Outcome of Risk & Viability Reporting survey from the FRC Financial Reporting Lab

Risk & Viability Reporting

Set up by the Financial Reporting Council to improve the effectiveness of corporate reporting in the UK, the Financial Reporting Lab provides a safe environment for listed companies and investors to explore innovative reporting solutions that better meet their needs.

Since the financial crisis there has been an increasing focus on how boards of companies manage risk and assess their viability. Investors are also increasingly focused on how directors promote the success of a company and how it manages risks that might threaten this success. In 2014, the Financial Reporting Lab ("the Lab") of the Financial Reporting Council announced a series of projects to cover business model, principal risk and viability reporting. These projects seek to explore the areas of most interest to investors and consider where companies face challenges in deciding what disclosures to make and how best to present them.

Having released *Business model reporting* in 2016, the Lab carried out a project on risk and viability project and published its report in November 2017. This project examines the views of companies and investors on the key attributes of principal risk and viability reporting, their value and use. In seeking the views of retail investors, a survey was sent out to UKSA and ShareSoc members, and it is encouraging that almost 200 responses were received.

Overall, the results from this survey were consistent with the messages heard from institutional investors. Below, we have provided more detailed results, split between principal risks and viability statements.

Principal risks

The questions on principal risk disclosures were aimed at understanding how the disclosures are used, and what information is most important to understand. Highlights from the survey results are as follows:

- 59% think that the annual report and accounts is important for providing principal risk information
- 57% say that their investment decisions are influenced by the robust risk assessment process in the annual report and accounts
- 62% say that their investment decisions are influenced by the principal risk disclosures in the annual report and accounts
- The most popular source of information to identify risks to companies is financial analysis and media, for example analysts' reports and financial/business publications (including business sections of national newspapers).
- For principal risk disclosures in the annual report:
  - The most useful piece of information is the changes in the principal risks since the previous year
  - Respondents also find categorization of risks useful, although had no preference between type or timeframe
  - There is no obvious preference for risks being presented as either gross or net.
- 61% find useful the quantification of the impact of each principal risk. The vast majority would like to see the quantification of monetary impact and likelihood. Some respondents also suggested quantification of the impact on stakeholders.

The Lab's report confirms that the annual report and accounts is an important document for all investors, and identifies the provision of specific risk information as a key need of investors. As well as changes in principal risks and categorisation, the report also highlights (i) information around the priority of risks and (ii) clear linkage to other areas of the annual report and accounts, as key information for most investors.

Long-term viability statement

Following the outcome of the Sharman Inquiry, the viability statement was introduced in the 2014 version of the UK Corporate Governance Code in order to provide a means for directors to report annually on the long-term prospects of the company. The survey questions were aimed at understanding how useful information on long-term viability is to investors, and how aware they are of the viability statement disclosure. Key points are:

- The long-term viability of a company is important to 87% of respondents when making their investment decisions.
- However, only 43% of respondents are aware of the viability statement requirement in the Code. Of those that are aware, over half consider the viability statement useful.
- The most important information to include in the viability statement is: i) Length of period over which the company has assessed viability; ii) The assumptions and qualifications included in the assessment; and, iii) The sensitivity/scenario analysis conducted by the company.
- Respondents on average think that a 4 year time frame for viability is right. However, individual views ranged from 1 to 10 years, with several citing that it is dependent on the sector and business cycle.
- Almost all respondents think that disclosures on principal risks & uncertainties and long-term viability could be improved.

The Lab's report observes that for most companies the introduction of the viability statement has resulted in greater focus on risk management at board level, but that this is often not reflected in the viability statement disclosures. The report encourages companies to communicate positive messages in the viability statement about the long-term future of the company and how it is managing its risks.

You can find *Risk and viability reporting* on the Lab's website, as well as copies of previous reports and information on future work. Finally, our thanks go to all members who have participated in the project.

Patrick Leach