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Dear Permanent Secretaries

The Chancellor has recently announced that the OFR will no longer be a mandatory requirement. The DTI has now published the amending Regulation and at the same time made a corresponding announcement seeking views on certain aspects of the business review that arise out of the EU Accounts Modernisation Directive requirements.

Financial reporting – reporting of numerical out-turns estimated to have arisen from prior operations at a past date – is inherently retrospective. Yet both running a company and making decisions on whether to invest, or maintain an investment in it, are essentially about the future.

The key requirements in the OFR were developed in the UK over many years and included:

- Narrative reporting
- Consideration of trends and risks
- Discussion of matters affecting future performance and the potential for business strategies to succeed

We hope that these main thrusts will be retained and encouraged under a voluntary arrangement.

We note too that the IASB has begun to consult about a requirement for a management discussion.

The Modernisation Directive and the need for a business review in Annual Accounts is about bringing the whole of Europe up to a *minimum* standard for corporate reporting. Current UK practice is materially superior to this, to the benefit of investors and issuers (our core Association membership is made up of individuals working for corporate issuers). This is not a question of “gold-plating” since the concept of an OFR is already well established amongst quoted companies on a voluntary basis. As professional treasurers we feel that good practice in the UK should go beyond the Modernisation Directive’s business review, since that is not

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particularly forward-looking. We hope that the FRC will continue to issue guidance on what is good practice for an Operating and Financial Review, as the ASB has done in the past, and that is based on reporting standard RS1.

Whatever the expressed intentions of any business review, however, discussion of the future inevitably involves the expression of opinion and the making of assumptions. There is great risk that such discussion will always be bland and tending to a legally drafted “boiler plate” format unless there is a clear and explicit (not merely implicit in other law) protection against civil suit, for Boards and individual directors, for statements made and opinions expressed in good faith and not recklessly.

Our members have extensive experience of involvement in corporate reporting by the companies they work for. This experience confirms that in the absence of explicit protections forward looking narrative reporting will not be done at all meaningfully. The experience in the US does suggest that safe harbour provisions do encourage more meaningful commentaries.

We know that the view has been expressed by the DTI that such an explicit safe harbour is not necessary in the UK. This may, strictly, be true. However, we are firmly of the view that in order to influence actual behaviour of directors to make the reports meaningful – which is, after all, the objective – rather more is necessary.

Given a supportive legal background, we believe that market pressures on listed companies and their own self-interest will drive practice towards much more useful narrative reporting by companies on those aspects the directors themselves consider to be important. Good practice can then be left to build up and adapt through guidance and best practice dialogue over a number of years.

This will enable the UK’s excellent traditions of corporate governance and (relative) openness voluntarily embraced by leading companies to develop ahead of the less open traditions of much of mainland Europe.

All of the above is consistent with our previous inputs to the UK’s long development of what has become called the Operating and Financial Review.

The ACT will be responding to the request for views on the business review in due course but we thought it might be helpful to flag the important point about the need for a safe harbour at an early stage.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'J. Grout', with a stylized flourish at the end.

John Grout  
**Technical Director**

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