



Governance *in brief* Tips for your 2018 annual report

Headlines

- There have been a large number of changes to the corporate governance agenda and the expectations of annual reports over the past year.
- Although disclosure requirements arising from changes to legislation and to the UK Corporate Governance Code will not take effect until 31 December 2019 annual reports, the board's work to implement some of the changes to the Code's principles and provisions will be well advanced and it will be helpful to investors and stakeholders to disclose this activity in this year's report.
- This publication summarises the key changes in a helpful checklist.

Introduction

Although the disclosure changes required by the 2018 legislation and the new 2018 UK Corporate Governance Code do not need to be seen in annual reports until early 2020, there is a huge weight of anticipation that companies now know what they will do and disclose in order to achieve the transparency and engagement sought in the new Code, and thereby improve trust in business.

Of course, it is for you to determine how far to go along this path and indeed to weigh encouragement for information against how far advanced you are in your implementation journey.

This publication is designed to help you make those decisions, together with a timely reminder about areas of focus for this year's annual report both from the regulator and from investor feedback we have received.

A note on how to use this document: use the weblinks for any research you want to undertake prior to printing this document.

The 2019 board agenda

The 2018 Code and other corporate governance reform

Agenda item	Reference material - with clickable links where available	On the board agenda? Y/N
<p>2018 UK Corporate Governance Code (2018 Code) – keep under review the decisions the board has made regarding implementing key elements such as board independence, workforce engagement. Good corporate governance is “a journey” and high quality corporate governance statements describe changes made during the year.</p> <p>For details on areas the board may wish to consider for further discussion during the year, see the next two items on this list and also “Implementation of the 2018 UK Corporate Governance Code” below.</p>	<p>Governance in brief – FRC issues new UK Corporate Governance Code</p> <p>Implementation of the 2018 UK Corporate Governance Code, below</p>	
<p>Does the annual report (or other papers accompanying the resolution to re-elect directors) set out the specific reasons why the individual director’s contribution is, and continues to be, important to the company’s long-term sustainable success?</p>	<p>2018 Code Principle J 2018 Code Provision 18</p>	
<p>All companies applying the Code are now required to re-elect all directors annually. Smaller companies that are doing this for the first time in 2019 AGMs may wish to draw out this change in the 2018 annual report.</p>	<p>2018 Code Principle J 2018 Code Provision 18</p>	
<p>For large private companies, including subsidiaries and other companies not required to provide a corporate governance statement under the DTR. Select a corporate governance code, if desired, and consider future reporting obligations for periods commencing on or after 1 January 2019.</p>	<p>Governance in brief – BEIS issues legislation to deliver key corporate governance reforms</p> <p>Governance in brief – The Wates Corporate Governance Principles for large private companies</p>	
<p>CEO pay ratio – in the audited section of the Directors’ Remuneration Report; need to manage internal and external messaging carefully; also note that it is complex to gather needed information for new disclosures.</p> <p>Applicable for periods commencing on or after 1 January 2019 – however, investors are pushing for early disclosures, in relation to 2018.</p>	<p>On the board agenda – Executive pay – in the spotlight</p> <p>Investment Association letter on Principles of Remuneration for 2019</p>	

This year’s annual report

Implementation of the 2018 UK Corporate Governance Code

Companies will report under the 2016 UK Corporate Governance Code for periods commencing prior to 1 January 2019. In this year’s annual report there is no required disclosure arising from the new “2018 Code”. However, in practice, in most cases the 2018 Code will already be either fully implemented or in course of implementation by the time companies publish this year’s annual report.

Disclosure under the 2018 Code in early 2020 will relate to activities undertaken throughout the year – for instance, for a December year end, the Code will apply from 1 January 2019 to 31 December 2019 and disclosure will cover the full year. Many companies will therefore wish to indicate where matters discussed in the annual report are different from 1 January, if decisions have been taken and implemented, both to provide good and current information to readers and to avoid any suggestion that there may have been a departure from the 2018 Code for any part of the year.

The checklist below indicates those areas where we expect to see disclosure from some companies in annual reports for 31 December 2018 and subsequent dates.

Area of potential disclosure	Reference material – with clickable links where available	In the annual report? Y/N
Does the annual report explain the nature of the work the board is performing (or has performed) to implement the 2018 Code?	2018 Code On the board agenda	
Is it clear from the annual report what the board considers the company’s purpose, values and strategy to be? Has company purpose been articulated and communicated?	2018 Code Principle A 2018 Code Provisions 1&2 On the board agenda – Purpose and the Sustainable Development Goals	
Does the board discuss how purpose, values and strategy are aligned to company culture and disclose the activities the board takes to monitor culture ? Does the board describe how its governance contributes to the delivery of its strategy ?	2018 Code Principle A 2018 Code Provisions 1&2 On the board agenda – Articulating the board’s monitoring and assessment of corporate culture	
Is it clear from the annual report that the board has put effective mechanisms in place to understand the views of the company’s key stakeholders ? Does the board identify which stakeholders it considers to be key?	2018 Code Principles D&E 2018 Code Provision 5 On the board agenda – Section 172 in practice and on paper	

Area of potential disclosure	Reference material – with clickable links where available	In the annual report? Y/N
<p>Has the board discussed who they consider to be part of their workforce and why, bearing in mind that this is a worldwide requirement and goes beyond employees? Is it clear from the annual report that the board has put effective mechanisms in place to engage with the workforce?</p> <p>Note that the method used is a focus area for government and investors and would be anticipated to be discussed in this year’s annual report.</p>	<p>2018 Code Principles D&E 2018 Code Provision 5 On the board agenda – Section 172 in practice and on paper</p>	
<p>Is it clear from the annual report in what way the board’s approach to whistleblowing / speaking up has changed from an audit committee led approach to a board led approach?</p>	<p>2018 Code Principle E 2018 Code Provision 6</p>	
<p>Is it clear whether board composition, including the tenure of the chair, will meet the requirements of the 2018 Code from the start of the year, or is there disclosure of how the board is planning to align to these requirements?</p>	<p>2018 Code Principle G 2018 Code Provisions 9-11, 19</p>	
<p>Where there is disclosure in the annual report regarding consideration of board directors’ other appointments or time availability, is it clear that the board now has a responsibility to give prior approval to new appointments?</p>	<p>2018 Code Principle H 2018 Code Provision 15</p>	
<p>In nomination committee disclosures and disclosure of the approach to succession planning, has the focus on diversity in the new Code been taken into account? Has the board considered whether to include the disclosure of gender diversity in senior leadership?</p>	<p>2018 Code Principle J 2018 Code Provision 23 On the board agenda – Talking about diversity</p>	
<p>Has the board considered how it identifies emerging risks and whether to disclose the procedures in place to identify these risks in the annual report?</p>	<p>2018 Code Principle O 2018 Code Provision 28 On the board agenda – Identifying and addressing emerging risks</p>	

Area of potential disclosure	Reference material - with clickable links where available	In the annual report? Y/N
Is the board satisfied with how it gains internal assurance ? Has the board considered disclosing how internal assurance is achieved, and if there is no internal audit function, how this affects the work of external audit?	2018 Code Principle O 2018 Code Provision 26	
Does the remuneration committee report acknowledge the new Code's focus on review of workforce remuneration and related policies ? Is there any discussion of planned policies to bring in changes to the Code regarding length of long-term incentive award schemes, post-employment shareholdings, pensions and application of discretion?	2018 Code Principles P-R 2018 Code Provisions 33, 36-37 On the board agenda – Executive pay – in the spotlight	

Other considerations for this year's annual report

Disclosure item	Reference material - with clickable links where available	Satisfactory disclosure? Y/N
New accounting standards - Final activity and disclosures around implementing IFRS 15 Revenue from Contracts with Customers Periods commencing on or after 1 January 2018	Closing Out 2018 On the board agenda – Key messages from the FRC's Corporate Reporting Review Team	
New accounting standards - Final activity and disclosures around implementing IFRS 9 Financial Instruments Periods commencing on or after 1 January 2018	Closing Out 2018 On the board agenda – Key messages from the FRC's Corporate Reporting Review Team	
New accounting standards - With the mandatory effective date of IFRS 16 Leases being only one year away, both the FRC and ESMA expect companies to provide both qualitative and quantitative company-specific disclosures on the effects of their adoption.	Closing Out 2018 On the board agenda – Key messages from the FRC's Corporate Reporting Review Team	

Disclosure item	Reference material - with clickable links where available	Satisfactory disclosure? Y/N
Viability statement – Have you described your longer term prospects over the business cycle in the manner requested by the FRC and investors?	On the board agenda – Key messages from the FRC’s Corporate Reporting Review Team Also see feedback from investors below	
Viability statement – Have you incorporated Brexit scenarios into both your assessment and your disclosures?	On the board agenda – Key messages from the FRC’s Corporate Reporting Review Team	
Strategic report – has consideration been given to the FRC’s updates to its Strategic Report Guidance, including disclosure on company purpose, sources of value (especially those elements not reflected in the financial statements) and stakeholder engagement ?	On the board agenda – Key messages from the FRC’s Corporate Reporting Review Team	
Strategic report - Those with “ complex supplier arrangements ” (i.e. including financing arrangements) are expected to disclose the nature and amount and impact on liquidity.	Closing Out 2018	
Strategic report - Companies in scope of the EU Non-Financial Reporting (NFR) Directive should provide a separate non-financial information statement within the strategic report, referring through to information required to be disclosed by law on environmental matters (including the impact of the entity’s business on the environment), employees, social and community matters, respect for human rights, anti-corruption and anti-bribery matters.	Closing Out 2018 On the board agenda – Key messages from the FRC’s Corporate Reporting Review Team	

Disclosure item	Reference material - with clickable links where available	Satisfactory disclosure? Y/N
<p>Strategic report - With initiatives such as the Task Force for Climate-related Financial Disclosure (TCFD) recommendations and greater investor and stakeholder interest bringing climate further into the spotlight, boards should consider how to report the impact of their company's operations on the environment and how environmental matters may affect development, performance and position – remembering that the NFR Directive (see above) also mandates certain disclosures in this area.</p> <p>Note: increasingly, some investors are asking questions directly of auditors. This is a key area where this is happening as some investors do not believe that current company disclosure is sufficient.</p>	<p>Closing Out 2018</p> <p>On the board agenda – Stepping up on climate change</p>	
<p>Strategic report – With the issue of disclosure of dividend policy and practice gaining recent traction, companies are reminded to report clearly in one place their policies in this area. In particular some investors are calling for clear disclosure of distributable reserves.</p>	<p>Closing Out 2018</p>	
<p>Taxation – have you considered how you will communicate with investors regarding the impact of tax changes on your ETR?</p>	<p>On the board agenda – Reporting on tax</p>	

Feedback from investors

Disclosure item	Satisfactory disclosure? Y/N
<p>Audit committees – investors are looking for more visibility around where the audit committee has challenged management on areas of judgement and the quality of the control environment.</p>	
<p>Audit committees – investors want more depth and clarity in disclosures around the quality of external audit to enable their own assessment. In particular, they are keen for audit committees to draw out:</p> <ul style="list-style-type: none"> • how they have supervised the audit and scope of the audit; • how they have supervised audit quality and what indicators they have used, including the quality of the firm and the lead audit partner; • where the auditor has made a difference; and • whether management has informed the auditor of any investor concerns in relation to financial reporting judgements and how they have been addressed if so. 	
<p>Investors also wish the audit committee to draw out the unadjusted differences and why they have not been adjusted.</p>	
<p>Audit committees – investors want to know that the audit committee has thoroughly considered key issues around accounting judgements and the disclosure on significant issues should be around the activities and separate and independent challenge by the audit committee, rather than relying on the audit report and the accounting policy disclosures.</p>	
<p>Audit committees – investors want to know about the scope, resourcing and quality of internal audit and, if there is no internal audit function, how the audit committee gains assurance over the control environment. They want information about controls and whether these are sufficient to prevent fraud.</p>	
<p>Viability statement – investors want the narrative around the viability statement to be informative and the quality of disclosure to reflect the rigour and extent of scenario planning regarding principal risks, in particular this year regarding Brexit.</p>	
<p>Long-term prospects – investors want the disclosure to be clear and differentiated. It should adequately draw out the strategic position of the company and activities to manage emerging risks such as decarbonisation and other disruptors to the business model.</p>	
<p>Business model – investors wish to see the business model description adequately describing shorter term risks and how the company is addressing these.</p>	
<p>Principal risks – investors want more informative detail around principal risks and the exposures the company faces, rather than simple assurance that they are under control. Details of how the board identifies emerging risks should also be included.</p>	
<p>Key performance indicators – investors want these to be the measures used in the business and to align clearly with strategy.</p>	
<p>New accounting standards - Final activity and disclosures around implementing IFRS 9 Financial Instruments, IFRS 15 Revenue from Contracts with Customers for periods commencing on or after 1 January 2018, plus the status of implementation of IFRS 16 Leases.</p>	

For further information:

All Governance in brief and Governance in focus publications can be found at www.deloitte.co.uk/governancelibrary. Need to Know and other accounting publications can be found at <https://www.iasplus.com/en-gb>.

Deloitte View

- All eyes will be on company annual reports this year as the government, investors and the media alike look to businesses for signs they are serious about restoring public trust.
- Although none of the new disclosure requirements take effect until periods commencing on or after 1 January 2019, we believe there are plenty of opportunities for companies to illustrate the path they are following in 2018 annual reports.

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For further details about the Deloitte Academy, including membership, please email enquiries@deloitteacademy.co.uk.

Contacts – Centre for Corporate Governance

Tracy Gordon – 020 7007 3812 or trgordon@deloitte.co.uk

Corinne Sheriff - 020 7007 8368 or csheff@deloitte.co.uk

William Touche - 020 7007 3352 or wtouche@deloitte.co.uk



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