean). The smaller companies showed a slight decrease in performance, taking 92 days on average (mean) compared with 91 days in 2009.

**Presentation**

As in prior years, many companies invested in producing glossy annual reports. 75% of companies presented their annual reports in a manner which was visually interesting. Again, the largest companies were the top performers, with 88% of the sample of top 350 companies producing interesting-looking reports, while only 61% of the smallest 350 companies produced an eye-catching annual report. It should be noted that the appeal of an annual report is a subjective assessment. Some of the criteria used to determine whether a report was well presented were the structure of the report, clear headings, and the use of colour, pictures, tables and charts.

Figure 6. How quickly was the annual report approved in 2010, compared with 2009?

![Graph showing the average number of days for approval of annual reports for different company sizes in 2010 and 2009.](image)

… the largest companies were the top performers, with 88% of the sample of top 350 companies producing interesting-looking reports …
Many companies choose to include a summary page at the start of their annual report. This is an option, rather than a regulatory requirement, but can be a useful tool to bring key information to the users’ attention.

In 2010, 83% of the companies surveyed included summary information, in one form or another (2009: 89%). 96% of summary pages included financial data.

Of those companies showing financial data in a summary page, 67% gave prominence to ‘adjusted’ financial measures.

**The summary information presented varied in content and structure …**

- The number of companies presenting summary information at the start of their annual reports has declined over the year from 89% to 83%.

- 96% of summary pages included financial data.

- Of those companies showing financial data in a summary page, 67% gave prominence to ‘adjusted’ financial measures.

---

**Information shown on the summary page**

The summary information presented varied in content and structure: some contained a simple table of key financial data; others used the summary to provide information about the structure and business of the organisation; and other summaries identified the key strategies, objectives and achievements during the year. Of those who presented summary information, 96% (2009: 91%) of companies chose to include financial data, 86% (2009: 90%) included narrative and 76% (2009: 74%) presented KPIs (as identified as KPIs later in the report).
Two good examples of the presentation of summary information can be found in the annual reports of Pearson plc and National Grid plc. Pearson provides more narrative information on divisions and markets with less emphasis on financial data and National Grid provides a mix of narrative and financial information plus clear cross references to further information in the annual report on particular areas included in the summary information.

Figure 8. What kind of information is presented in the summary page(s)?

Percentage of companies presenting this information

<table>
<thead>
<tr>
<th>Information Type</th>
<th>Total</th>
<th>Top 350 Companies</th>
<th>Middle</th>
<th>Smallest 350 Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overview</td>
<td>90</td>
<td>90</td>
<td>80</td>
<td>70</td>
</tr>
<tr>
<td>Financial Information</td>
<td>80</td>
<td>80</td>
<td>70</td>
<td>60</td>
</tr>
<tr>
<td>KPIs</td>
<td>70</td>
<td>70</td>
<td>60</td>
<td>50</td>
</tr>
</tbody>
</table>

Pearson plc Annual report and accounts 2009
Use of adjusted measures

While summary information can be useful to the users of the annual reports by drawing their attention to key events or results, there is a risk that the summary information can also be potentially misleading. As noted above presentation of summary information is not a regulatory requirement and so there are no rules on the content of such information. Of those companies who presented financial summary data, 71% (i.e. 56 companies) gave ‘adjusted’ financial measures such as pre-exceptional charges or before amortisation charges, impairment charges and the like. Of those 56 companies presenting ‘adjusted’ measures in their summary pages, the majority (67%) did not present the related statutory numbers within the summary page also (i.e. the nearest equivalent measures including items such as exceptional charges, amortisation charges and impairment charges).

The summary information provided by BT Group plc is a good example of the presentation of adjusted and reported results for all key measures.
6. The business review*

- 98% (2009: 99%) of companies formally identified a section called the ‘business review’.

- 66% of companies chose to disclose the required information in a section distinct from the directors’ report.

- Required information about the environment, employees and social and community issues were disclosed by 93%, 94% and 90% of companies, respectively.

- All companies (2009: 87%) surveyed included a statement of directors’ responsibilities.

Under section 417 of the CA06, all companies are required to include a business review in their directors’ report, unless they qualify as small. The review should include a fair review of the business and a description of the principal risks and uncertainties facing the company.

98% of the companies surveyed identified narrative which met the definition of a business review (2009: 99%). Both of the companies that failed to identify a business review had clearly included the requirements within an extensive directors’ report, but had not clearly identified any particular sections as fulfilling the business review criteria.

**Location of the business review**
The CA06 requirement states that the business review should be incorporated into the directors’ report. Most of the companies surveyed (67%) satisfied this requirement by including a cross-reference in the directors’ report to the statements within the front half of the annual report which contain the required disclosures for the business review. 17% of the companies surveyed included a cross-reference, as described above, and included some of the business review requirements within the body of the directors’ report. Only 14% included the entire business review in the body of the directors’ report.

The difference in choice of location for the business review varied with the size of the company, as shown in Figure 9. The middle-sized and smallest companies were more likely to split the business review between the directors’ report (DR) and elsewhere in the narrative (24%, in both cases) in comparison with the largest companies (3%).

![Figure 9. Where is the business review positioned?](image)

Certain aspects of the business review disclosures have been discussed elsewhere within this report.

**Operating and financial review**
The inclusion of a formal operating and financial review (OFR) remains voluntary. 13 companies presented a narrative section titled “Operating and Financial Review” in 2010 and OFR-style information is analysed in further detail in section 12.

**Principal risks and uncertainties**
95 companies clearly disclosed their principal risks and uncertainties, which are discussed in further detail in section 7.

* This section analyses the findings for all companies other than investment trusts
Key performance indicators

The CA06 requires an entity to include an analysis using financial and non-financial KPIs if this is considered necessary to provide an understanding of the business. 90 companies identified KPIs, with the majority of these being located in the business review. KPIs are discussed in more detail in section 8.

The rest of this section is devoted to analysing the other disclosure requirements of the business review and how these have been addressed by companies in 2010.

Performance of the business

As noted above, 98% of the companies surveyed provided a distinct section called a business review. 98% of companies included negative points in their business review, and therefore appeared to present a ‘balanced’ review of the business. Two companies did not include any negative points in their business review, despite their results suggesting otherwise, and therefore it is unlikely that the narrative reporting for these two companies could be deemed to be entirely ‘fair’ (a requirement of the business review).

94% of the companies surveyed made reference to trends and factors, likely to impact future performance of the company, within the business review (2009: 92%) as required by the CA06. Of the six companies which did not include this information in the business review, four included such references elsewhere in the narrative. This represents an improvement in comparison with 2009, when only two out of eight of those companies failing to include future trends and factors in their business review included this information elsewhere in the front half of the financial statements.

Of the companies surveyed, 69% included some reference to the long term success of the company (excluding any references to long term incentives for directors). The largest companies were particularly good at making such references, with 88% of large companies referring to long term success or strategies for long term success, compared with 61% of middle-sized companies and 58% of the smallest companies.

Contractual arrangements

The CA06 stipulates that information about persons with whom the company has contractual or other arrangements essential to the business of the company should be disclosed in the business review. 24% of companies (2009: 24%) included reference to contractual arrangements (either to disclose such arrangements or to state that there were none). Interestingly, compliance with this requirement has improved within the largest and smallest companies (44% and 15%, respectively, compared with 32% and 12% in 2009), at the expense of compliance within the middle group (12% of whom referred to contractual arrangements in 2010, compared with 27% in 2009).

Domino Printing Sciences plc provides an example of disclosure of essential contractual arrangements and Persimmon plc provides an example of a statement that there are no essential contracts or arrangements.
CAO6 requires a negative statement where the business review does not include any information about contractual or other arrangements which are essential to the business of the company.

It is difficult to say whether the 76% of companies have failed either to disclose essential contractual arrangements or to state that they do not have any such arrangements.

Corporate and social responsibility

Under the CAO6, companies are required to discuss additional information about environmental matters, the company’s employees and community and social issues. In addition there are two new disclosure areas this year. As set out in section 2, the Department for Environment, Food and Rural Affairs has issued guidance for companies on disclosing information about their greenhouse gas emissions. In addition, the Equality Act 2010 recommends that companies disclose gender pay gap information. Disclosure of this information is not mandatory at present but it is interesting to know how many companies are already attempting to tackle these areas and the nature of the disclosures.

None of the companies surveyed disclosed any gender pay gap information. However, 37% of companies made an attempt to disclose CO2 emissions, with 31% making disclosures with no reference to the DEFRA guidance and 6% disclosing and referring to the DEFRA guidance. An example disclosure using the DEFRA guidance is taken from MITIE Group plc.

The largest companies performed best in this area, with 71% of the top 350 companies making disclosures about their emissions, compared with a third of the middle group and 6% of the smallest 350 companies (none of whom made reference to the DEFRA guidance).
Most companies chose to include these disclosures in a Corporate Social Responsibility (CSR) statement and formats varied from tabular or diagrammatic disclosures to sections of prose.

Figure 12. How many companies made disclosures about the environment, employees and social and community issues?

<table>
<thead>
<tr>
<th></th>
<th>2010</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Environment</td>
<td>93%</td>
<td>87%</td>
</tr>
<tr>
<td>Employees</td>
<td>94%</td>
<td>89%</td>
</tr>
<tr>
<td>Social &amp; community</td>
<td>90%</td>
<td>70%</td>
</tr>
</tbody>
</table>

A good example was the Corporate Responsibility and Sustainability statement included within the annual report of Cobham plc. In addition to providing narrative descriptions and analysis, Cobham also provided the table set out below which linked each focus area with the relevant performance indicators, objectives, progress, targets and the company’s strategic objectives.

**Directors’ responsibilities statement**

The DTR require that all companies must provide a statement of directors’ responsibilities. All of the companies surveyed complied with this requirement in 2010, compared with just 87% in 2009. This marks a clear improvement in the current year.
7. Principal risks and uncertainties*

- 95% of companies (2009: 96%) clearly identify their principal risks and uncertainties.
- An average of eight risks (2009: 8) is disclosed per company.
- 74% of companies (2009: 61%) identifying principal risks identify the state of the economy as a key risk.
- 18% of companies identifying principal risks provide only generic descriptions of these risks.

The Disclosure & Transparency Rules (DTR) and the Companies Act 2006 (CA06) require directors to disclose the principal risks and uncertainties faced by the business in the annual report. Section 417 of CA06 requires that a description of these principal risks and uncertainties is included and DTR 4.1 requires the directors to confirm that this description is included within the review of the business.

Overall, 95 of the 100 companies sampled clearly identified their principal risks and uncertainties. Of the remaining five companies, three were in the middle 350 category and two were in the smallest 350.

Number of risks and uncertainties

The number of risks and uncertainties identified is in line with the findings of the 2009 survey. The overall average number of risks identified in both 2010 and 2009 was eight. On average, in both 2010 and 2009, the largest 350 companies identified eleven risks; the middle group identified an average of eight risks; and the smallest 350 averaged six risks.

The largest number of risks identified in the 2010 sample was 28 (2009: 30) by a company in the top 350. Having such a large number of identified risks can be seen as not in the spirit of disclosing principal risks and the FRRP has been picking up on this. As stated above, five companies (three from the middle group; two from the smallest 350) failed to identify any risks, whilst two companies (2009: three companies), both of which were in the smallest category, identified just one risk each.

Most companies, however, have complied with the spirit of disclosing principal risks by identifying between 5 and 11 risks, compared with between 4 and 10 risks in 2009.

In its annual report for 2010 and in a change to prior reports where the focus has been on non-compliance, the FRRP has highlighted good practice. The FRRP annual report can be accessed at http://www.frc.org.uk/images/uploaded/documents/ANNUAL%20REPORT%202010%20-%20FINAL1.pdf. The FRRP has set out the characteristics which it believes “make for a good annual report”. For principal risks and uncertainties the following characteristics are suggested:

“The risks and uncertainties described in the business review are genuinely the principal risks and uncertainties that the Board are concerned about. The descriptions are sufficiently specific that the reader can understand why they are important to the company. The links to accounting estimates and judgements are clear.”

* This section analyses the findings for all companies other than investment trusts.
Location
As noted above, DTR 4.1 requires that the description of the principal risks and uncertainties is included in the business review section of the directors’ report. Of the 95 companies that disclosed their principal risks and uncertainties, 61 (i.e. 64%) described their principal risks and uncertainties in a stand-alone business review, cross-referencing them from the directors’ report. 27 companies (i.e. 28%) described the risks directly in the directors’ report.

Four companies (two from the top 350 and one each from the middle and smallest categories) identified their risks within their corporate governance statement. However, these were clearly referenced from the directors’ report. Three companies (two from the middle category and one from the smallest 350 category) disclosed their risks in a separate statement within the narrative reporting that was neither part of the business review nor part of the directors’ report (for example one of the companies included the risks in its ‘Financial Review’ but this statement is excluded from the references in the directors’ report to those statements comprising the business review).

It is encouraging to note that most companies (92 companies being 97% of those identifying principal risks and uncertainties) adhered to the CA06 requirement by presenting the risks and uncertainties in the directors’ report, albeit with most clearly cross-referencing to other locations.

Type of risk and uncertainty
96% of companies (2009: 91%) who clearly described their principal risks and uncertainties covered strategic, commercial and operational risks as well as financial risks. All of the top and middle 350 companies identifying principal risks covered all types of risks, while 87% of the smallest 350 companies discussed all types.

The common risks identified were categorised as follows:

- State of the economy – including the impact of the credit crunch.
- Operational issues – factors directly affecting operational output.
- Financial instrument (IFRS 7) risks – market, credit and liquidity risks.
- Regulation and legislation – including political risk abroad.
- Demand – specific factors affecting demand, including competition.
- People – loss of key personnel.
- Financing issues – factors directly affecting the company’s ability to raise finance or meet loan covenants in the future.
- Foreign exchange – exposure to movements in foreign exchange rates.
- Legal action and litigation – uncertainty regarding outcome.
- Environmental issues – including natural disasters as well as CSR-type risks.
- Reputation and brand – loss of customer goodwill.
• Pensions – factors affecting pension contributions or liabilities.
• Cost of raw materials – movement in commodity prices or other direct costs of sales.
• Tax – including changes in tax rates and legislation.
• Research and development – including failure of R&D projects.

Perhaps unsurprisingly, the state of the economy remains the most common risk identified, with 74% of those companies identifying principal risks and uncertainties identifying this as a principal risk. This is an increase in comparison with last year, where 63% of companies identified the state of the economy as a principal risk. In contrast to the prior year, this now appears to be a key risk across all three categories of company, with 76% of the top 350 (2009: 82%), 77% of the middle 350 (2009: 52%) and 68% of the smallest 350 companies (2009: 48%) identifying the state of the economy as a key risk.

The second most common risks were operational issues and IFRS 7 risks, both of which were identified by 69% of those companies identifying principal risks and uncertainties. Most companies identified some sort of technological failure as being a significant risk to the company’s ability to continue operations. The majority of companies also identified credit risk (to themselves or counterparties) as being a fundamental risk to the company’s performance.

Regulation and legislation risks were the next most common risk, with 63% of those companies identifying principal risks and uncertainties identifying some kind of risk in this category. This was the most common risk category for the top 350 group of companies in 2010, with 82% of companies identifying a regulatory or legislative risk. Savills plc included both such risks in their risk disclosures.

<table>
<thead>
<tr>
<th>Key risk</th>
<th>Description</th>
<th>Mitigating factors</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maintaining standards of professional, regulatory and statutory compliance</td>
<td>We are required to meet a broad range of regulatory compliance requirements in each of the markets in which we operate. For example, in the UK, the Financial Services Authority (FSA) regulates the conduct of Savills Private Finance, Savills Capital Advisors and Cordelia Savills, and the insurance mediation businesses in our Commercial and Residential businesses. In addition, the UK Office of Fair Trading regulates our Residential business in the UK. A number of the services we provide through our Commercial and Residential businesses are also regulated by The Royal Institution of Chartered Surveyors (RICS). Also, a number of our employees are qualified members of RICS. Failure to satisfy regulatory compliance requirements may result in fines being imposed, adverse publicity and brand reputation damage and ultimately the withdrawal of regulatory approvals.</td>
<td>All areas relating to professional, regulatory and statutory compliance have benefitted from the continuing update of our Group Policy Framework which defines the compliance standards we expect from our businesses. In support of this Framework each of our businesses have their own regulatory and statutory compliance resources in place and they maintain the internal processes and controls required to fulfil our compliance obligations. Our compliance environment, at all levels, is subject to regular review by internal audit and other assurance providers.</td>
</tr>
</tbody>
</table>

Savills plc Report and Accounts 2009
Figure 15. What are the main categories of risks that are identified?

Percentage of companies who identified risks and uncertainties

Description of risks and their mitigation

In its 2010 annual report the FRRP has made it clear that it expects an indication of the measures taken to manage principal risks and uncertainties to be given. Unfortunately, this survey has found that there has been a slight deterioration in the proportion of companies who attempted to describe their strategies for mitigating the principal risks and uncertainties they had identified (84% in comparison with 88% in the prior year).

In addition, a significant minority (18%) provided only generic descriptions of risks, with no discussion of why those risks were important specifically to the company. This was most prevalent in the smallest 350 companies, with 32% of the companies providing only generic descriptions. The top 350 companies performed better with only 6% of the companies providing generic risk descriptions, with 17% of middle companies doing so. The FRRP is very clear on this issue: “Good descriptions which comply with the law say why they apply to the company, and why they are important”. Cobham plc represents an example of good practice.

Cobham plc Annual Report and Accounts 2009
8. Key performance indicators*

- 90% of companies clearly identified key performance indicators, an increase on 84% in 2009.
- An average of seven KPIs are disclosed (2009: eight).
- 65% of the KPIs identified were financial in nature, which is in line with the prior year.
- Only 17% of companies identified targets for their KPIs (2009: 14%), making it difficult to assess performance.
- Only 17% of companies provided a clear link between KPIs and their strategic aims and objectives.

The identification of KPIs is a requirement under the CA06. An analysis using financial and, where appropriate, ‘other’ KPIs is required to the extent necessary to provide the users of the annual report with an understanding of the development, performance and position of the company. ‘Other’ KPIs are non-financial. The CA06 notes that these may include information relating to environmental, employee and customer matters.

Identifying KPIs
For the purposes of this survey, KPIs were deemed to be any measure identified explicitly as such within the narrative of the annual report. There has been an improvement in 2010 with 90% of the companies surveyed clearly identifying KPIs (2009: 84%). 97% of the largest companies clearly identified KPIs (2009: 94%), while the smallest companies have also improved with 85% clearly identifying KPIs compared with 79% in 2009. For the second consecutive year, the greatest improvement was noted in the middle group, 88% of whom clearly identified KPIs in 2010 compared with 79% in 2009.

Of the ten companies in the sample who failed to identify specifically KPIs, only one included a statement as to why KPIs were not discussed (the stage of development of the company was the reason given). Most of the companies surveyed (92%) presented certain information as if it were a KPI although they did not specifically refer to it as such. The most common example of such a situation is where a financial or non-financial statistic, such as revenue growth or profit before tax, has been given particular prominence in the annual report (frequently on the summary page) and then is subsequently discussed as part of the business review narrative.

Location of KPIs
The remainder of the analysis in this chapter will focus on those KPIs which were specifically identified as such somewhere within the annual report. 62% of KPIs identified were included within the business review, where the measures were discussed and analysed. For 28% of companies, KPIs were identified in the directors’ report. In these cases, the reader was often referred to the business review for further analysis.

* This section analyses the findings for all companies other than investment trusts
Nature and number of KPIs identified

Overall, 65% of KPIs were financial in nature while 35% were non-financial measures, which is consistent with the balance of financial and non-financial KPIs identified in 2009. However, the average company identified seven KPIs in total in 2010, a decline from 2009 when the average company identified eight.

The larger companies not only tended to show more KPIs than the smaller companies, identifying an average of ten compared with an average of seven from the middle group and five on average within the smallest companies, but also tended to show the greatest proportion of non-financial measures – see Figure 19.

The range of measures identified as KPIs are largely similar to the prior year, as the figure below indicates. The most common measures related to profitability, with over 90% of those companies identifying KPIs including at least one measure of profitability. There are still relatively few companies identifying employee (27%) or environmental (21%) measures within their KPIs, with much of their discussion on these matters being confined to the corporate responsibility statement.

KPIs on cash and debt measures are likely to be of particular interest to users of the annual report in the current economic climate.
Box-ticking or valuable analysis?

There are two facets to the CA06 requirement on KPIs. Firstly it requires that sufficient KPIs are identified and secondly these are presented in such a way that the reader can measure effectively the development, performance and position of the business. As noted in previous years, many companies failed to provide enough information to give a full understanding of why the company had selected a particular KPI and what the factors driving the KPIs are.

The Reporting Statement (RS) recommends disclosure of the following items which may be considered to be best practice:

- definition and calculation method;
- purpose;
- source of data;
- reconciliation to amounts included in the financial statements;
- quantification or commentary on future targets;
- any changes to KPIs compared to previous financial years; and
- comparatives.

39% (2009: 31%) of companies defined or disclosed the calculation method for their KPIs. Only 24% of companies clearly gave the purpose of the KPIs they had selected (2009: 24%). In addition only 17% made reference to targets for their KPIs (a slight improvement from 14% in 2009), making it difficult for readers to assess a company’s performance. 59% of companies attempted to provide a link between the KPIs chosen and the directors’ strategies and objectives.

As noted in previous years, many companies failed to provide enough information to give a full understanding of why the company had selected a particular KPI …
MITIE Group plc and Cobham plc provide examples of good practice in the disclosure of key performance indicators. These companies provide a clear link between the chosen KPI and strategy plus comparative information and targets.

Figure 21. How much analysis and explanation is given alongside the KPIs identified?
The larger companies not only tended to show more KPIs than the smaller companies … but also tended to show the greatest proportion of non-financial measures.
9. Corporate governance – Compliance*

- 35% (2009: 32%) of companies comply fully with the provisions of the Combined Code.
- The chief executive is also the chairman for 13% of companies.

Statement of compliance
Listing Rule 9.8.6 requires that UK incorporated listed companies make a statement as to whether or not they have complied with the provisions set out in Section 1 of the Code. Consistent with 2009, 99% of the companies surveyed included a compliance statement. The one company which did not provide a statement of compliance is one of the smallest 350 companies.

Figure 22 shows how companies are complying with the Code in each of the three groups by market capitalisation. 35% (2009: 32%) of companies complied in full with all the provisions and 64% (2009: 67%) partially complied. 47% (2009: 38%) of the top 350 companies applied all provisions of the Code compared to 45% (2009: 39%) of the mid tier companies and 15% (2009: 18%) of the smallest 350 companies.

Figure 23. Where is the statement of compliance positioned?

Where a company has not complied with all the provisions of the Code, or complied with them for only part of the year, the Listing Rules require the company to set out those provisions. Figure 24 shows the most popular non-compliances for the smallest 350 companies which have reported partial compliance. Amongst the smaller companies the size of the company was the most common reason cited for not complying with specific provisions.

* This section analyses the findings for all companies other than investment trusts
Figure 24. What are the most common non-compliances for the bottom 350 companies?

Of the 53% of the top 350 companies who reported partial compliance with the Code, 61% stated that they did not comply with Code provision A.3.2 which requires that at least half the board, excluding the chairman, should comprise non-executive directors determined by the board to be independent.

The only other recurring non-compliances among the top 350 companies were in relation to Code provision C.3.1 (the composition of the audit committee) (28%) and Code provision A.3.3 (the role of the senior independent director) (17%).

Amongst the 18 companies from the middle tier reporting partial compliance, the most common areas of non-compliance were as follows:

<table>
<thead>
<tr>
<th>Code provision</th>
<th>Percentage of mid-tier companies reporting non-compliance</th>
</tr>
</thead>
<tbody>
<tr>
<td>B.2.1 Composition of the remuneration committee</td>
<td>28%</td>
</tr>
<tr>
<td>C.3.1 Composition of the audit committee</td>
<td>22%</td>
</tr>
<tr>
<td>A.3.2 At least half the board should be independent</td>
<td>17%</td>
</tr>
<tr>
<td>A.6.1 Performance evaluation</td>
<td>17%</td>
</tr>
</tbody>
</table>

**Board composition and decision making**

Code provision A.2.1 requires that the role of the chairman and chief executive should be clearly defined. The chairman has responsibility for leadership of the board and the chief executive is responsible for the day-to-day running of the business. The expectation is that the majority of the FTSE 350 companies would have separate people taking up these positions. There has been an increase in the number of companies where the roles of the chief executive and the chairman were performed by the same person between 2009 and 2010. In 2009 there were 9% of companies and this has risen to 13% in 2010. This comprised two (2009: one) companies in the top 350 companies, three (2009: two) in the middle group and eight (2009: six) within the smallest 350 companies. Only eight (2009: six) of these 13 companies provided reasons why this was the case. Two examples follow.
Nomination committee

94% of the companies which had prepared a corporate governance statement had a nomination committee. The other 6% of companies without a nomination committee comprised one company from the middle group and five companies from the smallest 350 companies. Of those companies which had a nomination committee 99% described the work of that committee in accordance with provision A.4.6 of the Code. In a slight increase from last year, 74% (2009: 70%) of those companies with a nomination committee included the terms of the nomination committee by reference to the company’s website.

Performance evaluation

The Code requires a statement of how performance evaluation was conducted for the board, its committees and individual directors. 92% of companies made such a statement, a significant increase on 2009 where just over two thirds of companies described how the performance evaluation process was conducted. This increase probably reflects the increasing value placed on the evaluation process. Extracts from companies commenting on the outcome of the evaluation process included:

“Overall, our process confirms that the blend of behaviours and skills around the Halma Board table are well suited to the task and consistent with Group values. With a Board that is free to openly express concerns comes more considered outcomes emphasising collective responsibility, transparency, clarity and sustainable conduct.”

Halma p.l.c Annual Report & Accounts 2010

“A report was prepared on the findings of these interviews and it also contained a number of recommendations designed to ensure that the current high standards of governance and processes were maintained. The report has been considered by the board and the board approved its recommendations. The report concluded that the board and its committees continue to work effectively.”

Johnson Matthey Annual Report & Accounts 2010

Redrow plc Annual Report & Accounts 2010

Tomkins Annual Report 2009

As described in section 2, the new UK Corporate Governance Code (applicable for periods commencing on or after 29 June 2010) requires that the performance evaluation process of the FTSE 350 companies be externally facilitated at least once every three years. With that in mind, the companies in this year’s sample have been surveyed to determine how many are already using external facilitators. 26% of the top 350 companies are already using an external facilitator and, unsurprisingly, none of the companies outside the FTSE 350 made reference to the use of an external facilitator.
Risk committees

In last year’s survey, further to recommendations in the Walker Review on the governance of financial institutions, the survey companies were reviewed to see if they had a separate risk committee. In 2009, seven of the top 350 companies surveyed disclosed that they had a separate risk committee and some also provided details of the availability of the terms of reference, the names of the members of the committee and the number of meetings. The seven companies with a separate risk committee included two banks with the other five companies being non-financial companies. In 2010, there were nine companies in the top 350 companies which had a separate risk committee and three of these were banks. Interestingly, one of the middle group of companies had a separate risk committee and two of the smallest 350 companies. All three companies were non-financial companies.

Looking ahead

As described in section 2, the new UK Corporate Governance Code was launched in May 2010. In addition to the new requirement on performance evaluation discussed above, there are a number of other new requirements which have been examined to determine levels of existing practice.

The first of these relates to the diversity of the board. The supporting principle B.2 states that:

“The search for board candidates should be conducted, and appointments made, on merit, against objective criteria and with due regard for the benefits of diversity on the board, including gender.”

The companies have been reviewed to determine the gender composition of the board. Figure 25 above shows the percentage of companies with female executive and non-executive directors. In the top 350 companies, two companies have greater than one female executive director and five companies have greater than one female non-executive director.

In addition to this new requirement in the Code, there is the Equality Act 2010. The Act provides a new cross-cutting legislative framework to protect the rights of individuals and advance equality of opportunity for all. A number of provisions come into force with effect from 1 October 2010 and there are some provisions the Government is still considering how best to implement. One of these strands for further consideration relates to the publication of gender pay gap information. As noted in section 6, the companies were surveyed to determine if any companies were already providing any information on gender pay gap, but no reference to this could be found in any of the companies surveyed.

One of the most controversial provisions in the new Code relates to the annual re-election of directors. Provision B.7.1 states:

“All directors of FTSE 350 companies should be subject to annual election by shareholders.”
The re-election policies of the FTSE 350 companies in the survey were examined. Only 6% of the top 350 companies already undertake annual re-election of all directors. Another 6% undertake annual re-election of some combination of the chairman, the deputy chairman and/or all committee chairmen. An example of annual re-election is as follows:

Barclays has announced that, going forward, the group chairman, deputy chairman and chairman of each principal board committee will stand for re-election on an annual basis.

One company outside of the FTSE 350 was found to have annual re-election of all directors.

A key new disclosure recommendation in the UK Corporate Governance Code is included in the preface to the Code. The preface states that:

“Chairmen are encouraged to report personally in their annual statements how the principles relating to the role and effectiveness of the board (in Sections A and B of the new Code) have been applied.”

The companies in the survey were reviewed to determine if any chairman’s statement included reference to how the Code had been applied. 12% of the chairmen of the top 350 companies included a statement on application of the Code in their annual statements. Sir John Parker of National Grid plc provided a statement on governance in his chairman’s statement in the 2009/10 annual report:

Pearson plc Annual Report and Accounts 2009

Barclays plc Annual Report 2009

National Grid plc Annual Report and Accounts 2009-2010
Another approach which was noted was for the Chairman to make a statement as part of the company’s corporate governance statement. An example of this was in the Halma annual report for 2009.

Discussion of the other new disclosure requirement from the UK Corporate Governance Code regarding the business model can be found in section 12.
The Code requires a separate section of the annual report to describe the work of the audit committee in discharging its responsibilities (provision C.3.3). In 2010 one company (2009: three) failed to describe the work of the audit committee. This company was from the middle tier. While the Code refers to a ‘separate section’ of the annual report, a subsection within a larger corporate governance statement is generally considered acceptable and this is how the vast majority of companies (87% (2009: 85%)) presented information on their audit committees. DTR 7.2 requires companies to provide disclosure about the audit committee for periods beginning on or after 29 June 2008. This explains the high percentage of companies providing this information within their annual reports.

The Code also requires that the terms of reference of the audit committee, including its role and the authority delegated to it by the board, should be made available. Companies can meet this requirement by including the information in the annual report or by making the information available on request or placing it on the company’s website. 83% of companies with an audit committee referred the reader to the company website or stated that the terms of reference are available on request.

The Guidance on audit committees recommends that the section describing the work of the audit committee should include the following:

- a summary of the role of the audit committee;
- the names and qualifications of the members of the audit committee during the period;
- the number of audit committee meetings; and
- a report on the way in which the audit committee has discharged its responsibilities.

99% (2009: 98%) of the companies which included an audit committee section in their annual report provided information on the role of the audit committee and all except four companies from the smallest 350 group indicated the number of meetings held during the period.

The following activities could be included in the report on the way in which an audit committee discharges its responsibilities:

- the activities carried out to monitor the integrity of the financial statements;
- the activities carried out to monitor the integrity of the internal financial controls and risk management systems;
- the procedures adopted to review the independence of the external auditors, including disclosure of the policy on the provision of non-audit services and an explanation of how the policy protects auditor independence;
• oversight of the external audit process and confirmation that an assessment of the effectiveness of the external audit has been made; and

• review of the plans and work of the internal audit department.

Although the detailed guidance above is not mandatory, it is an indication of best practice. Figure 27 indicates whether the companies included in the survey provided this information within their audit committee report.

The results were mixed. To achieve a positive result for each category in this section a company had to describe the activities undertaken to fulfil their responsibilities. It was not sufficient simply to repeat the responsibilities, the emphasis being on the ‘how’ as opposed to the ‘what’. Perhaps not surprisingly companies in the top 350 companies provided the most information and those in the smallest 350 companies disclosed the least. Probably as a direct result of the increasing focus on the external audit relationship, the majority of companies provided some information about auditor independence, non-audit services and the effectiveness of the external auditors. By contrast, less than half of companies disclosed the actual activities undertaken to monitor the integrity of the financial statements, the internal financial controls and risk management systems or whether the work of internal audit had been reviewed.

An example of reporting on the activities undertaken by the audit committee during the year is included in the Ladbrokes plc Annual Report and Accounts 2009.

In compliance with the Code (provision C.3.5), 36% (2009: 37%) of companies in the survey stated explicitly that they did not have an internal audit function together with an explanation of why this was the case. The external auditors provided non-audit services in 95% (2009: 95%) of companies surveyed. Where this is the case, provision C.3.7 of the Code requires an explanation of how auditor objectivity and independence are safeguarded. 87% (2009: 85%) of companies for whom it was applicable gave a more detailed explanation of how auditor independence was protected in these circumstances.

The main activities of the committee in 2009 were as follows:

- providing the assistance of reports received from management and the external auditor, the critical review of the significant financial reporting issues in connection with the preparation of the Company’s financial and related financial statements;
- assessing the scope and effectiveness of the systems established to identify, assess, monitor and report on financial and non-financial risks; and
- monitoring the integrity of the Company’s internal financial controls.

The committee does so by reference to:

(a) summaries of business risks and mitigating controls;

(b) regular reports and presentations from the head of key risk functions, internal audit and external audit; and

(c) the results of the system of annual self-certification of compliance with key controls and procedures;

- monitoring and reviewing the plans, work and effectiveness of the internal audit function, including any actions taken following any significant failures in internal controls;

- reviewing, with the external auditor, its terms of engagement, the findings of its work, and at the end of the audit process, reviewing its effectiveness; and

- reviewing the independence and objectivity of the external auditor.
The auditor selection decision

As noted in section 2, the Guidance on audit committees issued in October 2008 includes a recommendation that the audit committee should explain to shareholders in the audit committee report how it reached its recommendation to the board on the appointment, re-appointment or removal of the external auditors. 27% of all companies had attempted to explain their auditor selection decision, including 41% of the top 350 companies.

The revised guidance also recommends that the audit committee should consider disclosing any contractual obligations that acted to restrict the audit committee’s choice of external auditor. 14 companies in the sample made reference to any contractual obligations and that was to confirm that there was none. Information on tendering frequency and the tenure of the incumbent auditor are further recommendations for disclosure by the audit committee for periods commencing on or after 28 June 2008. 12% (2009: 3%) of the companies reviewed had provided details of tendering frequency and 20% (2009: 5%) on the tenure of the incumbent auditor. Fidessa group plc included disclosures on these areas in its annual report:

Board chairmen and the audit committee

The 2008 Code (Provision C.3.1) allows the chairman of a smaller listed company (outside the FTSE 350) to be a member of the audit committee where he or she was considered independent on appointment. When this provision was surveyed in 2009, prior to the implementation period of the 2008 Code, it was noted that this practice was already relatively common. As expected, the number of incidences of the chairman being a member of the audit committee has increased for those companies outside the FTSE 350 in 2010, now 33% (2009: 21%) of the middle group of companies and in 55% (2009: 42%) of the smallest 350 companies. In addition two of the top 350 companies have the chairman as a member of their audit committee. These companies include the following explanation.

Fidessa group plc Annual Report and Accounts 2009

Heritage Oil plc Annual Report & Accounts 2009

The BSS Group plc Annual Report & Accounts 2010
11. Corporate governance – Going concern*

As stated in section 2, the Listing Rules and the Code require a statement by the directors that the business is a going concern, together with supporting assumptions or qualification as necessary. This disclosure should be prepared in accordance with the “Going Concern and Liquidity Risk: Guidance for Directors of UK Companies 2009” (the Guidance) published by the FRC in October 2009. This Guidance is effective for accounting periods ending on or after 31 December 2009.

Location of statement
The 2009 guidance states that addressing the disclosure requirements in relation to going concern included in the FRSSE, UK GAAP, IFRS, CA 2006 and the Listing Rules that apply to a company may lead it to address going concern and liquidity risk in different sections of its annual report and financial statements. It is noted that this may create difficulties for investors and other stakeholders in seeking to obtain a clear, comprehensive and cohesive understanding of the issues facing the company.

The Guidance suggests that it would be helpful to investors and other stakeholders if all of the disclosures were brought together in a single place in the company’s financial statements. It may be necessary to provide a cross reference to that single place from other parts of the annual report. If it is not practicable to provide all of the information in a single place, it is still helpful if the key disclosures are brought together by way of a note that includes appropriate cross references to information in the financial statements and from the financial statements to information included elsewhere in the annual report.

All companies included a statement on going concern. Figure 28 shows where the statement was positioned. 50% (2009: 40%) of companies included the statement within the directors’ report, this being the most common place for the top and middle sized groups with 44% (2009: 35%) and 64% (2009: 45%) of them doing so respectively. For 34% (2009: 39%) the statement was situated within the corporate governance statement, this being the most popular for the smallest 350 companies with 45% (2009: 52%).

11% (2009: 15%) of companies placed the going concern statement within the stand alone business review which was referenced from the directors’ report. 5% of companies positioned the statement elsewhere. Of these, three companies included the going concern statement in the OFR or financial review and one positioned the statement in the statement of directors’ responsibilities. The remaining company included the going concern statement in the Chairman’s statement because there was a material uncertainty that cast significant doubt about the company’s ability to continue as a going concern.

* This section analyses the findings for all companies other than investment trusts

---

- 63% of companies clearly adopt the recent FRC guidance.
- The average length of the going concern statement is 156 words.
- Five auditors’ reports contain an emphasis of matter, of which four relate to going concern. In 2009 there were nine auditors’ reports with an emphasis of matter of which seven related to going concern.

---

As stated in section 2, the Listing Rules and the Code require a statement by the directors that the business is a going concern, together with supporting assumptions or qualification as necessary. This disclosure should be prepared in accordance with the “Going Concern and Liquidity Risk: Guidance for Directors of UK Companies 2009” (the Guidance) published by the FRC in October 2009. This Guidance is effective for accounting periods ending on or after 31 December 2009.

Location of statement
The 2009 guidance states that addressing the disclosure requirements in relation to going concern included in the FRSSE, UK GAAP, IFRS, CA 2006 and the Listing Rules that apply to a company may lead it to address going concern and liquidity risk in different sections of its annual report and financial statements. It is noted that this may create difficulties for investors and other stakeholders in seeking to obtain a clear, comprehensive and cohesive understanding of the issues facing the company.

The Guidance suggests that it would be helpful to investors and other stakeholders if all of the disclosures were brought together in a single place in the company’s financial statements. It may be necessary to provide a cross reference to that single place from other parts of the annual report. If it is not practicable to provide all of the information in a single place, it is still helpful if the key disclosures are brought together by way of a note that includes appropriate cross references to information in the financial statements and from the financial statements to information included elsewhere in the annual report.

All companies included a statement on going concern. Figure 28 shows where the statement was positioned. 50% (2009: 40%) of companies included the statement within the directors’ report, this being the most common place for the top and middle sized groups with 44% (2009: 35%) and 64% (2009: 45%) of them doing so respectively. For 34% (2009: 39%) the statement was situated within the corporate governance statement, this being the most popular for the smallest 350 companies with 45% (2009: 52%).

11% (2009: 15%) of companies placed the going concern statement within the stand alone business review which was referenced from the directors’ report. 5% of companies positioned the statement elsewhere. Of these, three companies included the going concern statement in the OFR or financial review and one positioned the statement in the statement of directors’ responsibilities. The remaining company included the going concern statement in the Chairman’s statement because there was a material uncertainty that cast significant doubt about the company’s ability to continue as a going concern.

* This section analyses the findings for all companies other than investment trusts
Adoption of the FRC guidance

63% (2009: 55%) of companies clearly adopted the Guidance (N.B. the Guidance had not been published at the time of the 2009 survey and so the comparative refers to the number of companies attempting to adopt the earlier FRC Update on going concern). Of the 37% which did not clearly adopt the Guidance, 17% were in the smallest 350 companies, 11% in the middle group and 9% in the top 350.

Cross-referencing

59% (2009: 57%) of companies either cross-referred to related discussion such as principal risks and uncertainties, liquidity and key judgements, or included or repeated relevant sections of narrative, such as liquidity, within the going concern statement. Of these, 25% (2009: 22%) were in the top 350 companies, 22% (2009: 26%) in the middle group and 12% (2009: 9%) in the smallest 350.

Cross-referencing is deemed to be a positive attribute of the going concern statement as it brings together all related information into one clear location, enabling the user of the report to have a full understanding of issues affecting the going concern assessment.

Identifying uncertainties

49 (2009: 31) companies referred to an uncertainty within their going concern statement. Of these, 17 (2009: 8) were from the top 350 companies, 19 (2009: 15) from the middle group and the remaining 13 (2009: 8) from the smallest 350 companies. In the current economic climate and given the increasing familiarity with the Guidance it is not surprising that there has been such a significant increase in the number of companies identifying uncertainties. Figure 29, above, illustrates to what the uncertainties discussed related. Results by category of uncertainty are presented as a percentage of all companies identifying uncertainty, with some companies listing more than one uncertainty.

There is a significant increase in the number of companies referring to uncertainties about financing and shareholder support (up from 42% in 2009 to 73% in 2010) in those 49 companies. This is not surprising given the current economic climate. Uncertainties about trading volumes have increased from 19% in 2009 to 35% in 2010. This is likely to reflect the stuttering recovery the UK economy is experiencing.

None of the largest companies considered there to be any uncertainty over a breach or potential breach of covenants. In stark comparison, 21% of the middle group and 23% of the smallest companies identified this.
88% of those companies reporting uncertainties included reference to an uncertainty other than those categories discussed above. For many companies this related to a cross-reference to the risk disclosures elsewhere in the annual report. Other companies included comment on the following types of uncertainty:

- currency risks;
- uncertain economic outlook;
- regulatory uncertainties;
- volatility in prices of raw materials; and
- working capital.

**Length of forecasts**

Standard UK practice, as confirmed under FRS 18 and auditing standards, is to prepare budgets and forecasts to cover a period of twelve months from the date of approval as a minimum. Medium or long term plans are also considered as they give an indication in general terms of how the directors expect the company to fare. The Guidance states that directors should prepare budgets or forecasts covering the period up to twelve months from the date of approval or for a longer period.

87% (2009: 80%) of all companies did not disclose the length of forecasts or budgets relied upon to support the going concern assumption.

Of the 13% of companies who disclosed the length of forecasts, three confirmed that they were longer than twelve months from the date of approval. A further six confirmed that forecasts covered the twelve month period from the date of approval. Four companies indicated that forecasts covered only twelve months from the balance sheet date.

**Length of statement**

Across all companies, the average length of the main statement on going concern was 156 words (2009: 164 words). The longest statement was 562 (2009: 716) words and the shortest only 30 (2009: 30).

The additional information, recommended by the Guidance, allows users of the annual report to have a more rounded understanding of the company’s position and its ability to continue in the near future. In a climate of significant uncertainty, clear disclosure and discussion around the directors’ assumption that the company is a going concern is undoubtedly of utmost importance.

A good example of companies which clearly adopted the spirit of the recent Guidance, providing appropriate information in a clear and concise manner, is Rexam.
Going concern
The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Business Review on pages 6 to 29. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are also detailed in the Business Review on pages 14 to 19. In addition, notes 22, 23 and 24 to the consolidated financial statements include the Group's objectives and policies for managing its capital, its financial risk management objectives, details of its financial instruments and hedging activities, and its exposures to credit risk and liquidity risk.

The Group has considerable financial resources, as detailed on pages 14 to 19 of the Business Review, together with established agreements with a number of customers and suppliers across different geographic areas and markets. During 2009, the Group accessed the equity markets to raise £334m (net of costs) through the rights issue and the bank debt market to both increase its committed bank facilities and also refinance a substantial portion of its 2010 maturities. As a consequence, the directors believe that the Group is well placed to manage its business despite the current economic environment which increases risks and uncertainties.

The directors, having made appropriate enquiries, are satisfied that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the consolidated and Company financial statements.

Consistent reporting
The going concern statements were considered for consistency with disclosure in the financial statements, the auditors' report and the narrative reporting as a whole. All going concern statements were consistent with any specific disclosures in the financial statements, the auditors' report and narrative reporting.

Similarly, Triad Group plc provides a good example of adopting the Guidance and highlighting key uncertainties facing the company in the current climate.

Going Concern
The Group's business activities, together with the factors likely to affect its future development, performance and position, are set out in the Chairman's statement, and Operating review on pages 2 to 4. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Chairman's statement on page 2 and in note 18 to the financial statements. In addition note 3 to the financial statements includes the Group's objectives, policies and processes for managing its capital, its financial risk management objectives, details of its financial instruments and hedging activities, and its exposure to credit risk and liquidity risk.

As highlighted in note 18 to the financial statements, the Group meets its day to day working capital requirements through an invoice finance facility. The current economic conditions create uncertainty particularly over (a) the level of demand for the Group's services and (b) the availability of bank finance in the foreseeable future.

The Group's projections, taking account of reasonably possible changes in trading performance, show that the Group should be able to operate within the level of its current facility. The facility may be terminated by either party with one month's written notice. The board receives regular cash flow and working capital projections to enable it to monitor its available headroom under this facility. These projections indicate that the Group expects to have sufficient resources to meet its reasonably expected obligations. The bank has not drawn to the attention of the Group any matters to suggest that this facility will not be continued on acceptable terms.

After making enquiries, the directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and accounts.

Triad Group plc Annual Report and Accounts 2010

Auditors' reports
Five companies had an emphasis of matter paragraph. This is a decrease on last year where nine companies had an emphasis of matter paragraph. For four of the companies, these paragraphs related specifically to the group's ability to continue as a going concern. The other emphasis of matter related to regulatory uncertainty.

One of the five companies had both an emphasis of matter paragraph and a qualified audit opinion due to limitation of scope. This is the same position as last year and relates to the same company.
12. OFR-style information*

13% of companies surveyed included a statement entitled ‘Operating and Financial Review’ (OFR), which is in line with the results seen last year (2009: 13%). All except one of the companies identifying an OFR had also identified a business review. Of those companies identifying both a business review and an OFR, 92% included the OFR within their business review. The remaining 8% of companies did not include the OFR within the business review; instead, the OFR was a stand-alone statement within the narrative reporting.

The preparation of an OFR is voluntary but, for those companies choosing to do so, it is considered best practice to follow the guidance in the ASB’s Reporting Statement (RS). Of the 13 companies choosing to present an OFR in 2010, five (2009: four) made a statement regarding their compliance with the RS, with four companies (2009: three) stating full compliance with the RS guidance and one (2009: one) reporting some exceptions.

Given that there is a definite overlap between the RS and the requirements of the business review, there is a possibility that the presence of two separate sources of rules and guidance may be over complicating the narrative reporting requirements. This is supported by the relatively low proportion of companies choosing to identify formally a separate OFR statement in their annual reports.

Even though the guidance in the RS regarding the content of the OFR is voluntary (for example, a description of the objectives, strategy and a description of the nature of the business), such descriptions would be expected in an annual report as they enhance a reader’s understanding of the business and set the context for the financial statements.

Mandatory requirements, such as KPIs and principal risks and uncertainties, have already been discussed in sections 6 to 8. The remainder of this chapter analyses whether companies have also included additional OFR-style information (regardless of whether they have labelled it as such) in their annual reports and whether this information meets the recommendations of the RS.

**OFR-style information**

There are two distinct elements to OFR-style information; the first part being discussion of the business divisions, objectives and strategy and the second part being a review of the financial information.

The RS states that the OFR should include a description of the business and the external environment in which it operates to set the context for the directors’ discussion and analysis of the performance of the business. Figure 31 shows the extent to which companies described various aspects of their business.

Companies were assessed in the following areas.

- Main industries – a description of the industries in which the company operates.

- Main products – including a description of the main products, services, customers, business processes and distribution methods.

- Markets – a description of the major markets in which the company operates, and a comment on the company’s competitive position.

* This section analyses the findings for all companies other than investment trusts.
• Business structure – a description of the structure of the business, its operating divisions and location.

• Legal/regulatory – a description of the legal or regulatory environment in which the company operates, even if referred to only in the principal risks and uncertainties discussion.

• Key dependencies – a reference to key relationships with customers, suppliers, financiers, regulators or key employees.

• Business model – the basis on which the company generates or preserves value over the longer term.

As can be seen from Figure 31, the extent to which the companies’ business was described was generally good, with particularly meaningful discussions provided by the companies in the top 350 sample. Overall, the quality and the extent of the descriptions have improved since last year, with 94% of companies providing a description of the main industries in which their companies operate, compared with 89% in 2009; 95% of companies describing the main products or services provided by the business, compared with 91% in 2009; and 88% of companies describing the markets in which they operate, compared with 74% in 2009.

Perhaps most encouragingly, the proportion of companies disclosing key dependencies and relationships has increased from 34% in 2009 to 67% in 2010. This information is particularly pertinent in the uncertain economic climate and is particularly useful to the users of the annual report. This result is also significantly greater than the proportion of companies who disclosed whether there were any contractual arrangements which were essential to the business which is a requirement under the CA06 (see section 6). Only 24% (2009: 24%) of companies made any reference to contractual relationships essential to the business, either to describe what they were, or to confirm there were none.

As might be expected, the companies within the top 350 sample provided more information, on average, than the smaller companies, with the companies from the smallest 350 sample consistently providing the least information on average. This disparity between the largest and smallest companies was particularly evident when analysing the disclosures regarding the business model, the legal and regulatory environment and the business structure. 94% of the top 350 sample included a description of the legal and regulatory environment, compared to 67% of the middle companies and just 48% of the smallest 350 companies. Similarly, 94% of the top 350 companies described the structure of their businesses, compared to 82% of the middle companies and only 48% of the smallest 350 companies.

Descriptions of the business model

Despite generally good disclosures in the areas discussed above, the number of companies attempting to disclose their business model was low, by comparison. Overall, only 21% of companies made an attempt to describe their business model. 44% of the top 350 companies sampled referred to their business model, but only 15% of the middle group did so, and 3% of the smallest 350 companies included any reference or description.

A description of the business model was deemed, for the purposes of this analysis, to be more than just a simple discussion of what the company does. A reference to the specific way in which the company generates value or an explicit reference to “business model”, together with a description of what the directors deem that model to be, was required to satisfy this requirement for the purposes of this survey.
An understanding of the company’s business model assists the users of the annual report in formulating opinions about the company or its financial statements. It would therefore be useful if more companies chose to disclose this information in the future, even though it is technically a voluntary disclosure at present.

As described in section 2, for periods commencing on or after 29 June 2010, provision C.1.2 of the new UK Corporate Governance Code states that there should be an explanation of the basis on which the company generates or preserves value over the longer term (the business model) and the strategy for delivery of the objectives of the company.

The BSS Group plc and Intermediate Capital Group plc provide examples of how disclosure of the business model is being approached.

**Method of disclosure**

The way in which companies disclosed the operational information about their businesses varied greatly. Some companies chose to present the information in a graphical or tabular format, while others chose to present the information in narrative. A relatively common approach, which worked well, was to present a separate review of operations for each division of the business. This approach enabled an overall description of each division to be presented clearly as well as facilitating discussion of both financial and non-financial performance of each division (including, in some cases, the identification of division-specific objectives, KPIs and risks). The extract (overleaf) taken from the annual report of Mondi plc is a good example of the disclosure of divisional summaries.
Objectives and strategy

The RS contains a recommendation that the OFR includes a discussion of the objectives of the business, including both financial and non-financial objectives, where appropriate.

Performance improved in this area, in comparison with 2009: 84% of companies included a discussion of the objectives of the business in comparison with 79% of companies doing so last year. Only 3% of the top 350 companies sampled did not include such a discussion, as did 12% of the middle companies and a third of the smallest 350 companies.

Figure 32 shows the balance of discussion between financial and non-financial objectives and the attempts made by directors to describe the strategies employed to meet these objectives.

Figure 32. What is the balance between financial and non-financial objectives and to what extent do links to strategies exist?

Mondi plc Annual report and accounts 2009
There was a good balance between financial and non-financial objectives, with a slight bias towards the disclosure of non-financial objectives, such as objectives relating to market position or corporate responsibility. 82% of companies sampled included a description of non-financial objectives, compared with 64% of companies providing a discussion of financial objectives.

A large proportion of companies have included a description of the strategies adopted to pursue these financial and non-financial goals. However, the nature and extent of these descriptions varied. Only 45% of companies were considered to have provided a clear and meaningful description. More consistency and clarity in the description of the strategies adopted by companies to pursue their objectives would assist the users of the accounts in formulating a sound understanding of the business. A good example of this is National Grid plc.

Other non-financial information

The RS also encourages discussion of other non-financial information, such as a description of the resources available to the entity and how they are managed. 28% of companies discussed the management structure of the business (2009: 24%), thereby providing helpful information on reporting lines and business divisions. All of the companies sampled provided a discussion of receipts from and returns to members (2009: 92%). This is unsurprising given the importance users place on dividend policies and the need for many companies to revise these policies in the current economic climate.

7% of companies made an explicit reference to off-balance sheet arrangements (either to confirm that there were none, or to describe any such arrangements in place). An example of this is Tomkins.

Financial information

The OFR should contain a description of the development and performance of the business in the financial year, as recommended by the RS, and covered by the business review requirement under the CA06. The OFR should contain an analysis of the financial position of the entity. The table below summarises the recommended content of this analysis and the percentage of companies including the items listed.

<table>
<thead>
<tr>
<th>Category</th>
<th>2010</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial position</td>
<td>95%</td>
<td>99%</td>
</tr>
<tr>
<td>Capital structure &amp; financing</td>
<td>73%</td>
<td>83%</td>
</tr>
<tr>
<td>Treasury policies</td>
<td>63%</td>
<td>69%</td>
</tr>
<tr>
<td>Cash flows</td>
<td>83%</td>
<td>84%</td>
</tr>
</tbody>
</table>

Tomkins Annual Report 2009
Forward-looking information

The RS states that OFRs should have a “forward-looking orientation”. 98% of companies included some discussion about the future (a slight improvement on last year, where this was discussed by 95% of companies surveyed), although only 40% of companies (2009: 40%) included a disclaimer about the forward-looking information included within the annual report. Two examples are presented below: one of a blanket disclaimer covering the entire annual report (Cobham) and one of a disclaimer specifically for the business review (Halma).

None of the companies surveyed this year included any references to past predictive comments that had not been borne out by subsequent events, as recommended by the RS. However, it is not clear if this is because they have chosen not to adopt the recommendation or if there have been no past predictive comments that have proven incorrect. It is likely that a higher degree of caution was exercised in the disclosures in 2009 given the uncertainty about the economic climate, meaning that very few predictions were made which would require retraction in the current year.

Investment for the future

Finally, the RS recommends that companies explain how they have invested in the future performance of the business. 63% of companies provided a discussion about investment in areas such as capital expenditure, research & development and new products. However, only 25% of companies provided a discussion about planned future investment in these areas. The majority of the companies surveyed confined their discussions to investment that had been made in these areas during the financial year. This could also be a reflection of uncertainty for the future, given the current economic climate.

All of the companies who included some discussion about the future also specifically commented on the trends and factors that were expected to affect the future development, performance or financial position of the business. This is a recommendation of the RS, but it is also a requirement of the CA06 that listed companies disclose such information in their business review (see section 6).
The sample of 30 investment trusts has been considered separately for the purposes of this survey and is analysed in this section. Investment trusts are those companies which have been classified by the London Stock Exchange as “non-equity investment instruments” or “equity investment instruments”. Real estate investment trusts have not been included in this category.

The investment trust sample has been divided into three categories by market capitalisation, as with the other corporate companies sampled. One third of the sample (i.e. ten companies) have been taken from the top 350 companies by market capitalisation at 30 June 2010, one third have been taken from the smallest 350 by market capitalisation, and one third have been taken from those that fall in between those categories (the middle group).

The average length of the annual reports has decreased this year. Last year the mean average length of investment trust annual reports was 52 pages, whereas this year the average length was 50 pages (a decrease of 5%). The decrease in report length has been seen across all three size categories, with the largest decrease seen amongst the largest trusts. As expected, the trusts from the top 350 are still producing the longest reports, while the smallest trusts are producing the shortest ones. The average report length by size category this year was 57 pages for the largest trusts (2009: 60), 49 pages for the middle group (2009: 51) and 44 pages for the smallest trusts (2009: 46).

It should be noted that the median data show a similar trend, as the investment trust report lengths appear to be more ‘normally’ distributed than the corporate sample (see section 4).

The ratio between narrative reporting and the financial statements has also decreased this year. Last year 63% of the average annual report was made up of narrative reporting. However this year this has fallen to 61%. This decrease has been observed in all three size categories, and has been particularly noticeable for the middle and smallest trusts. The narrative in largest trusts’ annual reports constituted 63% of the annual report (2009: 64%), the middle group’s annual reports were comprised of 60% narrative, on average (2009: 65%) and the smallest companies’ annual reports were comprised of 61% narrative (2009: 64%).

The ratio between narrative reporting and the financial statements has also decreased this year.
It was noted last year that investment trusts were getting slower, on average, at approving their annual reports. This trend has continued this year. The average annual report took 81 days to be approved, in comparison with 76 days in 2009 and 73 days in 2008. Trusts from the top 350 were quickest, although this category showed the largest (19%) increase in delay in reporting, taking 70 days on average, compared with 58 days in 2009. The middle group took 78 days, on average, to approve their annual reports compared with 73 days in 2009, while the smallest group actually showed a slight improvement by taking an average of 96 days compared with 97 days in 2009. It was not possible to discern from the annual reports any obvious reason for the trusts taking longer to report. It may be linked to the reports getting shorter. To paraphrase Blaise Pascal, it takes longer to write a short letter than a long letter.

Reporting framework
70% of the trusts surveyed were stand-alone companies and therefore not required to adopt IFRSs. 86% of these stand-alone companies continued to report under UK GAAP, which is in line with the proportion doing so in the previous year (2009: 86%). The remaining 14% had chosen to adopt IFRS for both the consolidated financial statements and the parent-only financial statements.

Investment managers
All of the reports surveyed identified their investment managers and made reference to their appointment. Only one trust, from the smallest 350 sample, did not provide an investment manager’s report in their annual report. The same trust failed to provide an investment manager’s report in 2009 and 2008 also.
Summary information
29 trusts (97%) included summary information (including financial highlights and/or key events during the year) at the start of their annual reports, in line with last year (2009: 29 trusts). This summary information was largely financial in nature, with only two companies (2009: 3) including narrative in their summaries. 28 annual reports also included a trust summary (a general statement about the trust, such as its investment objectives/ methods, information about the investment manager or information about its status as an investment trust) within the first few pages of the annual report, an increase on 27 reports in the prior year.

Of the trusts who included summary information, 93% included KPIs (as defined elsewhere in the narrative) within their summary pages, representing a slight decrease on 97% in 2009.

Gartmore Global Trust Plc provides a good example of a summary information page. It included information on its investment objectives, investment policy, performance, investment and structural highlights, including KPIs.
Key performance indicators
The proportion of trusts surveyed who identified KPIs within the front half of their annual reports have increased this year, from 93% to 97%. Of those who did not identify KPIs in both 2009 and 2010, all of these trusts were registered in Guernsey and were therefore not subject to UK company law.

The average number of KPIs has remained at four, in line with that noted in 2009. This figure includes both financial and non-financial KPIs but the vast majority of KPIs presented were financial.

As can be seen from the graph below, the categories of KPIs identified have remained roughly in line with the prior year. The notable movements are decreases in the number of trusts identifying dividends/earnings per share and comparisons against peer performance within their KPIs (down from 50% to 28%, and 39% to 28%, respectively). Net asset value remains the most popular KPI, being cited by 93% of those trusts identifying KPIs (2009: 89%).

Principal risks and uncertainties
Only one trust did not identify principal risks and uncertainties in the current year sample (2009: two). This trust was registered in Guernsey and so is not subject to UK company law (as was the case with the two companies identified in the prior year).

The average number of risks identified has increased this year, with the trusts identifying seven risks, on average (2009: five). The number of trusts identifying both financial and strategic risks has also increased from 82% to 90% in the last year. However, the proportion of trusts identifying strategies that have been put in place to mitigate these risks has decreased slightly from 100% in 2009, to 97% in 2010.

The profile of risk categories discussed by the investment trusts surveyed remains roughly comparable with the prior year, as shown in figure 37 with market and liquidity risks remaining the most common risks identified year-on-year. Accounting, regulatory and legal risks are also common risks in both the current and prior year.

JPMorgan Indian Investment Trust plc provides a good example of principal risks and uncertainties. It includes a description of strategic, commercial, operational and financial risks with the directors’ policy for managing those risks.
As noted in last year’s survey, the corporate governance disclosures provided by the trusts in the sample varied greatly in quality and quantity. Some companies provided relatively little information beyond the statutory minimum. However this is largely because of the nature of their business as an investment trust. Many of the trusts did not have any employees or any executive directors and delegated much of the responsibility of the Board to the investment manager. As a result, many of the ‘usual’ corporate governance disclosures were not applicable. On the other hand, some trusts did provide insightful, meaningful disclosures that were clearly specific to their business, rather than just generic comments.

**Corporate governance**

There are other important areas of governance which are specific to investment companies. For example, how does the Board manage its relationship with the investment manager? These aspects are not covered by the Combined Code, but are likely to be of interest to investors and users of the annual report. For this reason, the Association of Investment Companies (AIC) has developed a complementary corporate governance code and related guide. The Financial Reporting Council (FRC) has confirmed that trusts who report against the AIC Code of Corporate Governance (AIC Code) and who follow the AIC’s Corporate Governance Guide for Investment Companies (AIC Guide) will be meeting their obligations in relation to the Combined Code and paragraph 9.8.6 of the Listing Rules.

Several companies disclosed that they had reviewed the AIC Code to ensure they had met their specific obligations as investment trusts.

**Compliance**

Most investment trusts tend to outsource their day-to-day management and operational functions and do not have employees. In fact, only one of the trusts sampled had any executive directors, as was the case in the 2009 sample. As a result, many of the provisions of the Combined Code, such as the balance of executives and non-executives within the Board, are not relevant for such trusts.
Only two trusts (2009: one trust) stated that they had fully complied with the Combined Code. Of those trusts who stated that they had not fully complied with the Combined Code, 71% had identified which provisions they had not complied with and had offered some explanation as to why they had not complied with these provisions, which is a great improvement on the 34% in 2009.

One company did not provide any statement on corporate governance.

**Directors and board committees**

As expected, all companies had a chairman but only one of the companies surveyed had a chief executive, which is consistent with the prior year. This is likely to be due to the fact that the investment managers usually fulfil this role within investment trusts.

29 trusts identified their independent non-executive directors (NEDs) by name (2009: 30). The company who did not identify any independent NEDs was unable to do so because it did not have any independent directors (the Board comprised just the chairman and two non-executive directors, none of whom were deemed to be independent as a result of other directorships of companies managed by the same investment manager team). This trust included a statement to explain this.

All of the trusts sampled disclosed the number of Board meetings held in the year and showed the attendance at these meetings by individual director (as was the case in the prior year). 29 of the trusts also showed the number of audit committee meetings held in the year (2009: 29). The trust that did not disclose this information was unable to do so because it did not have a separate audit committee and was therefore in breach of the Combined Code’s provisions regarding audit committees.

Trusts appeared to make better disclosures regarding succession planning and each committee’s terms of reference this year. 40% of trusts referred to director succession planning, compared to 20% in 2009. Of those trusts with separate board committees, 93% disclosed where the audit committee’s terms of reference could be found (most were either available on request or available from the trust’s website) compared to 86% in 2009. 82% of the trusts who discussed their nomination committee disclosed where the committee’s terms of reference could be found, compared with 77% in 2009.

On the other hand, disclosures about performance evaluation have decreased slightly this year. 23 trusts made reference to performance evaluation procedures performed in relation to the Board as a whole, which is in line with 2009. However, only 18 trusts described the committee performance evaluation process in 2010, compared with 22 in 2009. 21 trusts referred to the evaluation of individual director’s performance in 2010 compared with 23 in 2009.

All trusts surveyed, in both 2009 and 2010, included a discussion regarding internal controls within their Corporate Governance reports, and there were no instances of controls breakdowns being identified in either year. All trusts stated that it was the audit committee’s responsibility to review the effectiveness of these controls, 60% of whom explained how the effectiveness of these controls had been reviewed.

**Going concern**

Going concern disclosures have improved this year, with all companies making a statement regarding going concern in the narrative part of the annual report. One of these companies included a statement to say that the financial statements had been prepared on a basis other than the going concern basis (2009: nil). This company’s audit report included an emphasis of matter paragraph regarding the basis of preparation of the financial statements due to its announced intention to conduct an orderly realisation of its investment portfolio. This was the only emphasis of matter paragraph noted in both the 2010 and 2009 samples.
As shown in the figure below, most trusts chose to discuss the going concern basis within the directors’ report, with the remainder including this discussion in the corporate governance statement. This was also the case in the prior year. However the proportion of companies presenting this information in the directors’ report has increased from 67% to 83%.

As previously discussed, the FRC has highlighted the importance of clear disclosure regarding going concern and liquidity risk, given the difficult prevailing market conditions. Disclosures in this area have improved since 2009, with 27% of trusts making cross references to risks and uncertainties from their going concern discussion (2009: 7%). It is hoped that disclosures in this area will continue to improve going forward as use of the FRC guidance on going concern and liquidity risk increases.

... the corporate governance disclosures provided by the trusts in the sample varied greatly in quality and quantity. Some companies provided relatively little information beyond the statutory minimum.
Appendix 1 – The missing links

It is clear that some companies view the narrative reporting process as a compliance exercise – a series of boxes to be ticked with new pieces of legislation or guidance being bolted on. There are, however, examples of companies which achieve a cohesive flow throughout their narrative report. The chart below demonstrates the clear links that these companies achieve. The arch to the right of the chart represents the elements of the governance process that should be disclosed to complete the narrative ‘story’.

<table>
<thead>
<tr>
<th>Agreement</th>
<th>Setting</th>
<th>Implementation</th>
<th>Governance</th>
<th>Monitoring</th>
<th>Enforcement</th>
<th>Re-assessment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agreement</td>
<td>Setting</td>
<td>Implementation</td>
<td>Governance</td>
<td>Monitoring</td>
<td>Enforcement</td>
<td>Re-assessment</td>
</tr>
<tr>
<td>Agreement</td>
<td>Setting</td>
<td>Implementation</td>
<td>Governance</td>
<td>Monitoring</td>
<td>Enforcement</td>
<td>Re-assessment</td>
</tr>
<tr>
<td>Agreement</td>
<td>Setting</td>
<td>Implementation</td>
<td>Governance</td>
<td>Monitoring</td>
<td>Enforcement</td>
<td>Re-assessment</td>
</tr>
<tr>
<td>Agreement</td>
<td>Setting</td>
<td>Implementation</td>
<td>Governance</td>
<td>Monitoring</td>
<td>Enforcement</td>
<td>Re-assessment</td>
</tr>
</tbody>
</table>

It is clear that some companies view the narrative reporting process as a compliance exercise – a series of boxes to be ticked with new pieces of legislation or guidance being bolted on. There are, however, examples of companies which achieve a cohesive flow throughout their narrative report. The chart below demonstrates the clear links that these companies achieve. The arch to the right of the chart represents the elements of the governance process that should be disclosed to complete the narrative ‘story’.

<table>
<thead>
<tr>
<th>Objectives</th>
<th>Short-term and long-term</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business model</td>
<td>How will the company generate or preserve value over the longer term</td>
</tr>
<tr>
<td>Strategy</td>
<td>How are the objectives achieved? How is the business model delivered?</td>
</tr>
<tr>
<td>Key performance indicators</td>
<td>Principal risks and uncertainties</td>
</tr>
<tr>
<td>How will achievement of strategy and delivery of business model be measured?</td>
<td>What could prevent or restrict execution of this strategy?</td>
</tr>
<tr>
<td>This could include targets, comparison over time and to peers</td>
<td>This could include references to internal controls, CSR policies, essential contracts and remuneration policies</td>
</tr>
</tbody>
</table>
Appendix 2 – Glossary of terms and abbreviations

AIC Association of Investment Companies
The Association of Investment Companies is the trade organisation for the closed-ended investment company industry. Amongst other initiatives, it provides technical support and guidance to Members and their advisers in areas such as accounting, tax, company law and regulation.

ASB Accounting Standards Board
The role of the Accounting Standards Board is to issue UK accounting standards. The ASB also collaborates with accounting standard-setters from other countries and the International Accounting Standards Board (IASB) both to influence the development of international standards and to ensure that its standards are developed with due regard to international developments.

BIS The Department for Business, Innovation and Skills

BR Business Review
The Companies Act 2006 requires that directors’ reports include a Business Review.

Combined Code
The Combined Code on Corporate Governance sets out standards of good practice on issues such as board composition and development, remuneration, accountability and audit, and relations with shareholders. All companies with a premium listing of equity shares in the UK are required under the Listing Rules to report in their annual report on how they have applied the Combined Code. The Combined Code is updated at regular intervals. The 2006 edition applies to accounting periods beginning on or after 1 November 2006. The June 2008 edition applies to accounting periods beginning on or after 29 June 2008.

CSR Corporate social responsibility
Corporate social responsibility is about how businesses take account of their economic, social and environmental impact. The Companies Act 2006 requires that companies disclose information, about environmental matters, their employees, and social and community issues, in their annual report.

DTR Disclosure and Transparency Rules
These rules, which include requirements for periodic financial reporting, replace some of the Listing Rules and have been inserted into the Disclosure Rules sourcebook of the Financial Services Authority (FSA). The periodic financial reporting rules of DTR 4.1 apply to companies with shares and/or debt admitted to trading on a regulated market. The corporate governance requirements of DTR 7 apply to the same companies.

EU European Union

EU Takeovers Directive
The main objectives of the Directive are to provide a framework of common laws for takeovers in the EU. It has been implemented in the UK via the Companies Act 2006. It requires in the directors’ report certain disclosures about capital structures.

FRC Financial Reporting Council
The UK’s independent regulator responsible for promoting confidence in corporate reporting and governance.

FRRP Financial Reporting Review Panel
The Panel seeks to ensure that the annual accounts of public companies and large private companies comply with the Companies Act 2006 and applicable accounting standards.

FSA Financial Services Authority
The Financial Services Authority is an independent non-governmental body, given statutory powers by the Financial Services and Markets Act 2000. The FSA regulates the financial services industry in the UK and acts as the Competent Authority for setting and enforcing the rules applicable to listed companies and those admitted to trading on a regulated market.

FTSE 100/350 Financial Times Stock Exchange top 100/350 companies (share index)

GAAP Generally accepted accounting practice

IASB International Accounting Standards Board
The IASB is an independent body that issues International Financial Reporting Standards.
KPI Key performance indicator
A factor by reference to which the development, performance or position of the company’s business can be measured effectively.

Listed company
A company, any class of whose securities is listed (i.e. admitted to the Official List of the UK Listing Authority).

Listing Rules
The Listing Rules made by the UK Listing Authority for the purposes of Part VI of the Financial Services and Markets Act 2000.

Market capitalisation
A measure of company size calculated as share price multiplied by the number of shares in issue at a certain point in time.

OFR Operating and financial review
The OFR is a voluntary statement for inclusion in annual reports. It provides an analysis of the business through the eyes of the board of directors. Where an OFR is prepared, the Reporting Statement: Operating and Financial Review issued by the ASB provides recommendations on best practice.

Quoted Company
Section 385 of the Companies Act 2006 defines a quoted company as a company whose equity share capital:

a) has been included in the official list in accordance with the provisions of Part 6 of the Financial Services and Markets Act 2000; or

b) is officially listed in an EEA State; or

c) is admitted to dealing on either the New York Stock Exchange or the exchange known as Nasdaq.

Regulated market
Regulated market is defined in the Markets in Financial Instruments Directive. The European Commission website also includes a list of regulated markets at: http://ec.europa.eu/internal_market/securities/isd/index_en.htm

RS The Reporting statement: Operating and Financial Review
A statement of best practice on OFRs published by the ASB in January 2006.

TOD EU Transparency Obligations Directive
This directive aims to enhance the transparency of publicly traded companies through an EU-wide framework, by improving the information available to investors. It has been implemented in the UK via the DTR (see above).

Turnbull guidance
The guidance issued by the Turnbull Committee in September 1999 (subsequently updated in 2005) to assist listed companies in implementing the requirements of the Combined Code relating to internal control.

UK Corporate Governance Code
The UK Corporate Governance code (formerly the Combined Code) sets out standards of good practice in relation to board leadership and effectiveness, remuneration, accountability and relations with shareholders. It is applicable for periods commencing on or after 29 June 2010.

UKLA UK Listing Authority
The FSA acting in its capacity as the competent authority for the purposes of Part VI of the Financial Services and Markets Act 2000.
Deloitte would be pleased to advise on specific application of the principles set out in this publication. Professional advice should be obtained as this general advice cannot be relied upon to cover specific situations; application will depend on the particular circumstances involved. If you would like further, more detailed information or advice, or would like to meet with us to discuss your reporting issues, please contact your local Deloitte partner or:

Fay Cooke
fcooke@deloitte.co.uk

Tracy Gordon
trgordon@deloitte.co.uk

Isobel Sharp
isharp@deloitte.co.uk

The Deloitte Global Centre for Corporate Governance
For further information and resources on governance matters please refer to:

Welcome to the Centre for Corporate Governance

The Deloitte Global Centre for Corporate Governance is the leading centre for corporate governance research, education and development. It is a global centre for research and development in corporate governance and provides a platform for the exchange of ideas, knowledge and best practice. Our Centre is a unique model of the latest thinking on corporate governance in a range of countries around the world.

The Centre is an independent, non-profit-making organisation, and it is funded by a range of corporate and individual sponsors. It is a unique model of the latest thinking on corporate governance in a range of countries around the world.

How can we help?

Deloitte would be pleased to advise on specific application of the principles set out in this publication. Professional advice should be obtained as this general advice cannot be relied upon to cover specific situations; application will depend on the particular circumstances involved. If you would like further, more detailed information or advice, or would like to meet with us to discuss your reporting issues, please contact your local Deloitte partner or:

Fay Cooke
fcooke@deloitte.co.uk

Tracy Gordon
trgordon@deloitte.co.uk

Isobel Sharp
isharp@deloitte.co.uk

The Deloitte Global Centre for Corporate Governance
For further information and resources on governance matters please refer to:

Learn More

Governance in Brief
Your summary of the latest corporate governance developments.

• Governance in Brief

Year End

Corporate Governance Updates
These updates provide a monthly review of current key governance developments.

• Year end

Corporate Governance Reports

• Financial

Corporate Governance Reports

• Directors' remuneration disclosure checklist

Checklist

A series of checklists to assist companies to comply with current legislation and regulatory requirements.

• Directors' remuneration disclosure checklist

Dig Deeper

Setting the scene - A New Focus for Governance
This publication sets out a summary of the key issues that will be discussed in the Company's annual report.

• Setting the scene

Governing the board - A New Focus for Governance
This publication sets out a summary of the key issues that will be discussed in the Company's annual report.

• Governing the board - A New Focus for Governance

Survival or success? Directors' Alert: 10 issues for 2010
This publication sets out a summary of the key issues that will be discussed in the Company's annual report.

• Survival or success? Directors' Alert: 10 issues for 2010

A typical performance

A look at what listed companies are reporting in the results sections, and the key issues that will be discussed in the Company's annual report.

• A typical performance
The following publications survey a consistent sample of companies through a full cycle of periodic financial reporting requirements. All are available at www.deloitte.co.uk/audit.

Drowning by numbers – Surveying financial statements in annual reports (due November 2010)
This survey analyses the financial statements of listed companies. It includes a review of how compliance with disclosure requirements and the accounting policy choices made under IFRS varied, the level of variety in the presentation of primary statements and which critical judgements and key estimation uncertainties directors consider to be the most significant.

And there’s more – Surveying second halves’ interim management statements (June 2010)
This publication considers how UK listed companies have met the requirements for an interim management statement (IMS) in the second year of compliance with the Disclosure and Transparency Rules with their second halves’ IMS.

Down the TRack – Surveying preliminary announcements (May 2010)
This publication reviews what form companies’ announcements of their annual results took, compliance with the dissemination requirements of the DTR and what information companies chose to include in the financial highlights section of preliminary announcements.

Measuring by halves – Surveying half-yearly financial reporting (February 2010)
"Measuring by halves" analyses half-yearly financial statements. It reviews compliance with the Disclosure and Transparency Rules and IAS 34, how companies dealt with developments in IFRSs and what information companies choose to include in their Interim Management Report (the narrative part of the half-yearly financial report).