

15 April 2016

Mark Jackson  
Business Environment

By email: [mark.jackson@bis.gsi.gov.uk](mailto:mark.jackson@bis.gsi.gov.uk)

Dear Mark

## **Association of Accounting Technician response to Non-Financial Reporting consultation response form**

The Association of Accounting Technicians (AAT) is pleased to have the opportunity to respond to the consultation response form on Non-financial reporting, released on 16 February 2016.

AAT is submitting this response on behalf of our membership and from the wider public benefit of achieving sound and effective administration of taxes.

AAT acknowledges that the response may be subject to publication.

AAT would like to register interest to attend the BIS NFR workshops and is content to be contacted in the future to comment on consultation documents and for future research.

AAT has taken the format of the BIS online response and inserted it into our own response style.

### **About AAT**

AAT is a professional accountancy body with over 49,800 full and fellow members<sup>1</sup> and 75,600 student and affiliate members worldwide. Of the full and fellow members, there are over 4,200 members in practice who provide accountancy and taxation services to individuals, not-for-profit organisations and the full range of business types.

AAT is a registered charity whose objectives are to advance public education and promote the study of the practice, theory and techniques of accountancy and the prevention of crime and promotion of the sound administration of the law.

If you have any questions or would like to discuss any of the points in more detail then please contact Aleem Islan, Technical Manager, at [consultation@aat.org.uk](mailto:consultation@aat.org.uk) or Brian Palmer, Tax Policy Advisor, at [aat@taxpolicyadvice.co.uk](mailto:aat@taxpolicyadvice.co.uk)

Yours sincerely



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<sup>1</sup> Figures correct as at 31 March 2016

**Association of Accounting Technicians response to consultation questions**

**Q1) Flexibility on where to provide the non-financial statement:**

What is your view on permitting companies flexibility to place information where they feel most appropriate within the boundaries laid out by the EU NFR Directive? Please explain your reasons.

**Comments**

It is AAT's view that non-financial reporting (NFR) information that is relevant to investors in judging the performance, future prospects and risks facing a company should be included in the Annual Report and Accounts (ARA) and should not be separated out into a separate report.

The current regime, developed over a considerable period of time, and revisited only recently with the introduction of the Strategic Report, has positioned the UK at the vanguard of transparent corporate reporting. The UK government is to be congratulated on its work to date, and as such AAT would not wish to see the progress made in the UK undermined through adoption of the Directive.

That said, to the extent that NFR information is not relevant to investors, or is not specific to the reporting of current performance or future prospects, e.g. is standing or static information, that information should be permitted to be published separately, and in situations where a company must maintain a website, the website may be the most appropriate place for it. This view is reflected in AAT's answers to the questions below on other information that the government could allow to be dropped or presented other than in the ARA.

However, in the case of the information required by the EU NFR Directive, as this is directed to investors and shareholders through the mechanism of requiring information to be given "to the extent necessary for an understanding of a company's development, performance, position and the impact of its activity matters"<sup>2</sup>, AAT believes that the NFR required by the Directive should accompany the audited financial statements in the ARA. The requirements are broadly similar to the current UK Strategic Report, which offers an important vehicle to illuminate and describe further the information in the audited financial statements, while also allowing management to discuss the future prospects of the business and the activities around human rights, the environment and so on which are not captured in the financial statements, but which are often vital to the sustainability of the business.

**Q2) Information that could be placed in a Separate Report:**

We would welcome suggestions for information, currently required by law that could be placed in the separate report

**Comments**

AAT does not believe that the Strategic Report information, however it is supplemented or amended by the NFR requirements, should be placed in a separate report, but should instead remain in the ARA, for the reasons noted in the answer to Q1. However, the government has recently begun to require information driven by other policy considerations, including Gender Pay Gap Reporting<sup>3</sup>, Modern Slavery and transparency in supply chains<sup>4</sup> and transparency on Prompt Payment Practices<sup>5</sup>, to be published on company websites or in other places, separately from the ARA.

AAT suggests that the government should take a much more comprehensive and holistic approach to this issue. It should review all the requirements for publishing information in the ARA and decide whether each can be better disclosed on company websites, probably in a designated "regulatory information" area. As well as disclosures not aimed directly at investors, this could include standing data about a company that does not particularly relate to any one accounting period and would not affect investor views of performance or prospects, but which are nevertheless still important for transparency reasons. It would include much of the current content of the Directors' Report and the list of subsidiaries and major holdings required under s 409 Companies Act 2006. The requirement for large groups to disclose the registered offices of subsidiaries takes up significant space in companies' reports and often becomes out of date during the succeeding period. If the requirement to disclose was moved from the companies' accounts to a designated section of a company's website, as well as being reported at least annually to Companies House, the list

<sup>2</sup> See p 15 of the Consultation Document.

<sup>3</sup> <https://www.gov.uk/government/consultations/mandatory-gender-pay-gap-reporting>.

<sup>4</sup> <http://www.legislation.gov.uk/ukpga/2015/30/section/54/enacted>.

<sup>5</sup> <http://www.parliament.uk/business/publications/written-questions-answers-statements/written-statement/Commons/2015-03-20/HCWS428/>.

could be updated in real-time and monitored more easily by those with an interest.

AAT believes that government needs to go even further and encourage regulators and arms of government to take a positive approach in this area so that websites are used as a means of disclosure wherever suitable. For example, there are requirements to disclose information in the ARA in Section 9.8 (continuing obligations) of the FCA Listing Rules, much of which could be moved to company websites. Moreover, where parts of government and regulators require information to be provided on company websites, it would be ideal if a consistent approach could be taken towards when the information must be put up (outside the ARA reporting timetable to spread workload), how long it should be kept, when and how it should be changed and updated, how to retain a history of changes, if and when old information can be removed and so on. A consistent approach, to the extent possible, across government and regulatory bodies, could make web-based reporting much more efficient and streamlined which, in itself, would offer greater scope for deregulation.

### **Q3) Advantages and Disadvantages of a separate non-financial statement:**

What do you see as the advantages and disadvantages, for your organisation of the separate statement?

#### Comments

In responding AAT has considered the broader perspective of companies required to publish the ARA and other information and for the recipients of that information. There are significant disadvantages in separating NFR information that is directly related to the company's performance for the period and management's current view of its future prospects from the audited financial statements, investors and shareholders may be prejudiced if they received the information separately.

It is not clear that there is much advantage in terms of a reduced workload if the contents are so closely related to investor communications about the company's results.

In addition, there are requirements for auditors to check such information for consistency with the audited financial statements and comment on compliance with the law (and indeed the auditor requirements in this area have only just been strengthened: see the answer to Q7). Removing it from the ARA would raise the question of assurance and it is not clear that there is any reason for the current requirements to be changed.

Only if a particular item of information is not investor focussed would a separate report seem sensible, and the advantage would come from allowing it to be produced outside the very busy ARA preparation timetable as well as it not impeding clear and focussed investor information in the ARA. Moreover, where information is required for specific public policy reasons and is reported outside the ARA, decisions can be made on a case-by-case basis on the need for assurance.

### **Q4) Advantages and disadvantages of the Implementation Options.**

What do you see as the advantages and disadvantages of the various implementation options?

#### Comments

It is AAT's view that both options have disadvantages that make them unattractive and risk undermining the very positive example set by the UK in this area.

Option 1 is complicated and would lead to companies that are large PIEs, with over 500 employees, producing slightly different information to those quoted companies that do not also fall into that PIE category and that follow what is required now for the Strategic Report. This would be unhelpful to users of the information and in any event these quoted companies are of a size and significance such that it does seem appropriate to require them to apply the additional requirements of the Directive, which are relatively modest compared to the current requirements of the Strategic Report that apply to quoted companies. In particular, all companies should already have anti-bribery and corruption policies and practices in place in order to ensure compliance with the Bribery Act 2010<sup>6</sup>.

AAT notes that PIEs are at risk of moving in and out of the affected category because their number of employees falls below or rises above 500 on a regular basis are likely to take practical measures to deal with the problem. It is likely they will follow the requirements once they reach 500 employees for the first time, and then would be unlikely to cease to provide the information – i.e. they would continue to do so on a voluntary basis - in any year where there was a temporary dip in the number of employees below 500; they would only cease to do so if the downsizing were sufficiently substantial and expected to be permanent. There does not appear to be much that can be done about this practical problem as the Directive does not

<sup>6</sup> <https://www.gov.uk/government/publications/bribery-act-2010-guidance>.

<p>allow for any relief, so while it is a disadvantage it may not be a relevant factor in the decision on how to implement the Directive.</p> <p>Option 2 would be most detrimental to users of quoted company accounts that fall outside the large PIE with over 500 employees category, when such companies have already expended considerable efforts to produce Strategic Reports that have helped them explain their performance and future prospects and which have been well-received by investors. If the government believes it made the right policy decision (a decision with which the market concurs) very recently when it introduced the Strategic Report with its additional requirements for quoted companies then Option 2 is not the right approach as it goes against that decision.</p>
<p><b>Q5): Preferred option relating to scope</b></p> <p>Considering the possible advantages and disadvantages provided by the flexibilities contained within the EU NFR Directive, which would be your preferred option in terms of which companies should be required to disclose non-financial information?</p>
<p>Comments</p> <p>AAT does not favour either of the proposed options: see the responses to Q4 and Q6.</p>
<p><b>Q6) Alternative Options</b></p> <p>Are there any other options for implementing the EU NFR Directive the Government should consider?</p>
<p>Comments</p> <p>The overall requirements of the NFR Directive are, through the UK government's excellent engagement with its development, very close to the UK's requirements for the Strategic Report, which rightly focusses on the information needs of investors. The government only recently created the requirement for a Strategic Report, including the scope for additional information falling on quoted companies (although this was similar to previous requirements, it did give an opportunity to revisit the scope, which was not changed). There is no evidence to suggest this scope is no longer appropriate and the companies involved have spent considerable time and effort improving their NFR reporting over the last few years, with positive feedback from investors.</p> <p>Therefore, AAT's view is that the government should implement the NFR Directive by requiring large PIEs with over 500 employees to prepare a Strategic Report through amendment to Section 414A CA 2006 (if there are any such PIEs that are currently not caught by that section).</p> <p>Government should amend the requirements of Section 414C CA 2006 as necessary to continue to include the current content required in the Act for the Strategic Report while adding the new information required by the NFR Directive, on anti-bribery and corruption for example, and align the wording where it is considered necessary.</p> <p>The additional information in Section 414C(7) should continue to apply to quoted companies, but the government should then simply extend the scope to large PIEs with over 500 employees as well. Section 414(4)(b) should be amended in line with the Directive and be the same for all companies required to produce a Strategic Report; such non-financial KPIs are important.</p> <p>In addition, AAT recommends that Section 414C(6), which allows an exemption from producing non-financial KPIs for medium-sized companies, ought to be withdrawn as it has always been problematic to allow such companies to not provide non-financial KPIs and yet expect that they can meet the overall objective of the Strategic Report.</p> <p>Although this will amount to a small amount of gold-plating of the minimum scope of the Directive, it is proportionate in relation to the types of companies affected. It has the virtue of relative simplicity and, most importantly, it will maintain the gains that have been made across quoted companies in this important area, established by the current legal requirements.</p>
<p><b>Q7) Assurance of Non-Financial Information</b></p> <p>Should the Government require that the non-financial statement be verified by an independent assurance service provider'?</p>
<p>Comments</p> <p>Section 496 CA 2006 already requires auditors to consider the consistency of the Strategic and Directors' Report with the audited financial statements. The section has also recently been expanded to require auditors to state whether the reports have been prepared in accordance with the applicable requirements</p>

and whether any information has come to their attention during the course of the audit that suggests the reports are misleading in any way. AAT believes these requirements to be appropriate for NFR material that is relevant to investors and should accompany the audited financial statements.

For other information that may be placed on a company website or in a separate report, the need for assurance should be assessed on a case-by-case basis. AAT can envisage a situation where such information is not assured to begin with, but once companies have experience in producing the information, assurance may be demanded by the market. Of course company boards may wish to obtain their own internal assurance or validation of new information to be published.

**Q8) Advantages and Disadvantages of third-party validation**

What do you see as the advantages and disadvantages of requesting third party assurance?

**Comments**

For NFR information within the ARA, auditors already have an appropriate role, as noted in the answer to Q7 above, which should be allowed to bed down. Therefore, AAT recommends that there is no further need for change at the current time.

AAT suggests that for any other NFR information disclosed outside the ARA, as noted above, the need for any assurance should be considered on a case-by-case basis.

For any form of assurance however, there needs to be a strong framework for the preparation of the material, against which it can be judged by the assurer. This is not always the case and it may not always be possible to provide suitable assurance. However, it appears to AAT that there is more scope for an innovative approach to assurance when such information is outside the usual scope of auditor review within the ARA.

**Q9) Other Options**

Are there any other options the Government should consider for Third Party Verification?

**Comments**

The government should consider further research on whether non-investor NFR information and on what forms of assurance might be possible or appropriate. See the answer to Q19 below.

**Q10) Advantages and Disadvantages**

What do you see as the advantages and disadvantages of preparing or receiving the non-financial statement electronically via a company's website?

**Comments**

As already noted, AAT's view is that investor-focused NFR information should remain with the audited financial statements. In that context, this question is only appropriate to the extent that one considers whether the whole of the ARA might be delivered electronically.

The Financial Reporting Lab at the FRC is looking at this issue and their work would seem to indicate that the current needs of users would be served by requiring companies to publish their ARA as a searchable PDF<sup>7</sup>. Most listed companies already do so, but this is in addition to supplying paper copies where requested. There is a risk in disenfranchising those who do not wish to receive information electronically if government moves too quickly in this area. AAT recommends that market practice and demand should be allowed to develop ahead of any regulation.

One issue the government could tackle, in conjunction with the FCA, is to deregulate and cut costs by allowing the ARA of listed companies to be "made public" in PDF only, rather than require publication in unedited full text.

A more joined up approach is required between different arms of government and regulators, including across Europe. The government may wish to monitor responses to the recent ESMA consultation<sup>8</sup> on electronic reporting and consider how it will respond to the debate at that level.

**Q11) Additional Protections**

Considering your response to Q7, are there any additional protections that the government should consider?

<sup>7</sup> <https://frc.org.uk/Our-Work/Publications/Financial-Reporting-Lab/Lab-Project-Report-Digital-Present.pdf>.

<sup>8</sup> <https://www.esma.europa.eu/press-news/consultations/consultation-paper-european-single-electronic-format>.

<p>Comments</p> <p>AAT is not aware of any further protections that should be considered.</p>
<p><b>Q12) Number of Companies Providing an Electronic Report</b></p> <p>We are interested in the number of companies that currently send their annual report electronically. Considering your shareholders, how many, as a percentage, opt to receive their annual report as a printed copy?</p>
<p>Comments</p> <p>AAT does not have access to such information on the number of companies that currently send their annual report electronically. However, the Companies House website mentions<sup>9</sup> that, “Data is only available for electronically filed accounts, which currently stands at about 60% of the 2.2 million accounts filed at Companies House each year”, which suggests that these companies have the capacity to send their annual report electronically.</p> <p>To clarify, AAT is a charity limited by guarantee therefore has members rather than shareholders. A conservative figure of over 96% of AAT’s members opted to receive their annual report electronically last year.</p>
<p><b>Q13) Definition of Senior Manager</b></p> <p>BIS would welcome suggestions as to how this definition may be improved to reflect better the intention of this requirement.</p>
<p>Comments</p> <p>AAT agrees that the definition is not appropriate in that companies are required to include in the category of senior managers all those who are directors of subsidiary companies in a group. For many if not most groups, this does not reflect a true picture of the “pipeline” of talent which might ultimately get to main board level, and whose identification we think is the aim of this part of the legislation.</p> <p>In order to remove this problem, the government should simply delete Section 414C(10) and if necessary add in to Section 414C(9) the requirement to apply the same principles in a group situation.</p>
<p><b>Q14) Other Comments on this requirement</b></p> <p>BIS would also welcome other comments on this regulation including views on the approach suggested</p>
<p>Comments</p> <p>AAT has no other comments on this particular requirement, other than to note that with the advent of Gender Pay Gap Reporting, companies are now asked to disclose information on gender in multiple formats and using different information. A more joined-up approach ought to be considered, but in any event there are wider diversity issues that need to be addressed, not just on gender.</p>
<p><b>Q15) Reporting Regulations</b></p> <p>What other reporting regulations would you suggest that could be repealed?</p>
<p>Comments</p> <p>AAT recommends that the government liaise with the FCA and FRC in order to consider more broadly the regulations that could be repealed across all sources of requirements. Much of the continuing obligations for disclosure in the FCA rules in particular is of questionable value and sometimes repeats (but with small differences) disclosures required by other sources. There is real scope for deregulation in this area if a joined-up approach is taken.</p>
<p><b>Q16) Other Information</b></p> <p>Is there any information that could be moved outside the Annual Report?</p>
<p>Comments</p> <p>AAT recommends that the government should be much bolder in considering allowing certain information to be moved online, but widen the consideration to requirements elsewhere, particularly in the FCA Listing Rules, where the Continuing Obligations chapter requires a whole raft of disclosures whose value is</p>

<sup>9</sup> <https://www.gov.uk/government/organisations/companies-house/about/about-our-services>

doubtful but in any event which might be better moved out of the ARA.

Of the examples listed in the table on page 24 of the consultation, AAT suggests that repeal is appropriate for the policy on employment of disabled persons for the reason given. For the other information listed, most of it is standing information or information in the company's articles which could easily be disclosed and regularly updated on a company's website. To the extent that investors believe such information should be drawn to their attention, companies should be permitted to disclose it on a regulatory section of a company's website.

AAT suggests that all the requirements of the Directors' Report should be considered as a possible candidate for online disclosure, as much of it does not relate to specific performance of the company for a particular period or indicate its future prospects. It is AAT's view that if the government enables this, it will encourage companies to experiment with the placing of the information and that they will gain feedback from their investors as to their preferences.

**Q17) Analysis of the Costs and Benefits of implementing the NFR Directive**

Type of Organisation

**Q17a) Are you a company (not a PIE), a company which is a PIE (as described in para 2.6), an NGO, institutional investor or other type of organisation? If you are a PIE please specify whether you are a parent company or a subsidiary company.**

PIE (Parent)	
PIE (Subsidiary)	
Non-Governmental Organisation	
Institutional Investor	
Other (please specify)	AAT is an incorporated charity.

When considering your answers, we would very much appreciate information on any costs you will incur as a result of the proposals for implementing the EU NFR Directive, both in terms of money and time (e.g. describe which type of staff will be involved, for how long). We would appreciate any information on new systems or practices your organisation may adopt, or existing processes that may change, because of the Directive.

**Q17b) Do you expect to incur any "one off "or "ongoing costs" as a result of having to comply with the requirements of the EU NFR Directive over and above what you incur currently on your non-financial reporting obligations? Please describe these costs. (One off costs could include staff time to familiarise your organisation with the regulations or updating of internal guidance for staff; on-going costs could include additional time to review non-financial data in each year subsequent to first year)**

**Q18c) How would your costs change if you were allowed to provide your non-financial statement separately within six months of the balance sheet date on your financial report?'**

**Q18d) How would your costs change if you were allowed to provide this report electronically on your website and did not have the obligation to provide hard copies except in exceptional circumstances?'**

**Q18e) What additional costs would you expect if the government required that an independent assurance services provider verify the non-financial statement? This may be in terms of money or resources costs such as staff time.'**

Benefits to your company of the EU NFR Directive?

**Q18f) Please describe any benefits to your company you expect will arise because of the EU NFR Directive (to your organisation or more widely).**

If you are happy for BIS officials contact you with further questions about the impact of the EU NFR directive, please provide your contact details.

Comments

AAT has no direct access to cost or benefit information, subject to our answer to Q18g below.

## Q18g) Any Other Comments

Do you have any other comments about the costs and benefits that will result from the EU NFR Directive?

## Comments

In AAT's view companies need to regain the trust of the public given the trauma of the financial crisis that arose in the last decade.

The types of disclosures required by the NFR Directive will increase transparency by indicating the business's attitude to ethical issues that will affect the longterm sustainability of the business for the benefit of investors, employees and the wider community.

It is AAT's view the government should not underestimate the benefits that should flow from these disclosures and the aid it will give to the rebuilding of trust. For that reason, if for no other, a wider group of companies should be subject to the requirements than the scope of the NFR Directive, as advocated in our answer to Q6 above.

## Q19) Additional Comments

Do you have any additional comments on this directive

## Comments

AAT recommends the government put in place the requirements of the NFR Directive quickly and use the opportunity for efficiency by repealing disclosure requirements that are no longer of value and allowing some information to be moved to company websites, as outlined in the above answers.

Beyond that, AAT's view is that the government should be prepared to devote an appropriate amount of time to working with the FRC and its Digital Futures<sup>10</sup> project in order to explore the options available for more electronic reporting of ARA material, assessing user wishes and the potential barriers represented by the current patchwork of legislative and regulatory requirements across multiple laws and regulations.

In addition, there is a clear need for a dialogue with the auditing profession on the extent to which the current audit boundary is also a barrier to further integration of reporting financial and non-financial information and what innovative means can be developed to deal with the issue.

This work needs to be carried out in a spirit of innovation and openness, outside the usual statutory or regulatory mechanisms, and AAT commends the FR Lab at the FRC as an ideal forum for debate and experimentation. All participants need to take some time to consider the next steps as there are unlikely to be any easy solutions.

<sup>10</sup> <https://frc.org.uk/Our-Work/Codes-Standards/Our-Work-Codes-Standards-Financial-Reporting-Lab/Current-Projects.aspx>.