



Governance in Brief

Your summary of the latest corporate governance developments

Headlines

- EC publishes Green Paper on the EU corporate governance framework.
- FRC sets out thoughts on cutting clutter in annual reports.
- Deloitte's view on the future of financial reporting in the UK and Republic of Ireland.

EC publishes Green Paper on the EU corporate governance framework

In Brief: Following interviews with a sample of listed companies from different Member States and different economic sectors and meetings with corporate governance experts and representatives of the investor community, the EC has requested views on a number of areas relating to the board of directors, shareholders and the 'comply or explain' approach.

The Green Paper puts forward questions on a number of matters which are already dealt with in the UK Corporate Governance Code, company law or other relevant guidance.

For example:

- clear division of functions and duties between the chairman and the chief executive;
- diversity of the board;
- measures to protect the availability and time commitment of non-executive directors;
- external evaluation of the board at regular intervals;
- disclosure of remuneration policies and a shareholder vote on those policies and the remuneration report;
- a requirement to disclose departures from the country's corporate governance code and monitoring of these disclosures by an independent body;
- employee share ownership; and
- monitoring of asset managers with regard to strategies, costs, trading and the extent to which asset managers engage with the investee company.

It had been thought that the Green Paper might question the validity of the “comply or explain” approach but this has not been the case. The paper states that the approach is widely supported by regulators, companies and investors. However, shortcomings in the quality and sufficiency of explanations given in corporate governance statements have been noted. The paper asks whether companies should be required to provide detailed explanations where they depart from the recommendations of corporate governance codes and describe the alternative solutions adopted.

The paper states that the board should develop an adequate risk culture and arrangements to manage external and internal risks. There are questions about risk in terms of whether the board should approve and take responsibility for the company’s ‘risk appetite’ and report it meaningfully to shareholders. This is consistent with the existing Code Principle (C.2) that the board is responsible for determining the nature and extent of the significant risks it is willing to take in achieving its strategic objectives. A potential extension of this principle is that the board should ensure that the company’s risk management arrangements are effective and commensurate with the company’s risk profile. This goes beyond the current UK requirement for the board to conduct an annual review of risk management systems.

Other areas where the Commission is seeking views are as follows:

- existing EU legal rules which may contribute to inappropriate short-termism among investors;
- incentive structures for and performance evaluation of asset managers managing long-term institutional investors’ portfolios;
- independence of asset managers’ governing bodies from its parent company to enhance disclosure and management of conflicts of interest;
- obstacles to shareholder cooperation;
- influence of proxy advisers;
- shareholder identification; and
- additional rights for minority shareholders (including protection against related party transactions).

The Commission will take a decision on next steps after consideration of responses received. Any future legislative or non-legislative proposals will be accompanied by an extensive impact assessment taking into account the need to avoid disproportionate administrative burden for companies.

Date: 5 April 2011

Deadline for comments: 22 July 2011

Source: European Commission

Further info:

http://ec.europa.eu/internal_market/company/modern/corporate-governance-framework_en.htm

FRC sets out thoughts on cutting clutter in annual reports

In Brief: As demonstrated in the Deloitte publication “Swimming in words”, annual reports are getting longer and longer. The FRC recognises that clutter in annual reports is a problem, obscuring relevant information and making it harder for users to find the salient points about the performance of the business and its prospects for long-term success.

The ‘Cutting clutter’ report provides preparers of annual reports with practical aids for reducing clutter, giving ideas for how disclosures might look without the clutter, and factors to consider when planning the annual report process.

The FRC is keen for all of those involved in regulating, reviewing, preparing and using annual reports to change their behaviours to help remove clutter and improve corporate reporting. The Department for Business, Innovation and Skills will be consulting further on the framework of narrative reporting. The FRC will coordinate its work with that and will also seek further debate on how materiality should be applied to financial statement disclosures.

Date: 6 April 2011

Deadline for comment: 30 September 2011

Source: Financial Reporting Council

Further info:

<http://www.frc.org.uk/about/cuttingclutter.cfm>

Deloitte's view on the future of financial reporting in the UK and Republic of Ireland

In Brief: Deloitte has responded to the ASB's invitation to comment on the future of financial reporting in the UK and Republic of Ireland following the publication of FRED 43 ("Application of financial reporting standards") and FRED 44 ("Financial Reporting Standard for Medium-sized Entities") (together the FREDs).

In summary we:

- welcome the FREDs and support the ASB in seeking to replace UK GAAP as it currently stands;
- believe that the ASB should have a vision and plan to allow the UK to use international standards without amendment or deviation in the medium term;
- ask the ASB to promulgate the new rules as soon as possible;
- recommend that the ASB permits a lengthy conversion period through to 2015 so that companies may convert at their optimal point within this window; and
- indicate that further research and discussions are needed to assist the ASB in determining many of the details of the new regime. These are highlighted in our submission.

Date: 13 April 2011

Source: Deloitte

Further info:

http://www.frc.org.uk/documents/pagemanager/asb/Responses_to_FRED_UK_GAAP/CL25%20-%20Deloitte%20LLP.pdf

Time to take action

- Input to the debate on the EC Green Paper on corporate governance to help ensure that "comply or explain" survives.
- Consider using the FRC tips for cutting clutter when starting your annual report process and refer to the Deloitte publication "Swimming in words" for further analysis and guidance on the narrative reporting process.

On the horizon

- BIS proposals on narrative reporting.

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Designed and produced by The Creative Studio at Deloitte, London. 10941A

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