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FRC PUBLISHES ITS ANNUAL REVIEW OF CORPORATE REPORTING 2022/23

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SUMMARY

The FRC has set out its expectations, in its Annual Review of Corporate Reporting, for the coming reporting season amidst the current economic background of high inflation, high interest rates and ongoing economic uncertainty.

This article will focus on some of the FRC's findings and expectations together with its plans to shine a spotlight on a number of large private companies and existing areas of poor compliance with reporting requirements.

The FRC's Annual Review of Corporate Reporting (Report) found that the general quality of corporate reporting across the 263 FTSE 350 company reports reviewed has been maintained. The Report discusses the top ten issues on which the FRC raised substantive questions with companies, its findings from thematic and other reviews and its overall expectations for 2023/2024, driven by its findings as well as matters which are likely to present reporting challenges for companies.

2023/2024 FRC EXPECTATIONS

Companies should:

- ensure disclosures about uncertainty are sufficient to meet the relevant requirements and for users to understand the positions taken in the financial statements;
- give a clear description in the strategic report of risks facing the business;
- provide transparent disclosure of the nature and extent of material risks arising from financial instruments;
- provide a clear statement of consistency with the Taskforce for Climate-related Financial Disclosures (TCFD); and

- perform sufficient critical review of the annual report and accounts including taking a step back to consider whether the report as a whole is clear, concise and understandable and undertake a robust pre-issuance review to consider issues commonly challenged by the FRC.

STRATEGIC REPORT AND OTHER COMPANIES ACT 2006 MATTERS

This year the most common areas where the FRC raised questions related to the requirements for the strategic report to be 'fair, balanced and comprehensive' together with compliance with the legislative requirements relating to distributable profits and dividends/share repurchases.

Points to note:

- The strategic report should not only focus on financial performance, but also explain significant movements in the statements of financial position and cash flows.
- Companies should ensure that they comply with the legal requirements for making distributions and share repurchases, including the requirement to file interim accounts that show sufficient distributable profits to support the transaction, if the distribution or repurchase exceeds distributable profits reported in the most recent annual accounts.

Inflation and rising interest rates: Companies should consider, amongst other things, how resilient their business model is to an inflationary environment, changes to the principal risks and uncertainties and the related mitigation actions, and the impact of inflation on suppliers, customers and employees.

REVIEW OF DIRECTORS' REMUNERATION REPORTS (DRR)

The FRC have extended its review to include directors' remuneration reporting for ten companies in preparation for its transition to the Audit, Reporting and Governance Authority (ARGA). Most of the points raised related to the clarity of targets and achieved performance for the annual bonus and long-term incentive plan awards.

Points to note:

- The FRC expect the salary component of Key Management Personnel (KMP) compensation to be higher than the remuneration disclosed in the single total figure table on the basis that KMP may include other senior employees in addition to the executive and non-executive directors.
- There should be consistency between the Alternative Performance Measures (or key performance indicators) used in the strategic report and the performance measures disclosed in the DRR. Where this is not the case, any differences, and the reasons for them, should be clearly explained.

- There should be consistency between ESG targets within the DRR and the narrative included within the TCFD disclosures.

THEMATIC REVIEW: REPORTING BY THE LARGEST PRIVATE COMPANIES

As previously set out in the consultation on 'Restoring Trust in Audit and Corporate Governance', the UK government is proposing to introduce new reporting requirements for companies that have an annual turnover of £750 million or more and 750 or more employees. To identify whether and where there are areas of poor compliance with existing reporting requirements for private companies that currently meet these thresholds, the FRC is undertaking a thematic review of between 20 and 25 private companies with year ends falling between September 2022 and March 2023 focussing on, amongst other things, revenue, financial instruments, strategic reports, judgements and estimates.

Their review is currently ongoing and the final report will be published in early 2024.

REVIEW OF TCFD AND CLIMATE IN THE FINANCIAL STATEMENTS

The FRC's current review cycle (2023/24) is the second in which premium listed companies have been required to provide TCFD disclosures, on a comply or explain basis, and the first for standard listed companies. As noted, companies are at very different stages of maturity in their reporting and the FRC expect to enter into substantive correspondence with companies who fail to meet their expectations on TCFD disclosures as practice becomes more established.

THEMATIC REVIEW: TCFD METRICS AND TARGETS DISCLOSURES

For further details on this, please see our article in Law360.

UPDATE ON THE FRC'S TRANSITION TO ARGA

Previously the UK government reported proposals to transform the FRC into a new regulator, ARGA, with increased scope and powers. However, several of the changes proposed require primary legislation and it is still unclear when the ARGA Bill will receive parliamentary time.

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