EQ BOARDROOM

Bulletin

Welcome to our monthly bulletin of what's happening within the financial services industry that will impact our EQ Boardroom clients.

This month we cover...

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The FRC's annual review of corporate governance and reporting	The FRC's review of the annual reports of smaller listed and AIM companies	Equiniti ES Forum

Dates for your diary

TUESDAY 4 DECEMBER
Equiniti end-of-year Drinks Reception at St Pauls Cathedral

WEDNESDAY 5 DECEMBER
ProShare Awards

BEIS target the 'broken' statutory audit market

A new Business, Energy and Industrial Strategy (BEIS) Committee inquiry into the future of audit has been launched.

This is in response to recent misleading audits such as at BHS, Carillion and Patisserie Valerie and the view put forward by the chair of the inquiry that the current audit market is 'broken'. The Financial Reporting Council (FRC) has also been criticised by BEIS for its passive record. The inquiry will feed into the recently announced review of the audit market by the Competitions and Markets Authority (CMA) and review of the Financial Reporting Council (by Sir John Kingman) on improving audit quality and competition in the audit market. BEIS states that its aim is to ensure that audit reform is linked to coherent reform of the wider corporate governance agenda.

The BEIS Committee's inquiry is asking for input on the following questions:

- What is the relationship between competition and quality in the audit market? How should reforms in one area complement the other?
- Do you agree with the CMA proposals (when published)? Will the remedies proposed be likely to increase quality and trust in audits? Are there any potential unintended consequences?
- Do you agree with the Kingman proposals regarding the FRC (when published)?
- To what extent do conflicts of interest undermine trust in audit? How best can they be removed or mitigated?
- How important to the quality of audit is the relationship between auditor and audited company? How can the right level of challenge be achieved? What role should shareholders have in ensuring high quality audits?
- Are the proposed reforms of audit consistent with other recent reforms of corporate governance? Are there any other consequential reforms required?

The deadline for submissions is 11 January 2019.

The press release announcing the inquiry is available here.

The Competitions and Markets Authority's review of the statutory audit market

The Competitions and Markets Authority is carrying out a market study into the statutory audit market to assess whether it is working as well as it should.

The study is focussing on three main issues:

1. Choice of auditor and switching between auditors;
2. The long-term resilience of the sector;
3. Incentives between audited companies, audit firms and investors.

The review will look at the characteristics of the audit market and at ideas to improve the market including how to improve incentives, further separating audit and non-audit services; and reducing barriers to entry and expansion of non-Big Four firms. Results of the review are expected early in 2019.

The Statutory Audit Market: Invitation to comment document is available here.

The FCA raises the profile of climate change risk

The Financial Conduct Authority (FCA) has published a Discussion Paper on climate change and green finance.

The FCA stated that it has published the paper as it must consider all major risks that have an impact on markets and institutions and climate change likely to have a significant impact on the UK's economy and financial services markets. The Discussion Paper sets out:

- How the different impacts of climate change could impact the FCA's long and short term objectives;
- Opportunities and risks the transition to a low carbon economy may present in the UK's financial services markets;
- Specific action the FCA will take to ensure that markets function well and deliver good outcomes for consumers.

The Discussion Paper also considers the necessity for climate related disclosures to be made to investors and asks a series of questions around how this might operate.

Comments on the Discussion Paper are requested by 31 January 2019 and is available here.

Business model, risk and viability reporting

The Financial Reporting Council (FRC) has published an implementation study report into business model, risk and viability reporting.

The report considers the development of reporting on these areas and follows on from its reports in 2016 and 2017. The FRC carried out its analysis by reviewing a sample of more than 100 annual reports covering 2017 and 2018.

Items of note in the review include:

- Investors still feel there is more that can be done to make business model, risk and viability disclosures more valuable. There have been some good developments but there is still a need for reporting to be more consistent and clearly linked throughout the annual report;
- Investors need information that is broad enough to give them a good understanding of the overall business but with enough detail to provide information about the performance and position of the company in the context of its business model;
- Successful business model disclosures often act as a guide for the content of the rest of the annual report, and it is here that the disclosure of business models are falling short;
- Risk reporting is relatively well developed and improvements have been made since the FRC's original report to the level of detail on risk tolerance, responsibilities and mitigating actions. However, there continues to be a lack of detail in areas, such as mitigating actions and links to the business model and key performance indicators (KPIs);
- Investors are now focussing on disclosures around the UK's withdrawal from the EU. Many companies highlight that Brexit creates a principal risk, however more detail is needed on the level of preparedness, the current stage of implementation of mitigating activities and numerical breakdowns of the impact. This type of disclosure was rare;
- Improvements have been made to viability reporting with some companies separating the viability statement into an assessment of prospects followed by an assessment of viability, providing more disclosure on both. Greater disclosure is required on scenario and sensitivity analysis that supports the viability statement, and reasoning behind the period selected.

The review gives examples of good practice reporting in these areas including those from Howden Joinery Group plc, Drax Group plc, SSE plc, Land Securities Group plc, Burberry Group plc, Vodafone Group plc and Informa plc.

Business model reporting; Risk and Viability Reporting – Where are we now? is available here.

The GC100 Group publishes guidance on Directors' Duties

The GC100 first issued a guidance note on s172 directors' duties when they came into force in 2007 under the Companies Act 2006.

This guidance has now been supplemented with additional guidance on practical steps directors can take to ensure s172 duties are addressed (the Guidance). The Guidance covers the following areas:

- A summary of suggestions of matters for directors to consider;
- Practical steps that can be taken by directors;
- A summary of the legal context;
- An example scenario of how s172 duties can be discharged in a specific business situation.

The Guidance states that having the correct culture within the company should form the context in which board decisions are made. Recommended practical steps for directors to consider include to:

- Ensure the company's strategy reflects the s172 duty.
- Establish and attend training courses on induction and with updates;
- Consider the information that is needed in order for the directors to carry out their role;
- Put in place policies and processes appropriate to support the company's strategy;
- Consider the approach to engagement with employees and other stakeholders.

The GC100 s172 Guidance is available here.

The FRC's annual review of corporate governance and reporting

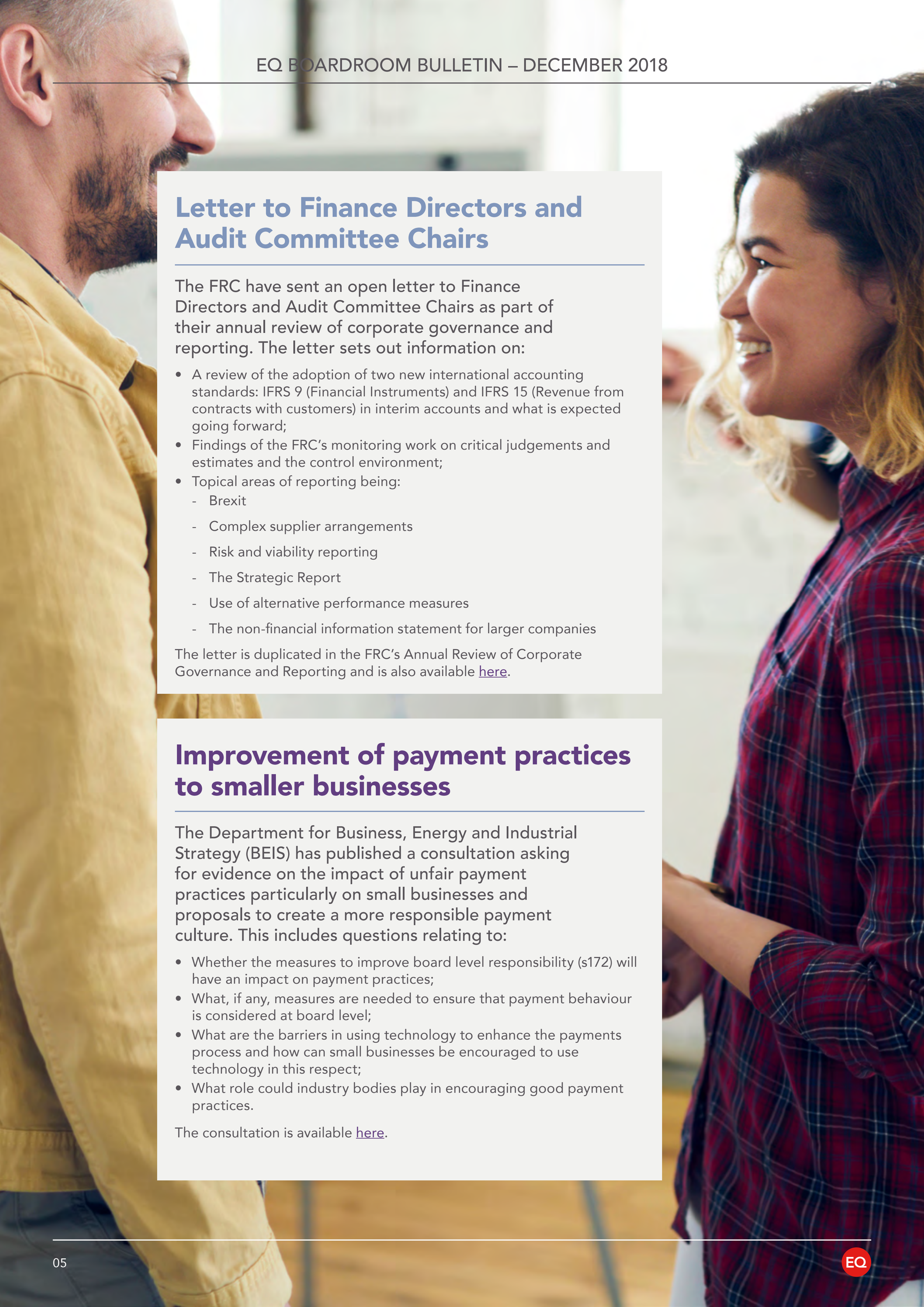
The Financial Reporting Council (FRC) has published its annual review of corporate governance and reporting.

The report was compiled from the analysis of the 220 annual and interim reports reviewed by the FRC for the year ended 31 March 2018 together with a number of thematic reviews. The thematic reviews included one on smaller listed and AIM quoted company reports and accounts.

The key areas on corporate reporting and governance highlighted by the FRC in its annual review are:

- Reporting on judgements and estimate disclosures and cash flow statements continue to be of the most concern to the FRC;
- The areas that cause challenges for companies in reporting are the use of alternative performance measures and whether reports are fair, balanced and comprehensive;
- Viability reporting has improved as has the increased focus on risk management. However, further improvements could be made to show more clearly how companies have assessed their prospects and viability;
- Compliance with the UK Corporate Governance Code (the Code) remains high with 95% of FTSE 350 companies reporting that they comply with nearly all of its provisions. Reporting on how companies have applied the Principles in the Code is often inadequate however with companies relying on the fact that they comply with the provisions;
- Explanations for non-compliance with the Code are often poor and need to be improved in order that the Code operates properly.

The Annual Review of Corporate Governance and Reporting 2017/2018 is available here.



Letter to Finance Directors and Audit Committee Chairs

The FRC have sent an open letter to Finance Directors and Audit Committee Chairs as part of their annual review of corporate governance and reporting. The letter sets out information on:

- A review of the adoption of two new international accounting standards: IFRS 9 (Financial Instruments) and IFRS 15 (Revenue from contracts with customers) in interim accounts and what is expected going forward;
- Findings of the FRC's monitoring work on critical judgements and estimates and the control environment;
- Topical areas of reporting being:
  - Brexit
  - Complex supplier arrangements
  - Risk and viability reporting
  - The Strategic Report
  - Use of alternative performance measures
  - The non-financial information statement for larger companies

The letter is duplicated in the FRC's Annual Review of Corporate Governance and Reporting and is also available here.

Improvement of payment practices to smaller businesses

The Department for Business, Energy and Industrial Strategy (BEIS) has published a consultation asking for evidence on the impact of unfair payment practices particularly on small businesses and proposals to create a more responsible payment culture. This includes questions relating to:

- Whether the measures to improve board level responsibility (s172) will have an impact on payment practices;
- What, if any, measures are needed to ensure that payment behaviour is considered at board level;
- What are the barriers in using technology to enhance the payments process and how can small businesses be encouraged to use technology in this respect;
- What role could industry bodies play in encouraging good payment practices.

The consultation is available here.

Summary of the first year of gender pay gap reporting

The Government has published a summary of data reported by employers under the first year of the Gender Pay Gap Information Regulations 2017.

Key findings were:

- Compliance with the regulations is 100% as at August 2018;
- 77% of median gender pay gaps were positive, 14% were negative and 9% reported a median gap of 0%;
- 57% of employers have more women than men among their lowest paid employees;
- 33% have more women than men among their highest paid employees;
- As at May 2018, 48% of employers had published an action plan setting out how they intended to tackle their gender pay gap.

The report is available here.

The future of corporate reporting

The Financial Reporting Council (FRC) has launched a project to challenge existing thinking about corporate reporting.

The project will consider current reporting practices, what information is needed by investors and other stakeholders, the purpose of corporate reporting and the annual report. Communication channels will also be considered. A thought leadership paper will be published by the FRC in the second half of 2019.

The FRC's press release on the project is available here.

Revision to the guidance on new reporting regulations

The Department for Business, Energy and Industrial Strategy (BEIS) has published revised 'frequently asked questions' (FAQ) which will assist companies in implementing changes brought in by the Companies (Miscellaneous Reporting) Regulations 2018.

The regulations were made in July 2018 and apply to financial years beginning on or after 1 January 2019. The first FAQ were published June 2018.

The main changes made to the FAQ include:

- Subsidiaries that are subject to the requirement to include a s172 statement in their strategic report may not have to provide as much detail if the relevant policies are set by the parent company. In this case they would need to report on how the group policies have been applied;
- If the required corporate governance statement is contained within an annual report that is published on the company's website then the statement does not have to be published separately;
- The government's preferred corporate governance code for private companies to use is the 'Wates Corporate Governance Principles for large Private Companies' currently under development;
- The new regulations apply for financial years beginning on or after 1 January 2019. However, any new remuneration policies for 2019 onwards will need to include the requirement for the illustration of impact of share price increased on incentive scheme outcomes;
- There is a little more detail on the methodology for calculating the CEO pay ratio.

The revised FAQ are available here.

The FRC's review of the annual reports of smaller listed and AIM companies

The Financial Reporting Council (FRC) has published the results of its thematic review into the annual reports of smaller listed and AIM companies.

The review specifically looked at the following areas:

- Strategic Reports;
- Alternative performance measures (APMs);
- Pension disclosures;
- Accounting policies, including critical judgements and estimates;
- Tax disclosures; and
- Cash flow statements.

The FRC gave advance notification of the review and reported that most of the companies notified made some improvements to their disclosures across all areas of the review. The larger companies generally made the most significant improvements. Improvements were mainly around the disclosures related to APMs and judgements and estimates. There were also some enhancements to the strategic report to provide commentary on all significant matters including tax, pensions and cash flows.

The report sets out the FRC's expectations for each item, what disclosures companies should include and best practice examples from some of the companies reviewed.

Reporting by Smaller Listed and AIM Quoted Companies is available here.

Guidance on the presentation of performance metrics in company reporting is published

In response to calls from investors, the Financial Reporting Lab (the Lab) has published guidance on the presentation of performance metrics in company reporting.

The guidance points out that performance metrics are used by investors for a wide range of purposes, from understanding how a company measures and views its own performance to assessing the value of the company or the forecasting of future performance. This raises the question of which metrics are most important to disclose and which provide the best picture of performance. The Lab has identified five principles for the reporting of performance metrics that will help investors. These are disclosing metrics that are:

- Aligned to strategy;
- Transparent;
- In context;
- Reliable; and
- Consistent.

The guidance – "Performance Metrics: Principles and Practice" is available here.

The 2018 Hampton-Alexander Review

The Hampton-Alexander Review published its first report in November 2016.

The aim of the review is to increase the number of women on FTSE 350 boards and in senior leadership positions below the board by a voluntary business-led approach. The key recommendations of the Hampton-Alexander Review are:

- 33% target for women on FTSE 350 Boards by the end of 2020;
- 33% target for women on FTSE 350 Executive Committees and Direct Reports to the Executive Committee on a combined basis by 2020;
- FTSE 350 companies to increase the number of women in the roles of Chair, Senior Independent Director and Executive Director positions.

The 2018 Hampton-Alexander Review has now been published and highlights the following:

- The top 100 companies are on track to meet the target of women holding one third of board level positions by 2020;
- All-male boards across FTSE 350 continue to fall from 152 in 2011 to 5 in 2018.

However, in the FTSE 350 almost one in four companies have only one woman on their board, and there remain 5 all-male boards. The review states that one in two appointments to boards for FTSE 350 firms must be women if the 33% target is to be met.

The 2018 Hampton Alexander Review is available here.

Employee Share Plan Updates

Employment Related Securities Bulletin

HMRC's most recent Employment Related Securities Bulletin (ERS Bulletin 30) was issued in November with updates on the non-statutory clearance process, share scheme catch-all rules, Enterprise Management Incentives, Shared Incentive Plans and penalties.

Employment related securities bulletins give information and updates on developments relating to ERS, including tax-advantaged employee share schemes. ERS bulletins are published when articles or updates are available and when HMRC have items to bring to our attention quickly.

You can subscribe to 'Business tax: Employment related securities' email alerts on GOV.UK by following this link and selecting 'Subscribe to email alerts'.

Brexit and Irish approved SAYE plans

In July, both ProShare and the Irish ProShare Association (IPSA) issued articles about Brexit and Irish approved SAYE plans. Current passporting rules enable financial firms in the UK to offer their services throughout the EU with a UK banking license, rather than obtaining a license to operate in each member state where they do business. Brexit will change this, potentially having an adverse impact on Irish employees who currently hold their Irish SAYE savings with UK-based SAYE savings carriers Barclays and Yorkshire Building Society.

Yorkshire Building Society and IPSA have written to the Irish Finance Department asking for an amendment to the rules to safeguard current Irish approved SAYE schemes even if no Brexit deal is struck.

Reported recently in the Irish press, the Irish Revenue is quoted as saying, "We will need to await the final outcome of negotiations between the EU and the UK to determine the implications, if any, for certified contractual savings schemes, post-Brexit."

Employee Share Plans – Ownership Matters

In October, Equiniti, along with a record number of attendees, came together at ProShare's 26th Annual Conference in London.

With a conference theme of 'why share ownership matters', delegates had an opportunity to learn more about what's topical with employee share plans.

Included in the speaker line-up were Equiniti's Phil Ainsley and Graham Bull whose discussion topic was 'To be or not to be a shareholder…is that the question?'. After joining their company's share plan, employees need to make a series of decisions on their savings and share entitlements. The session looked at when, what and how you can communicate with employees to help their decision to be, or not to be, a shareholder. Phil and Graham also looked at the different approaches taken by companies to inform employees about their choices at different stages of the share plan lifecycle.

Their presentation slides are available here.

An interesting write up 'Share plans conference serves a timely reminder that ownership matters', by Simon Osborne, CEO of ICSA: The Governance Institute, is produced on the ICSA website and can be read here.

Continuing the theme of employee share ownership, an update from the European Federation of Employee Share Ownership highlights that "Employee share ownership for all" has been the goal of European Policy for 30 years. The need for a European Action Plan was reaffirmed through a European Parliament Resolution of 23 October 2018 and a conference is taking place on 6 February 2019 in the European Parliament building to generate more support for the initiative.

ProShare Awards 2018

'Good Luck!' from Equiniti to all the companies shortlisted for this year's ProShare Awards being held on Wednesday 5 December.

Equiniti Employee Services Forum

For those who missed our annual Employee Services Forum, this year's key takeaway was the importance of telling a compelling, cohesive corporate narrative – for shareholders, employees, investors, customers and the media.

The Forum featured big picture discussions on Executive Remuneration, Corporate Governance reform, technology trends and Brexit. We delved deep into the details of international share plans and the latest LTIP rules.

All the slides, an overview of the event and two articles covering the key topics of Corporate Governance and how to set up a Global Share Plan can be found here.