Annual Review of Corporate Reporting:

2020/21

Contents

1. Introduction 3

2. Findings: overview 6

3. Findings: in greater depth 7

3.1 Ten most frequently raised topics 8

3.2 Other findings 27

4. Thematic reviews and other guidance 30

4.1 CRR's thematic reviews 30

4.2 Financial Reporting Lab 35

5. Our expectations for 2021 and future developments 36

5.1 Key disclosure expectations for 2021/22 36

5.2 Developments in corporate reporting 37

6. CRR monitoring activity 42

6.1 How we perform our reviews 42

6.2 Review activities for the year 43

6.3 Publication of CRR interaction 45

6.4 Post-review survey 49

6.5 Transforming the FRC 50

Appendices 51

Appendix I: Scope of CRR work 51

Appendix II: How to deal with a CRR enquiry 52

1. Introduction

Quality of corporate reporting and areas for improvement

We were pleased to note that our detailed monitoring work did not identify a decline in reporting quality, despite the challenges of reporting in the continuing Covid-19 pandemic. Most of the company reports covered by this review commented on the pandemic: the earliest, published in March 2020, referred to the potential risks arising, while later reports showed the effects on companies' results and prospects. We saw companies responding to FRC guidance by including additional information on key forward-looking judgements, such as going concern, which were of particular interest to investors. We encouraged companies to take advantage of temporarily delayed filing requirements to help manage disruption to their usual governance processes.

We observed incremental improvements in the quality of information reported in strategic reports and better linkage to the financial statements. Disclosure of significant judgements and estimation uncertainty also continued to improve. Both of these areas had been subject to our increased focus in recent years. We welcome the enhancements adopted by many entities.

This year we raised an increased number of queries in relation to the more recently introduced standards; specifically, IFRS 15 'Revenue from Contracts with Customers' IFRS 16 'Leases' and financial instruments standards (IFRS 9 'Financial Instruments' and IFRS 7 'Financial Instruments: Disclosures').

We continue to identify numerous errors in cash flow statements. Our Cash flow and liquidity disclosures thematic provides detailed information about the nature of the questions we raise in this area.

We also raised a considerable number of queries in relation to deferred taxation, particularly in relation to the evidence supporting the recognition of deferred tax assets by loss-making entities. We will continue to challenge companies where disclosures in this area are lacking, especially where:

- the factors taken into consideration in such cases or the sensitivities to changes in the underlying assumptions are not explained; or
- the disclosures are inconsistent with other information available in the rest of the annual report, or elsewhere.

Companies should carefully consider the issues most frequently identified in our reviews (see section 2). 'Corporate Reporting highlights' provides a summary of the most significant findings from our reviews.

2021/22 priorities

Our routine monitoring of annual reports and accounts during the 2021/22 cycle includes a focus on:

- climate-related risks and new disclosures; and
- judgement and uncertainty in the face of the continuing economic and social impact of Covid-19.

Companies should ensure that the impact of these matters on their business is appropriately reflected in the financial statements and wider annual report.

Climate-related reporting

In 2020, the FRC undertook a thematic review of climate-related considerations in the context of compliance with regulatory requirements, good governance and investor expectations (see section 3.2.2). More recently we carried out a thematic review of emissions and energy use disclosures under the new Streamlined Energy and Carbon Reporting (SECR) rules (see section 4.1.4). We encourage companies to take account of our findings when preparing their future reports, and we will continue to monitor how well companies have met our expectations as part of our routine reviews.

Next year, premium listed companies will be required to disclose their compliance with the Taskforce for Climate-related Financial Disclosures (TCFD) recommendations on a comply-or-explain basis. We will consider the quality of their disclosures against this new requirement. Please see section 5.2.3 for more details.

1. Introduction (continued)

Impact of Covid-19

Our 2020 thematic review of the financial reporting effects of Covid-19 found that, although companies provided sufficient information to enable a user to understand the impact Covid-19 had on their performance, position and future prospects, some reporting - particularly in relation to interims - would have benefited from more extensive disclosure.

We were reassured that our detailed monitoring work during the 2020/21 review cycle did not identify a decline in reporting quality as a result of the pandemic. However, disclosures on judgements and assumptions about the future will remain important to users of reports, particularly when considering matters such as going concern and liquidity. In consequence, as part of our routine reviews in 2021/22, we continue to consider whether companies:

- explain the significant judgements and estimates made;
- provide meaningful sensitivity analysis or details of a range of possible outcomes;
- describe any significant judgements made in determining whether there is a material uncertainty about their ability to continue as a going concern; and
- ensure that assumptions used in the going concern assessment are compatible with those used elsewhere.

Overview of our monitoring activities and outcomes

We performed 246 reviews as part of our 2020/21 review cycle, which represents a 14% increase on the reviews conducted in the prior year (2019/20: 216 reviews; 2018/19: 207 reviews). We expanded our resources this year and used our larger team to focus on topical matters though our thematic work.

Our focus continues to be on larger companies, which have the greatest effect on market confidence, with 72% of our reviews attributed to FTSE 350 companies (2019/20: 67%; 2018/19: 65%).

Just over half of our cases arose from thematic reviews. As part of 2020/21 review cycle, we performed thematic reviews on:

- the financial reporting effects of Covid-19;
- IFRS 15 'Revenue from contracts with customers' (a follow-up);
- disclosure of the impact of IFRS 16 'Leases' in the first year of application;
- cash flows and liquidity disclosures;
- quality of reporting in relation to climate change; and
- Interim reporting.

We have performed four further thematic reviews as part of our 2021/22 review cycle. Our findings from these reviews and the Interim reporting thematic are outlined in section 4.1. The results of our 2020/21 thematic reviews have been incorporated into the overall findings in section 3.1.

We wrote to 97 companies (2019/20: 96; 2018/19: 80) with substantive questions about their reporting, asking for additional information or further explanation. As with previous years, the majority of these cases resulted in companies volunteering or agreeing to make improvements to their future disclosures. We always follow up such undertakings by reviewing companies' subsequent reports. We expect companies to check that they have met their undertakings to us when they perform the pre-issuance checks of their reports and accounts. In 2020/21 we had to re-open one case where a significant breach of financial reporting requirements had been identified during the undertakings check. In 2019/20 we reopened one case (2018/19: two cases) where the companies had not adequately fulfilled their agreed undertakings.

We asked 15 companies (2019/20: 14) that had to restate comparative information in their report and accounts as a result of our enquiries to draw the restatements to users' attention in those accounts, as these cases represented more significant non-compliance.

No Press Notices in relation to companies' accounts were issued during the year (2019/20: one).

1. Introduction (continued)

Purpose of the report

Who is this report for?

This report is primarily aimed at preparers and auditors of corporate reports and accounts, and investors.

The following documents are also available:

- A Corporate Reporting highlights document - a separate short summary of our key messages intended for CEOs, CFOs, audit committee chairs, other senior management and for others with an interest in corporate reporting who do not need the detail in the main report or who would find a summary helpful.
- Key matters for 2021/22 annual reports and accounts - a summary of key considerations for the forthcoming reporting season.

What is this report for?

This report contains the main findings arising from the FRC's corporate reporting monitoring work, which is conducted by its Corporate Reporting Review (CRR) team.

It sets out our view of the current state of corporate reporting in the UK, what makes for better quality reporting, and where we see shortcomings requiring improvement. We explain our expectations for the next reporting season. These are shaped by our findings, as well as developments in the reporting requirements and business environment.

The report also shares relevant insights from recent FRC Lab reports, which invite input from investors as well as preparers.

This report provides preparers and auditors with an understanding of what needs to be on, or higher up, their agenda in relation to financial and narrative reporting against the backdrop of the continuing effects of the Covid-19 pandemic and the risks posed by climate change. Users expect to see both issues integrated into companies' decision making and reporting.

This report refreshes the key messages from our thematic review of the financial reporting effects of Covid-19, published in July 2020. It also reflects our work on enhancing the quality of narrative and financial reporting of the effects of climate change.

Our findings and case studies

We include case studies to illustrate selected key findings and areas for improvement. Our case studies provide examples of better disclosure, annotated to explain what makes it more effective. They do not represent any particular company’s reporting. However, the points they illustrate reflect real matters that have arisen in the course of our reviews and enquiries.

2. Findings: overview

As in prior years, we saw both examples of good practices and areas for improvement. The table opposite shows the ranking of the ten topics that arose most frequently in our correspondence with companies over the last three years.

During the 2020/21 review cycle, we continued to focus on the quality of reporting against the requirements of International Financial Reporting Standards 9 and 15, which are still relatively new. We considered how well companies complied with the requirements of IFRS 16 and the Streamlined Energy and Carbon Reporting (SECR) rules for the first time. We also assessed the quality of interim reporting in a thematic review.

We were pleased to see examples of good quality reporting and improvements in some specific aspects of certain disclosures. For example:

- The quality of strategic reports continued to improve – there were fewer instances where we challenged companies' compliance with the requirement to produce a report that is fair and balanced, or where the principal risks were omitted. We were also pleased to see some improvements in the reporting on climate change, following our 2020 thematic review into that topic. For example, we noted better explanations of net zero commitments and scenarios. However, considerable scope for further enhancements in this area remains.
- Companies also improved their reporting of alternative performance measures (APMs). We saw companies providing more reconciliations of APMs to their IFRS or UK GAAP equivalents. We also saw improvements in labelling of APMs and in their definitions.
- We were pleased that the companies generally complied with the minimum statutory reporting requirements of the SECR rules.
- The quality of interim reporting was generally good.

However, opportunities for further improvement remain, as evidenced by the fact that a large majority of our reviews result in companies enhancing their disclosures as a minimum. We still identify some potential issues from desktop reviews, causing us to seek clarification or further explanation from companies.

Many of the queries we raise are a result of apparent inconsistencies in information reported in the financial statements and another part of the annual report and accounts.

We continue to be concerned about the number of queries we raise in relation to compliance with the requirements of IAS 7 'Statement of Cash Flows'. As in prior years, many of the cash flow statement errors described in sections 3.1.3 and 6.3 were identified through critically analysing the line items appearing on the face of the statement. Companies should increase their focus on cash flow statements as part of their pre-issuance reviews.

Ten most frequently raised topics

Topic	2020/21	2019/20	2018/19
Judgements and Estimates	1	1	1
Revenue	2	3	10
Statement of Cash Flows	3	7=	5
Impairment of Assets	4	2	4
Alternative Performance Measures (APMs)	5	5	3
Financial Instruments	6	4	8=
Strategic Report and Companies Act	7	6	2
Provisions and Contingencies	8	7=	7
Leases	9=	-	-
Income Taxes	9=	-	-
Fair Value Measurement	-	9=	8=
Business Combinations	-	9=	-

Section 3 analyses each of the above topics in further detail.

3. Findings: in greater depth

Section 2 includes a table that lists the ten topics that we raised most frequently in our correspondence with companies.

Sections 3.1.1 to 3.1.10 provide further detail in relation to each topic. These sections also provide bullet point summaries of the more significant or common issues identified during our reviews, with examples of how better disclosures met our expectations. This year we include case studies on two of the top ten topics:

- Expected credit loss provisions and credit risk-related disclosures (section 3.1.6) ; and
- Disclosure of evidence supporting recognition of deferred tax by loss-making entities (section 3.1.10).

These summaries and case studies are not a substitute for considering the detailed requirements of relevant reporting requirements, but they do provide insights into common areas for improvement. We encourage preparers and their auditors to familiarise themselves with the issues identified and consider whether they are relevant to their own reports and accounts.

Sections 3.2.1 and 3.2.2 summarise findings in other areas of our focus, which we encourage companies to consider in their future reporting.

Disclosure objectives

We expect companies to consider the overall objectives of financial reporting, as well as the detailed requirements of individual standards. Providing only the specifically required disclosures may not always be sufficient to comply with the overall objectives. In these circumstances additional information should be disclosed to supplement a standard's required disclosures. Conversely, if the specifically required disclosures are immaterial, they may obscure more important information. In these circumstances those immaterial disclosures should be omitted from the financial statements.

Topic pages include a chart showing the relative frequency of the key sub-topics, identified by the colour of the commentary tables.

We have highlighted on the following pages the overall disclosure objectives of the relevant standards and other similar disclosure requirements or suggestions. We have identified the IFRS sources.

3.1.1 Judgements and estimates

A. B. C.

The disruption and uncertainty caused by the pandemic has been significant for many businesses throughout 2020/21. The extent of the uncertainty, and lack of any consensus view of the future impact of Covid-19 on the economy, made the need for full disclosure of judgements, assumptions and sensitive estimates significantly more important than usual. Company Guidance, issued by the FRC in March 2020, and updated in December last year, highlighted the need for enhanced disclosures and encouraged companies to provide as much context as possible for the assumptions and predictions underlying the amounts recognised in the financial statements. This included, where relevant, information about potential sensitivities to changes in assumptions or ranges of possible outcomes. The disclosure of significant judgements and estimation uncertainty was a key area of focus in our reviews, which is reflected in the findings for the year.

In addition, we conducted a thematic review of Viability and Going Concern disclosures, in response to the increased attention to such disclosures and the underlying judgements in the current environment. Please see section 4.3 for a summary of the key findings from that review.

A. Key sources of estimation uncertainty

- Carrying amounts of the assets and liabilities subject to estimation uncertainty were not identified in some instances.
- The key assumptions underlying the measurement of assets or liabilities subject to a significant estimation uncertainty were not always quantified.
- Disclosure of sensitivities or ranges of potential outcomes were sometimes missing or cross-referenced to parts of the annual report that did not contain the required information.
- It was sometimes unclear whether the estimation uncertainty had been disclosed because there was a significant risk of a material adjustment in the following year (paragraph 125 of IAS 1 ‘Presentation of Financial Statements’) or for some other reason.

We do not discourage additional disclosures where the directors believe that it is relevant to users. We encourage companies to make a clear distinction between disclosures required under paragraph 125 of IAS 1, where there is significant risk of a material adjustment in the following year, and disclosures of other uncertainties (for example, where the risk of a material adjustment is not significant or arises over a longer period). This helps users to focus on the most important areas of estimation uncertainty.

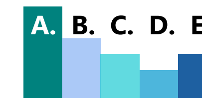
B. Significant accounting judgements

- We queried significant judgements where the associated disclosures were not clear (e.g. the reasons why the judgement was necessary, the factors considered and the outcomes not explained).
- We queried where there was an apparent inconsistency between a significant accounting judgement or a significant estimation uncertainty disclosure and another part of the report (e.g. as indicated in the audit committee report, audit report, viability statement or going concern disclosure).

C. Material uncertainties in relation to going concern

- One company included information about material going concern uncertainties outside of the financial statements. However, the financial statements neither identified the uncertainty, nor disclosed a significant judgement in relation to the going concern assessment.
- Another company’s disclosure about expected compliance with banking covenants was inconsistent with the conclusions reached by the auditors in their report. However, the judgement made by management in reaching their conclusion was not explained.

3.1.2 Revenue



We continue to raise a considerable number of queries in relation to revenue recognition policies and related disclosures. The findings below are from our routine reviews and our follow-up thematic review on IFRS 15. We strongly encourage preparers to read the thematic report, which provides more context and disclosure tips, as well as examples of good and inadequate disclosure.

... an entity [should] disclose sufficient information to enable users... to understand the nature, amount, timing and uncertainty of revenue and cash flows (paragraph 110 of IFRS 15)

A. Transaction price and the variable consideration constraint

- Descriptions of the types of variable consideration that exist within customer contracts were sometimes unclear or incomplete.
- The methods used to estimate variable consideration, either 'the expected value' or 'the most likely amount', and how the variable consideration constraint was applied to the estimated amount, were not disclosed or unclear in some cases.

Companies need to consider how the application of the variable consideration constraint affects disclosures about estimation uncertainties. Disclosures that refer to a significant risk of a downward adjustment to revenue suggest that the variable constraint may not have been applied appropriately.

B. Performance obligations

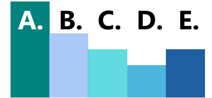
- Accounting policies for revenue from significant performance obligations were sometimes not clear or missing.
- There was scope for improvement in disclosures of the timing of revenue recognition, including whether this is at a point in time or over time, and exactly when revenue is recognised for 'point in time' performance obligations.
- Some financial statements contained insufficient information about the methods used to measure the extent to which 'over time' performance obligations had been satisfied. This should include: a description of the method, how it was applied in practice and why the method resulted in the faithful depiction of the transfer of goods or services.
- Some disclosures required by IFRS 15 in relation to performance obligations were missing or incomplete (such as the significant payment terms, nature of promised goods and services and information about the remaining performance obligations).

Companies need to disclose significant accounting judgements made in applying IFRS 15.[1] This could include judgements made in determining:

- the timing of satisfaction of performance obligations (e.g. judgements made in evaluating when a customer obtains control of promised goods or services for performance obligations satisfied at a point in time); and
- the transaction price and the amounts allocated to performance obligations.

1 IFRS 15, paragraph 123

3.1.2 Revenue (continued)



C. Principal versus agent considerations

- It was sometimes unclear how a company had concluded whether it was acting as a principal or agent when transacting with customers. The related judgements were not always explained.

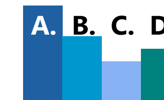
D. Contract balances

- Accounting policies and disclosures required by IFRS 15 in relation to material contract balances were sometimes missing, including: an explanation of the nature of the balances; significant changes; how the timing of satisfaction of performance obligation relates to the typical timing of payment; and the corresponding effect on contract assets and liabilities.

E. Other IFRS 15 points

- We raised queries in relation to the costs to obtain or fulfil a contract, including: the basis for concluding that certain costs fell into the scope of IFRS 15 and not another standard (e.g. IAS 16 'Property, Plant and Equipment'); and missing IFRS 15 disclosures, such as a breakdown of closing balances of capitalised costs by category.
- The accounting for claims recoverable from third parties was not always disclosed (this is an area where IAS 37 'Provisions, Contingent Liabilities and Contingent Assets' may apply).
- In several cases, we queried whether variations on construction contracts were accounted for as contract modifications.
- We asked for clarification where disaggregated revenue disclosures were inconsistent with other information in the annual report and accounts.

3.1.3 Statement of cash flows



The findings in this section are those from our routine reviews and our thematic on cash flow and liquidity disclosures.

The quality of reporting in relation to cash flow statements remains an area of significant concern. In 2020/21, six companies (2019/20: five, 2018/19: four) restated their cash flow statements as a result of our enquiries. Further details of the most recent restatements are provided in section 6.3.

We believe that many of the errors could have been avoided by robust pre-issuance reviews by companies, built into their financial statement close process. We encourage companies to consider the guidance in our thematic report, which provides further information about the nature of the questions we have raised on the cash flow statement in the last three years.

A. Reported cash flows

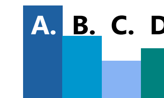
- There were apparent discrepancies between the amounts in the cash flow statement and the amounts reported elsewhere in the annual report and accounts.
- Descriptors used in the cash flow statement were sometimes confusing or misleading, such as cash flows described as 'principal on leases' including interest.
- The indirect method of reporting cash flows from operating activities was applied incorrectly in some cases (e.g. the net cash flow reconciliation was determined starting with an incorrect number, which was an APM, rather than the profit or loss reported under IFRSs).
- Cash flows were reported on a net basis in a number of cases, which was not in compliance with the requirements of IAS 7.
- The aggregated cash outflow within investing activities due to an acquisition did not take account of the cash acquired in the subsidiary.

Additional information may be relevant to users in understanding the financial position and liquidity of an entity (paragraph 50 of IAS 7)

B. Classification of cash flows

- We queried inconsistent application of accounting policies for similar items, such as interest payments on leases being classified as operating cash flows, while interest on borrowings was classified as a financing cash flow.
- Acquisition-related expenses were incorrectly classified as investing, rather than operating cash flows.
- Parent company accounts reported amounts borrowed from subsidiaries as investing, rather than financing cash flows; and amounts lent to subsidiaries as financing, rather than investing cash flows.

3.1.3 Statement of cash flows (continued)



C. Accounting policies

- We continued to challenge companies where accounting policies suggested that cash equivalents included amounts with an original maturity of greater than three months from the date of acquisition.[2]
- Borrowings can be included as a component of cash and cash equivalents only in very limited cases: where the balances are repayable on demand and often fluctuate from being positive to overdrawn. We identified instances where this requirement was overlooked (e.g. an invoice discounting facility, which did not fluctuate between a positive and negative balance was included as part of cash and cash equivalents.)

Even if borrowings can be classified as 'cash and cash equivalents' in the cash flow statement, the IAS 32 'Financial Instruments: Presentation' criteria for offset need to be applied to determine whether cash and borrowings can be presented on a net basis in the balance sheet. Please see section 3.1.6 Financial Instruments for further details.

D. Disclosures

- The nature of material supplier financing arrangements, their implications for the company's liquidity, and the relevant amounts were not always explained.
- Reconciliations of liabilities from financing activities[3] contained errors (e.g. derivative cash flows, classified as part of investing activities in the cash flow statement, were included in the reconciliation; leases were omitted; and movements did not reconcile to the amounts in the cash flow statement).
- Necessary explanations in relation to material cash flows were missing, such as the nature of the cash payments to non-controlling interests.
- Some disclosures required by IAS 7 were missing (e.g. disclosure of the amounts of the assets and liabilities, other than cash or cash equivalents, in the subsidiaries over which control is lost[4]).

2 IAS 7, paragraph 7
3 IAS 7, paragraph 44A
4 IAS 7, paragraph 40

3.1.4 Impairment of assets

Impairment of assets continues to be one of our areas of focus, especially in the light of the continuing uncertainty as a result of the Covid-19 pandemic. In most cases, our queries could have been avoided by clearer disclosures. We encourage companies to consider the guidance in our thematic Impairment of non-financial assets and the FRC Covid-19 Thematic Review[5] in preparing their impairment-related disclosures.

The FRC Climate Thematic – Reporting[6] explains that companies need also to consider the impact of climate change on companies' impairment reviews, especially in those industries where investors may reasonably expect climate changes to significantly affect future expected cash flows for particular assets or cash generating units (CGUs).

A. Key inputs and assumptions

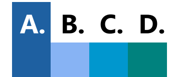
- We queried whether assumptions were consistent with past experience or external sources of information.
- In some cases, the strategic report identified uncertainties that suggested possible impairment of assets. However, it was not clear:
  - how the uncertainties had been addressed in the impairment reviews; or
  - whether they represented key sources of estimation uncertainty subject to IAS 1 disclosure requirements.
- We challenged companies where disclosures suggested that impairment testing was carried out using a post-tax discount rate (instead of pre-tax) and where the tax rate used was not explained.
- We queried significant reductions in discount rates where the reasons for this were not explained.

B. Impairment indicators and impairment testing method

- We queried whether climate change and the move to decarbonisation by carbon intensive companies were considered impairment indicators.
- In one instance, the recoverable amount of a CGU appeared to be compared with the carrying value of goodwill only, rather than with the carrying amount of the whole CGU, including goodwill.
- In several cases, value in use calculations appeared to include cash flows from enhancing the asset's performance, rather than being estimated for the asset in its current condition.
- The carrying value exceeded the value in use of a CGU, but no impairment was recognised and the reasons for this was not explained.
- In one company, it appeared that the goodwill impairment testing had been performed at a level higher than an operating segment, which is not permitted by IAS 36 'Impairment of Assets'.

5 Pages 44 to 48
6 Page 56

3.1.4 Impairment of assets (continued)



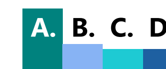
C. Investments in subsidiaries

- As in prior years, we continue to raise queries with those companies where there are impairment indicators (such as the net assets of the parent company exceeding the market capitalisation) and no disclosures in relation to the impairment review of the parent company's investments in subsidiaries are provided.
- In one instance, the discount rate used in the impairment review of the parent's investment in subsidiaries was lower than the rates used for impairment reviews at the consolidated level without explaining the reason for this.
- In another case, we queried the impairment test performed on a portfolio basis at the group level, rather than at the individual subsidiary level. As a result of our enquiry, a more detailed impairment review was carried out by the company, which confirmed that the parent's investments in subsidiaries were not impaired.

D. IAS 36 disclosures of sensitivity to key assumptions

- We asked whether reasonably possible changes in key assumptions could result in the recoverable amount of CGUs being less than their carrying amounts where this was unclear from the disclosures.
- We challenged the approach to sensitivity analysis where the impairments recognised during the year were significantly larger than those that would have arisen from reasonably possible changes in assumptions disclosed the year before and the reasons for this disconnect were not clear.

3.1.5 Alternative performance measures (APMs)



We expect UK companies to continue to apply the ESMA Guidelines on Alternative Performance Measures (the Guidelines) when preparing annual and interim reports following the UK's exit from the European Union. We consider that the Guidelines are consistent with the requirements of the Companies Act 2006 and codify best practice in supporting a strategic report that is fair, balanced and comprehensive.

The most frequent issues identified in our routine reviews this year related to reconciliations and calculations of APMs. We also challenged companies where undue prominence was given to such measures, the rationale for including or excluding certain items from the calculation of APMs was not clear, or there were issues with labels and definitions used. We also undertook a thematic review on APMs, the findings of which are summarised in section 4.1.3.

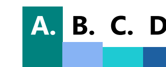
A. Reconciliations and calculations

- Reconciliations for some APMs to the most directly reconcilable line item, subtotal or total presented in the financial statements were missing. This tended to be for less frequently used items, such as net asset value per share and pre-tax return on equity.
- In some cases, reconciling items could not be identified directly in the financial statements and there was no reconciliation or calculation, to show how the figure was determined.
- Items in the reconciliations did not always agree to the corresponding amounts in the financial statements.
- The APMs were defined, but not reconciled, in the glossary, and we were unable to recalculate the numbers using the information in the financial statements.

B. Prominence

- In two cases, the APMs appeared to have been given more authority than measures directly stemming from financial statements (e.g. APMs were described as "a truer measure of performance" in one and as " better representing the economics [than the IFRS numbers]" in the other).
- We challenged the balance of APMs to IFRS measures in some cases (for example, where performance highlights in the annual report emphasised APMs and either did not comment on or gave insufficient prominence to the corresponding IFRS amounts).

3.1.5 Alternative performance measures (APMs) (continued)



C. Rationale and consistency of APMs

- In some cases, it was not clear why restructuring costs that recurred over a number of years were considered exceptional or non-recurring. We expect companies:
  - to explain why the costs are considered non-recurring;
  - not to use such labels for multi-year restructuring programmes with recurring costs; and
  - to reference multi-year programmes in each year affected and disclose information in relation to the costs to-date, total expected costs and timeframes.
- We queried the fluctuation in the tax rate on non-underlying items where the non-underlying items were substantially of the same type each year.

D. Labels and definitions

- One company's strategic report referred to 'Operating profit' in relation to the information presented on an IAS 17 'Leases' basis. IAS 17 had been superseded by IFRS 16 for the period in question and information provided in accordance with IAS 17 was, therefore, an APM and not IFRS operating profit.
- Another company reported measures called 'revenue' and 'net revenue'. It was not clear which measure was determined in accordance with IFRS 15 and which was an APM.
- Definitions of APMs (e.g. net asset value per share) were sometimes missing.
- One company labelled a measure as EBITDA but did not add back amortisation charges as implied by the label.
- Another company included the cash gain on the sale of a non-controlling interest, as well as full results of the same subsidiary for the year in the adjusted EBITDA, which was not clear from the definition provided for the measure.
- One company did not exclude a one-off tax benefit from adjusting items, which was inconsistent with the company's definition for such items.

3.1.6 Financial instruments

A. B. C. D.

Financial Instruments remains an area of focus in our routine reviews. The findings are those from our routine reviews and our thematic review on cash flows and liquidity disclosures.

We raised queries where it was not clear how specific transactions or financing arrangements were reflected in the financial statements, which factors management considered in developing an appropriate accounting policy, or where the disclosures did not fully explain the financial risks or mitigating actions. Factoring and reverse factoring arrangements remain an area on which users need transparent disclosures, covering the nature of any material arrangements, the liquidity implications and the relevant amounts.

A. Scope, recognition and measurement

- We queried the basis for one company's conclusion that its contractual arrangements fell into the scope of IFRS 15, rather than IFRS 9, which had significant implications for the measurement.
- We asked one company to explain how it had reflected the effect of significant changes in estimated interest cash flows on the measurement of liabilities at amortised cost, following a downgrade in credit rating. The company explained that, as the change was considered to represent a movement in the market rate of interest, the related liabilities were treated as floating rate instruments and the increased interest cost was accounted for prospectively.
- Accounting for the derecognition of a company's debt, including the extent to which it gave rise to any gain or loss, was not clear in another instance.
- We queried how balance sheet movements on derivatives related to the relevant gains and losses in the statement of comprehensive income.
- One entity had not disclosed its assessment of whether hedged forecast transactions were highly probable, no longer highly probable but still expected to occur, or no longer expected to occur. The consequential impact on hedge accounting was also not disclosed.

If significant judgement is required to determine the accounting standard under which a balance or transaction falls, or the appropriate measurement basis, we expect this to be explained.

These findings related to non-banking entities.

B. ECL provisions and credit risk

- Credit risk-related disclosures required by IFRS 7 were missing, including:
  - the inputs, assumptions and estimation techniques used to apply the IFRS 9 impairment requirements;
  - the gross carrying amounts of financial assets by credit risk rating grades;
  - information about the credit risk management practices, including the definitions of default and the reasons for selecting specific definitions; and
  - information about the concentration of credit risk.
- Information regarding the impairment assessment for financial assets other than trade receivables and contract assets was missing in a number of cases.

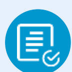
3.1.6 Financial instruments (continued)

A. B. C. D.

C. Other disclosures

- In some cases, annual reports referred to access to supplier financing arrangements, but the extent to which such arrangements were utilised was not clear.
- We wrote to companies that did not disclose their loan covenants and/or the performance against them, where this information appeared to be significant for the understanding of solvency and liquidity assessments (e.g. due to the material going concern uncertainties).

Some of the uncertainty caused by the pandemic has now abated. However, we continue to expect companies to provide additional information about their banking covenants unless the likelihood of any breach is considered remote.



Companies should provide disclosures that enable users to evaluate (paragraphs 1 and IG2 of IFRS 7):

- **the significance of financial instruments for its financial position and performance; and**
- **the nature and extent of risks arising from financial instruments to which the entity is exposed at the end of the reporting period.**

D. Offsetting

- In several cases, bank overdrafts or similar liabilities had been offset against cash and cash equivalents in the statement of financial position but it was not clear how the IAS 32 criteria for offset were met.

IAS 32[7] states that a financial asset and a financial liability should be offset when, and only when, an entity intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously. In March 2016, in relation to a specifically described cash-pooling arrangement, the IFRS Interpretations Committee concluded that the settlement of the entire period-end balance on a net basis is necessary to meet the requirement.

7 IAS 32, paragraph 42(b)

3.1.6 Financial instruments (continued)

Case Study[8]

Impairment of financial assets

The Group measures the loss allowance at an amount equal to lifetime expected credit losses for all trade receivables.

The disclosures explain that the simplification available under paragraph 5.5.15 of IFRS 9 has been applied to all trade receivables.

Intercompany receivables

Included in loans to subsidiary undertakings is an £85 million unsecured subordinated loan to TradeCo Limited. The loan was advanced on 27 September 2012, at a fixed rate of 9.5%, with a repayment date of 27 September 2032.

TradeCo Limited has cash and cash equivalents of £614.7 million and borrowings of £240.0 million. Based on its liquidity and expected cash generation, there has been no significant increase in credit risk and the expected 12 months credit loss for TradeCo Limited trade and other receivables is not considered to be significant. As a result, no impairment has been recorded for amounts owed by Group companies on the grounds of materiality.

Disclosure explains how ECLs have been assessed for intercompany receivables.

Receivables excluding trade receivables

The Group's credit risk is primarily attributable to its trade receivables and the risk of customer default. Credit risk also arises on accrued income, which primarily arises where services have been provided but the amount has yet to be invoiced on to the client. The accrued income balance is short term in nature, with an average ageing of 21 days, and relates to clients with a strong credit history. Therefore, the expected credit losses on receivables, other than trade receivables, were negligible.

The company confirmed that it considered impairment of receivables other than trade receivables, and provided specific detail in respect of the accrued income balance.

Concentrations of credit risk

The Group has no significant concentrations of credit risk. The trade receivables balance is spread across a large number of different customers with no single debtor representing more than 5% of the total balance due (last year: 6%).

The company provided a helpful indication that there is no significant concentration of credit risk to individual customers.

However, the Group's debtors include counterparties in sectors that have increased exposure to Government-imposed Covid-19 lockdown restrictions, which may increase the risk of non-payment. The proportions of the trade receivables balance relating to these sectors are: Retail 12%, Leisure 5%, and Office Space 18%.

The company highlights its credit exposure to certain sectors which may result in increased credit risk as a result of the economic impact of Covid-19.

8 The case study provides an example of better disclosure, annotated to explain what makes it better. It has been developed from our observations during the year, but does not represent any particular company's reporting.

3.1.7 Strategic report and the Companies Act

This year we raised fewer substantive queries in relation to strategic reports, which reflects companies' improved focus on this area following our significant attention over the past few years.

Our reviews of the strategic report consider an overarching requirement for the strategic report to provide a fair, balanced and comprehensive analysis of the development and performance of the business in the financial year and of its position at the end of the year. We encourage companies to refer to the FRC Guidance on the Strategic Report (the FRC Guidance), which includes principles that are relevant for the preparation of the annual report as a whole. In addition, entities need to consider the ESMA Guidelines on Alternative Performance Measures (the Guidelines). Section 3.1.5 provides more detail of our findings of companies' reporting against the principles of the Guidelines.

In 2020/21 we also issued the FRC Climate Thematic, which provides an overview of the narrative reporting requirements most affected by climate change, together with detailed findings from our reviews, our expectations and examples of better disclosures.

A. Fair, balanced and comprehensive

As in the prior year, we challenged companies where significant matters were not addressed in the financial review. For example:

- a material impairment loss on trade receivables was not mentioned in the report;
- a financial review commented on the growth of overseas revenue and profitability, but did not explain to what extent the growth rates had been affected by foreign currency movements; and
- cash generation was identified as a key strategic action, but only a brief discussion on the group's cash flow performance was included in the strategic report.

The strategic report has five main content-related objectives (the FRC Guidance, paragraph 4.3):

- **to provide insight into the entity's business model and its main strategy and objectives;**
- **to describe the principal risks the entity faces and how they might affect its future prospects;**
- **to provide relevant non-financial information;**
- **to provide an analysis of the entity's past performance; and**
- **to provide information to enable shareholders to assess how directors have had regard to stakeholders and other matters when performing their duty under section 172.[9]**

9 The FRC Guidance explains how to satisfy the requirement to produce a non-financial information statement (in paragraphs 7B.83 and 7B.84) and S172 statement (in section 8).

3.1.7 Strategic report and the Companies Act (continued)

B. Non-financial reporting (NFR)

There was scope for improvement in addressing climate change in Non-financial Reporting (NFR) disclosures:

- Some reports identified the existence of a relevant policy, for example, an environmental policy or a sustainability policy, but did not describe what it was.
- Cross-references were included to disclosures outside of the annual report, instead of including sufficient information to meet the legal requirements within the report itself.

C. Section 172 statement and stakeholder engagement

- Section 172 and stakeholder engagement disclosures were often combined, sometimes leading to the omissions of certain aspects of disclosure. This was particularly the case for those requirements that do not refer to engagement with stakeholders, such as the impact of the company's operations on the environment. Where the disclosures are combined, care is needed to ensure both sets of requirements are met.
- One company's press reports indicated that it had been discussing significant climate-related matters with investors, but this was not referred to in its stakeholder reporting.

Climate change and related disclosures will continue to be an area of focus for the CRR in its reviews. Page 9 of the thematic report summarises our expectations in relation to the narrative reporting in this area.

Where company law-related issues come to our attention, we will raise these with companies even when they are outside of our statutory powers. These include matters such as Companies House filing requirements and the lawfulness of distributions. We are pleased to note that companies generally respond constructively to these interventions.

D. Distributable profits

- We questioned whether the dividend receivable from a company's subsidiary met the criteria for qualifying consideration when determining the realised profits and distributable reserves of the parent company.
- We questioned the lawfulness of a company's distributions (dividends and share repurchases) that were not supported by the company's last audited accounts and where the required interim accounts had not been filed.[10]

E. Other Companies Act matters

- In one instance, the company did not prepare group accounts, but reference to the exemption taken was omitted from the individual accounts.
- In another instance, we questioned the basis on which the directors of a company concluded that group accounts, and strategic and directors' reports for the year were not required.
- We queried the steps taken by one public company to address the requirement of the Companies Act 2006 to call a general meeting when the net assets were half or less of its called-up share capital.[11]
- We queried the basis for an appointment of auditors, who were not a member of a recognised supervisory body in the UK.[12]

10 S830 and 836 of CA 2006
11 S656 of CA 2006
12 S1212 and 1217 of CA 2006

3.1.8 Provisions and contingencies

Provisions and contingencies remains one of our frequently raised topics. Most of our queries have been triggered by inconsistent or unclear information in the annual report and accounts.

Key findings of our reviews are set out below. Recognising the importance of the topic, we also conducted a thematic review as part of our 2021/22 monitoring, the findings of which are outlined in section 4.1.5.

A. Disclosures

- In some cases, queries were prompted by information in the annual report or elsewhere implying that there were unrecognised provisions or undisclosed contingent liabilities.
- We asked one company why possible litigation and regulatory enforcement actions that had been identified in its prospectus were not disclosed in its annual report and accounts.

Sometimes the determination of the probability of a cash outflow to settle the obligations (and accordingly whether a provision needs to be recognised or a contingent liability disclosed) requires a significant judgement. In such cases, the judgement and relevant assumptions should be disclosed.

B. Recognition and measurement

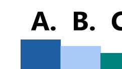
- We asked a company to explain the accounting treatment applied to claims recoverable from third parties (reimbursement assets) as this was not addressed by the accounting policies.
- We challenged companies where the reasons for changes in accounting policies, significant increases or exceptional releases of provisions were not explained.
- In one case, a professional indemnity provision and the related reimbursement asset were identified as an area of a significant accounting judgement and estimation uncertainty, but the amounts involved and accounting treatment adopted were not clear.
- Some companies had material provisions dependent on the future performance of part of the business expected to be heavily impacted by climate change (e.g. decommissioning provisions for fossil fuel assets). One company had not explained how climate change had been taken into account in estimating the amount of a provision.

Other aspects of the effects of climate change on the financial statements are considered in more detail in our Climate Thematic.

C. Presentation

- We challenged two companies that aggregated 'provisions' with 'trade and other payables', rather than presenting them separately.

3.1.9 Leases



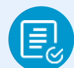
Our findings for 2020/21 reflect our focus on the initial application of IFRS 16 in both thematic and routine reviews.

Our main review findings are outlined below and explained in more detail in the thematic review report, which we encourage companies to read. We remind companies that all material transactions need to be covered by entity-specific accounting policies. We also draw the attention of both lessees and lessors to the overall disclosure objective of IFRS 16, which is to disclose information in the notes that, together with the information provided in the statement of financial position, statement of profit or loss and statement of cash flows, gives a basis for users to assess the effect of leases on the financial position, financial performance and cash flows.

A. Accounting policies

- The rationale for material transactions being outside the scope of IFRS 16 was not clear in some cases.
- Material accounting policies were sometimes missing or not clear (e.g. in relation to sale and leaseback transactions, lease incentives, items outside the scope of IFRS 16 and non-lease components).
- We queried reassessment of the lease term by one company shortly after the commencement of the lease, where the reasons for this were not explained.
- We queried another company's accounting for the acquisition of a property it had been leasing previously.
- Lessors sometimes failed to explain the basis for classifying their leases as operating or financing.

Please see section 3.1.3 for other observations in relation to the disclosure of changes in liabilities arising from financing activities.



Lessees and lessors [should] disclose information in the notes that … [enable] users to assess the effects of leases on the financial position, financial performance and cash flows… (paragraphs 51 and 89 of IFRS 16)

B. Disclosures

- Lessees with significant variable payment features (such as features linked to sales or inflation) did not always explain the nature and the potential accounting effect of those features.[13]
- In some cases, lease extension or termination options were identified as a significant judgement, but the required quantitative and qualitative disclosures about potential future cash outflows not recognised were not provided.
- Disclosures were sometimes inconsistent with the information provided elsewhere in the accounts.
- The maturity analysis of lease liabilities was sometimes insufficiently disaggregated (e.g. years 1 to 5 were treated as a single time band).
- Changes in the lease liability were sometimes inconsistent with the cash flow statement or finance cost disclosures.
- Other disclosures required by IFRS 16 were sometimes missing, such as the total annual cash flows relating to leases and any material commitments.

C. Transition

- Material aspects of transition to the new standard were not clear in some cases (e.g. significant transitional adjustments or significant reconciling items between the IAS 17 lease commitments and the IFRS 16 lease liability were not explained).

13 Paragraph B49 of IFRS 16 includes examples of the information that may need to be provided

3.1.10 Income taxes

This year we raised an increased number of queries on income taxes. Most of our queries were in relation to the nature of evidence supporting the recognition of deferred tax assets by loss-making entities in the light of the current economic environment and the related uncertainties faced by many entities. We remind companies that, where material deferred tax assets are recognised in such cases, the disclosure of significant accounting judgements and significant sources of estimation uncertainty will often also be required.

A. Recoverability of deferred tax assets (DTAs)

- There is scope for enhanced disclosure of the nature of evidence supporting recognition of deferred tax assets by loss-making entities where the utilisation of those assets depends on future profits.

In addition, all entities are required to disclose:[14]

- the amount (and expiry date, if any) of deductible temporary differences, unused tax losses or unused tax credits for which no deferred tax asset is recognised; and
- for each type of temporary difference and unused tax losses: the amount of deferred tax assets recognised and related movements in profit or loss.

In such circumstances, entities are required to disclose:[15]

- the amount of recognised deferred tax assets;
- the nature of evidence considered;
- critical judgements used in the recognition of DTAs (e.g. how the probability of recoverability of deferred tax assets was determined[16]); and
- the key sources of estimation uncertainty, including the carrying amounts affected and an explanation of the effect of any significant changes in key assumptions on the recovery of DTAs.

We also encourage companies to consider disclosing:[17]

- the identity of the taxable entity, its location and the applicable tax rules;
- negative, as well as positive, evidence considered; and
- the periods over which the DTAs are expected to be recovered.

14 Paragraphs 81 (e) and (g) of IAS 12 'Income Taxes'
15 Paragraph 82 of IAS 12 and paragraphs 122, 125 and 129 of IAS 1
16 Paragraph 36 of IAS 12 provides the relevant criteria in assessing the probability
17 Please see also paragraph 25 of the ESMA's public statement issued in July 2019, 'Considerations on recognition of deferred tax assets arising from the carry-forward of unused tax losses'

3.1.10 Income taxes (continued)

B. Tax reconciliation

- In a number of cases, we questioned explanations (or a lack thereof) for significant reconciling items affecting the relationship between income tax expense and accounting profit multiplied by the applicable tax rate (e.g. large one-off reconciling items not explained; incorrect explanations/descriptions in tax rate reconciliations).

C. Recognition of deferred tax assets and liabilities

- One entity had significant deferred tax liabilities in respect of accelerated capital allowances. However, there was no deferred tax asset recognised to offset the liabilities. We queried whether the company had considered the reversal of taxable temporary differences in assessing the probability of utilisation of the unused tax losses or tax credits.
- We queried the accounting for deferred tax on business combinations where the deferred tax effect of adjustments to recognise acquired assets was unclear.

D. Other IAS 12 issues

- The nature and/or the accounting treatment of significant temporary differences was not clear in some cases.
- We requested explanations of the basis for offsetting deferred tax assets and liabilities relating to different classes of temporary differences, where this was not addressed in the accounts.
- Significant judgements or key sources of estimation uncertainty were insufficiently explained in relation to the uncertain tax positions in some cases.
- We queried certain deferred tax amounts where there was a significant difference between the implied rate on the underlying item and the standard or effective rate of tax reported by the company.

We expect disclosures of significant judgements and key sources of estimation uncertainty to be sufficiently specific in the explanation of the judgements made, recognised amounts at risk and potential additional exposure to tax.

3.1.10 Income taxes (continued)

Case Study[18]

Deferred tax assets of £30m (2020: £28m) include £20m (2020: £26m) relating to the carry forward of unused tax losses. These arose predominantly in Subsidiary A, domiciled in country A (£10m), and Subsidiary B, domiciled in country B (£8m), which have a recent history of losses for tax purposes. However, due to the reasons set out below, the directors consider it probable that sufficient taxable profit will be available against which the unused tax losses can be utilised. Management expects these deferred tax assets to be utilised over a period of between five and seven years.

In the prior period, Subsidiary A reported a one-off loss due to the recognition of a provision for legal claims arising from a breach of health and safety regulations at Factory A. Management does not consider this event will affect the sustainability of future taxable profits in the jurisdiction.

The losses recorded by Subsidiary B in the current and previous period were due solely to losses suffered by division P as sales of product X diminished. Following the strategic decision to cease manufacture of product X, management is confident that this division will return to profitability on the basis of the historical profitability of the ongoing activities and previous forecasting accuracy.

In evaluating whether it is probable that taxable profits will be earned in future accounting periods, management derived their forecasts from the approved three-year budget and the forecasts used for the purposes of reviewing goodwill for impairment, updated for the effect of applicable tax laws and regulations relevant to those future taxable profits. No reasonably possible change in any of the key assumptions would result in a significant reduction in projected tax profits such that the recognised deferred tax asset would not be realised.

At the balance sheet date, the group had total tax losses arising in countries C and D of £21m (2020: £18m) for which no deferred tax asset is recognised because of the unpredictability of future taxable profits. These tax losses can be carried forward indefinitely.

Amount of deferred tax assets disclosed in respect of subsidiaries with a recent history of losses.

Periods over which deferred tax assets are expected to be utilised.

Explanation of the evidence supporting recognition of the deferred tax assets, despite the companies reporting a recent history of losses.

The company considers that there are no significant sources of estimation uncertainty.

18 The case study provides an example of better disclosure, annotated to explain what makes it better. It has been developed from our observations during the year, but does not represent any particular company's reporting.

3.2.1 Other issues: presentation of financial statements and related disclosures

Although the issues identified in the following slides have not made it in to our top ten in terms of their frequency, they have been recurring matters. Consequently, we consider it appropriate to remind companies that the relevant requirements of IAS 1 should not be overlooked during the year-end reporting process.

Presentation of primary statements

- We challenged companies where items of income and expense were inappropriately offset, line items in primary statements were duplicated or amounts did not reconcile with the information in the rest of the financial statements.
- We queried the aggregation of items on the face of the statement of financial position in some cases where the size, nature or function of the items indicated that separate presentation may be relevant (e.g. a significant landfill tax deposit included in other debtors).
- We queried the classification of assets and liabilities as current or non-current in a number of cases.
- We wrote to companies where material expected credit losses were not disclosed separately on the face of the income statement or the amounts separately disclosed did not reconcile to the notes.

The overall objective of the financial statements is to provide information about the financial position, financial performance and cash flows that is useful to users (paragraph 9 of IAS 1).

Where current/non-current classification of assets or liabilities requires a significant judgement, we expect this judgement to be disclosed.

Disclosures and other matters

- We raised queries where material transactions for the year were not covered by an accounting policy or the basis of measurement of a material item on initial recognition or subsequently was not explained.
- In several cases, it was not clear which standard was applied to particular transactions and whether the assessment of the scope of the relevant standard required a significant management judgement.
- Comparative information was missing for material amounts reported in the financial statements in one instance.

In addition, we remind companies that IAS 1 requires entities to:

- disclose information that is relevant for an understanding of the financial statements and, but is not presented elsewhere;[19] and
- not to obscure material information.[20]

Information may be obscured where material information is:

- disclosed, but the language used is vague or unclear;
- scattered throughout the financial statements;
- inappropriately aggregated / disaggregated; or
- hidden by immaterial information.

19 Paragraph 112 (c)
20 Revised definition of materiality applies for the annual periods beginning on or after 1 January 2020. Examples of information being obscured are provided in paragraph 7.

3.2.2 Other issues: climate change

In 2020, the FRC undertook a thematic review into how companies and auditors assess and report on the effects of climate change. The report incorporated findings from across the FRC's Regulatory Standards and Supervision divisions, as well as views from investors.

Key messages of 2020 Thematic

We found that, although reports usually comply with Companies Act requirements for narrative reporting on environmental matters, including climate change, most are not meeting investor needs. Moreover, some financial statements did not reference climate change, even when their narrative reporting implied that it might have a significant effect on key financial statement assumptions.

As a result of our review, we encouraged companies to:

- provide strategic reports that clearly describe their environmental policies, rather than simply naming or listing them;
- explain any terminology such as 'net zero' or 'Paris compliant' and provide transparent explanations about which emissions are included in any emissions targets, how progress will be measured and reported, and what assurance will be sought;
- give a balanced description of how climate policies and targets have been incorporated into business plans and their expected effect on the business, making appropriate use of key performance indicators, where relevant, and without disproportionate focus on 'good news' stories in parts of the business that are not material;
- describe the impact of their businesses, including their supply chains, on the environment;
- provide required segmental and disaggregated revenue disclosures to enable users to understand the relative sizes of operations for which climate change presents substantially different risks and opportunities; and
- provide financial statements that, where relevant, explain the effect of climate related risks, policies and strategies on both measurement and disclosure.

For example, the following considerations may be relevant:

- impairment of individual assets as well as cash generating units;
- useful economic lives of assets;
- expected amounts and timing of cash outflows for provisions and other liabilities;
- fair values of assets and liabilities; and
- disclosure of key accounting judgements, estimation uncertainties and related sensitivities.

3.2.2 **Other issues: climate change** (continued)

We continue to consider how well companies have met these expectations as part of our routine reviews. We have seen some improvements to disclosures, including some better explanations of net zero commitments and scenario testing, but there is still considerable scope for further enhancement.

Section 3.1.7 gives some examples of areas where we have challenged companies regarding environmental matters with respect to their Non-Financial Reporting, section 172 and stakeholder engagement reporting.

We have also challenged the disclosure of the effect of climate change on the financial statements.

Earlier this year, we published a thematic review of the application of the new Streamlined Energy and Carbon Reporting requirements. See section 4.1.4 for further details.

For accounting periods beginning on or after 1 January 2021, we will also review compliance with the Listing Rules requirement for premium listed companies to report in line with the Taskforce on Climate-related Financial Disclosures (TCFD guidelines) on a comply or explain basis. See section 5.2.3.

Some examples have included:

- querying why climate change is not considered to be an impairment indicator for assets in industry sectors most at risk;
- where impairment reviews have been carried out, asking for details of the effect of climate related risk on the underlying assumptions;
- seeking to understand the relationship between impairment assumptions and the company's strategic aims with respect to climate change;
- challenging the sensitivity of the company's goodwill impairment assessment to 'reasonably possible' climate change outcomes;
- questioning the effect of climate change on the useful economic lives and residual values of assets;
- querying the effect of climate-related uncertainties on the valuation of decommissioning and restoration provisions and the recoverability of deferred tax assets; and
- challenging the level of disaggregation of revenue and segmental disclosures where companies have distinct business operations, affected in substantially different ways by climate change, but provided no insight into the relative sizes of those operations (please see page 65 of our **Climate thematic** for further information).

4.1.1 Thematic reviews: interim reporting

This thematic review considered compliance with the requirements of the Disclosure Guidance and Transparency Rules and IAS 34 to identify areas of better practice or improvements. Our review consisted of a limited scope desktop review of the interim reports of entities listed on the main market of the London Stock Exchange, whose interim period ended between June 2020 and September 2020. The key findings from our review are summarised below:

- Overall, we were pleased with the quality of interim reports.
- Companies had heeded our recommendations from previous thematic reviews and other guidance, and enhanced their disclosures in relation to going concern and the statement of cash flows and related notes.
- Management commentaries provided an overview of the key events in the first half of the year and how these had affected operations and results. The best examples differentiated the effect that the various stages of the pandemic had on the financial statements.
- Where necessary, companies gave an update of the risks and uncertainties for the remaining six months of the financial year.
- The majority of the companies in our sample provided detailed explanations of their use of APMs and reconciliations to financial statement line items.
- Better disclosures on impairments included reasons for the impairments and quantified the key assumptions used in the impairment assessments.
- The best examples of changes in estimates disclosures included an update of the IAS 1 estimation uncertainty disclosures, where relevant, in addition to disclosing the nature and amount of the changes.
- Better disclosures of significant changes in tax balances included a breakdown of the components of the tax charge and the deferred tax balance by category of temporary difference.
- When an event or transaction is significant to an understanding of the changes in financial position and performance of the company since the last annual reporting period, better disclosures followed the disclosure guidance of individual IFRSs to provide updated relevant information.
- We expect companies to communicate material information clearly and concisely.

4.1.2 Thematic reviews: viability and going concern

This thematic review focused on assessing the quality of the viability and going concern disclosures for a selection of main market and AIM listed companies.

We identified several areas where viability and going concern reporting could be improved. We encourage preparers to consider carefully the findings of this thematic when preparing their forthcoming annual reports and accounts:

- The disclosures of inputs and assumptions used to support the viability and going concern assessments often lacked sufficient qualitative and quantitative detail to enable a reader to fully appreciate the scenarios that were considered and the stress testing that was performed. We encourage companies to include more granular qualitative and quantitative information of input and assumptions within their disclosures.
- All the companies in our sample that prepared a viability statement included a statement that the directors had a reasonable expectation that the company was viable over the period of assessment chosen. However, we identified several cases where conclusions did not clearly highlight the significant assumptions on which the viability statement was dependent.
- The most common viability period selected by companies was three years. We encourage companies to provide longer-term information and extend their period of assessment where possible. We do not expect the period of assessment to be shorter than the period covered by detailed budgets or forecasts (before extrapolations) approved by management and used in other forward-looking areas of the financial statements, such as deferred tax asset recoverability assessment or impairment testing.
- In some cases, information in the annual report and accounts indicated that significant judgement may have been applied in determining whether the company was a going concern or whether there was a material uncertainty, yet there was no disclosure, as required by accounting standards, of any significant judgement having been applied.
- There is opportunity for companies to cut clutter and duplication through the better use of specific cross-referencing between the viability statement, the going concern statement and other parts of the annual report and accounts.

4.1.3 Thematic reviews: alternative performance measures (APMs)

This thematic review assessed the quality of APM reporting in the UK, five years after the implementation of the European Securities and Markets Authority (ESMA) Guidelines on APMs (the 'ESMA Guidelines') and the introduction of the IOSCO statement on Non-GAAP Financial Measures (the 'IOSCO statement'). The review also followed on from our previous APM thematic review report, published in November 2017.

We found that, generally, companies provided good quality disclosures around their use of APMs. We saw companies providing more reconciliations of APMs to their IFRS or UK GAAP equivalents ('GAAP measures'). We also saw some improvement in the labelling of APMs and in their definitions. However, around half of the companies in our sample gave APMs more prominence or authority than GAAP measures in some areas of reporting. We expect companies to ensure that these supplementary measures are not displayed more prominently than GAAP measures and that their narrative reporting does not give them greater focus.

The companies in our sample used between 13 and 23 APMs, which is consistent with our experience that APMs are widely used by UK companies. As high levels of APM usage may obscure relevant GAAP information, companies should consider reducing the number of APMs disclosed, for example, by removing multiple variants of similar APMs and avoiding using APMs with only immaterial adjustments to IFRS measures.

We continue to find that companies adjust for more costs than income when calculating profit-based APMs. 19 of the 20 companies in our sample excluded more expenses than income from their APMs, with the result that they reported more favourable APMs than GAAP results. In six of these cases, the adjustments changed a GAAP loss into an adjusted profit. We remind companies to be even-handed in the treatment of gains and losses when classifying amounts as adjusting items. Companies should avoid practices that systematically present a more favourable view of their performance than would be obtained through the use of GAAP measures.

We were pleased that the companies sampled did not adopt APM reporting practices that we discouraged in our Covid-19 thematic review. For example, we did not identify companies that reported normalised or proforma results that excluded the estimated effect of the pandemic. With one exception, we did not identify any company that split its costs into Covid-19 and non-Covid-19 elements.

Many companies can still improve the quality and value added by their explanations for APMs and adjusting items by providing more granular information and, where relevant, by providing explanations at the level of individual APMs or adjusting items.

All the companies in the sample provided reconciliations for their most commonly used APMs. However, we identified examples where reconciliations of some APMs were omitted, the explanations of reconciling items could be improved, or the APM had not been reconciled to a GAAP number.

4.1.4 Thematic reviews: streamlined energy and carbon reporting

As part of the FRC's ongoing programme of work on climate change, we carried out a thematic review of emissions and energy use disclosures provided by a sample of quoted companies, large unquoted companies and limited liability partnerships under the new Streamlined Energy and Carbon Reporting (SECR) rules.

The principal findings of the thematic review are set out below.

- The entities in our sample largely complied with the minimum statutory disclosure requirements. However, more needs to be done to make these disclosures understandable and relevant for users.
- We identified challenges in this first year of reporting and identified a number of entity-specific errors and omissions:
- Reports did not always provide sufficient information about the methodologies used to calculate the emissions and energy use information. In particular, it was not always clear which entities were included in groups' SECR disclosures.
- More thought is needed about how to integrate these disclosures with narrative reporting on climate change and make them easier for users to navigate.
- It was sometimes unclear whether the intensity ratios selected were the most appropriate for the entities' operations. It was also not always possible to recalculate emissions ratios by reference to other disclosures in the report, for example, emissions per £m revenue.
- The extent of third-party assurance obtained over the SECR information was not adequately explained in most cases.
- Disclosures about energy efficiency measures did not always clearly describe the 'principal measures' taken by the entity in the current year.

We were pleased to see some examples of emerging good practice, including disclosure of Scope 3 emissions and information about emissions-reduction targets, 'net zero' strategies, or other emissions-reduction commitments. We were also encouraged to see many entities making progress towards reporting in a format consistent with the recommendations of the Taskforce for Climate-related Financial Disclosures.

4.1.5 Thematic reviews: provisions, contingent liabilities and contingent assets

Issues relating to compliance with IAS 37 have featured in the FRC's 'top ten' findings for several years. In this thematic we considered how effectively a sample of 20 companies met the disclosure requirements of IAS 37 and provided other relevant information.

We found numerous instances of good practice across each individual aspect of disclosure. However, there remains general scope for improvement in several areas despite CRR drawing attention to these matters in previous publications. These areas include: the disclosure of quantitative information on expected timing of future economic outflows, the key assumptions used to estimate those outflows, and the associated uncertainties. We also identified opportunities to clarify the nature of the costs included in certain types of provision, to disclose more specific accounting policies and to provide more quantitative information about contingent liabilities.

- Most companies explained provisions and contingencies in a brief paragraph, which was typically proportionate to the amounts concerned. Companies with more complex provisions gave more detail to aid the user's understanding. In some cases, extensive historical information was included that did not appear directly relevant to an understanding of the nature of the provision or contingent liability and made it difficult to get a clear and concise picture of the potential financial effects and uncertainties.
- Companies could improve the clarity of their description of the underlying obligating event, notably for restructuring, property-related and self-insurance provisions. We expect companies to consider the nature of provisions as well as their amounts when grouping them into classes. Classes should carry specific, informative labels.
- Companies rarely specified the method used to determine the best estimate. We expect companies to explain their approach – the 'expected value' or 'most likely outcome' method – where the most appropriate choice is not obvious. Where management had been unable to estimate the amount of probable or possible economic outflow, better disclosures explained why and provided 'order of magnitude' information.
- We expect companies to provide more information about the anticipated timing of outflows, particularly for longer-term provisions.
- A majority of companies identified provisions as a key source of estimation uncertainty. Most of these companies disclosed sensitivity information for changes in key assumptions. For longer-term provisions, this was most commonly provided for changes in the discount rate, which was identified as the factor more likely to materially affect the carrying amount. We expect companies to disclose how the discount rate is calculated where the effect of discounting is material. We also expect companies to explain material sensitivity to cash flow forecasting.
- Companies gave more limited quantitative information about contingent liabilities than we would expect, with a large minority using the 'not practicable' disclosure exemption for at least one contingent liability.
- We expect companies to explain significant movements in their provision balances or contingent liability exposures where this is important to provide a fair, balanced and comprehensive review of the development, performance and position of the business.

4.2 Financial Reporting Lab

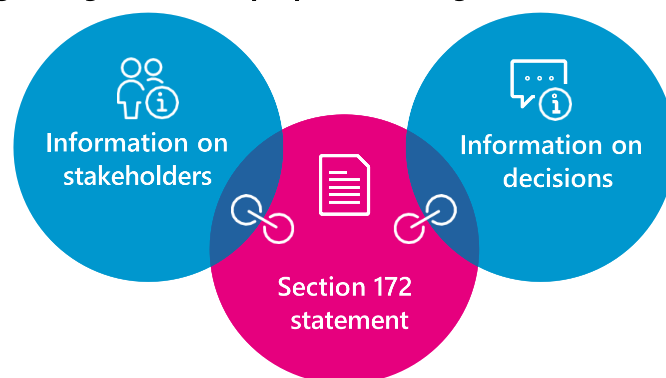
The work of the FRC's Financial Reporting Lab ('the Lab') has continued to focus on better practice reporting to meet the needs of investors. The Lab held many discussions with investors during their work on responding to Covid-19, emphasising the need for companies to enhance their disclosures around stakeholders and to clearly set out the risks and scenarios they have considered in response to Covid-19, with an eye to their longer-term resilience. The Lab's reports, set out below, provide some practical guidance on how to report more effectively in response.

Stakeholders, decisions and Section 172

With changes to the UK Corporate Governance Code and the requirement to include a Section 172 statement in strategic reports, there has recently been a greater focus on how companies are reporting on stakeholder-related matters. In response, the Lab carried out a project to consider the usefulness to investors of disclosures about stakeholders, including the Section 172 statement, across a range of reporting formats.

In late 2020, the Lab published a set of tips on Section 172 statements aimed at helping companies consider what content to include, how to present it and how to facilitate the process of preparing these statements. In July, the Lab published the final project report, which looks at reporting on stakeholders, decisions and Section 172. The report outlines what investors want to see from this reporting, finding that investors ultimately want to understand how a company is progressing towards fulfilling its purpose and achieving long-term success. Information on stakeholders and information on decisions can help with that understanding and Section 172 statements can act as a helpful bridge. The report poses a series of questions for companies and provides practical examples of corporate reporting considered to be better practice by investors.

Information that investors need in order to understand how a company is progressing towards its purpose and long-term success includes:



Risks, uncertainties, opportunities and scenarios

The Lab also carried out a project on risk to identify whether investor expectations are being met in relation to risks, uncertainties, opportunities and scenarios. The project report, published in September, highlights the information investors seek that will contribute to their understanding of a company's business model, longer-term strategy, resilience and viability. Many companies have evolved their internal processes and conversations around risks, uncertainties and opportunities (especially because of the Covid-19 pandemic), and these are becoming more integral to strategy and operations. However, there remains a gap between the information investors want and the disclosures that companies provide. The report includes practical examples of corporate reporting considered to be better practice by investors.

Structured electronic reporting

Companies admitted to trading on UK and EU regulated markets will need to prepare their annual financial report in a structured electronic format. The Financial Conduct Authority ('FCA') introduced this requirement (DTR 4.1.14) as part of the UK implementation of a cross-EU initiative known as 'ESEF' (European Single Electronic Format). Companies are required to prepare their annual financial reports in an electronic format (XHTML) and basic financial information should be tagged according to a taxonomy.

Given the pandemic, requirements for tagging annual reports and accounts were postponed to financial years starting on or after 1 January 2021 in the UK, so mandatory publication will commence from 1 January 2022.

Some companies have tagged their annual reports and accounts on a voluntary basis ahead of the mandatory requirement for this year's financial reports. The Lab published a report setting out some of the quality issues it had seen in the voluntary tagging. Companies will need to devote sufficient management and operational resource to ensure that they will be able to submit their December 2021 annual financial reports in the required format.

5.1 Key disclosure expectations for 2021/22

Our overall expectations for disclosures include:

... clear explanation of the significant judgements made by management, including those used in their assessment of going concern, with sufficient detail to understand the specific judgements made and their financial reporting effects.

... clear description of key assumptions underlying major sources of estimation uncertainty, including information about the sensitivity of amounts recognised in the financial statements to changes in assumptions.

... information in the financial statements to be consistent with that reported in the rest of the annual report and accounts.

... material climate change policies, risks and uncertainties to be discussed in narrative reporting and appropriately considered and disclosed in the financial statements, particularly where investors may reasonably expect a significant effect on the expected life or fair value of an asset or liability.

... the nature and extent of material risks arising from financial instruments and related risk management are adequately addressed, including: the use of factoring and reverse factoring in working capital financing; the approach to and significant assumptions made in the measurement of expected credit losses; concentrations of risks and information about covenants (where material).

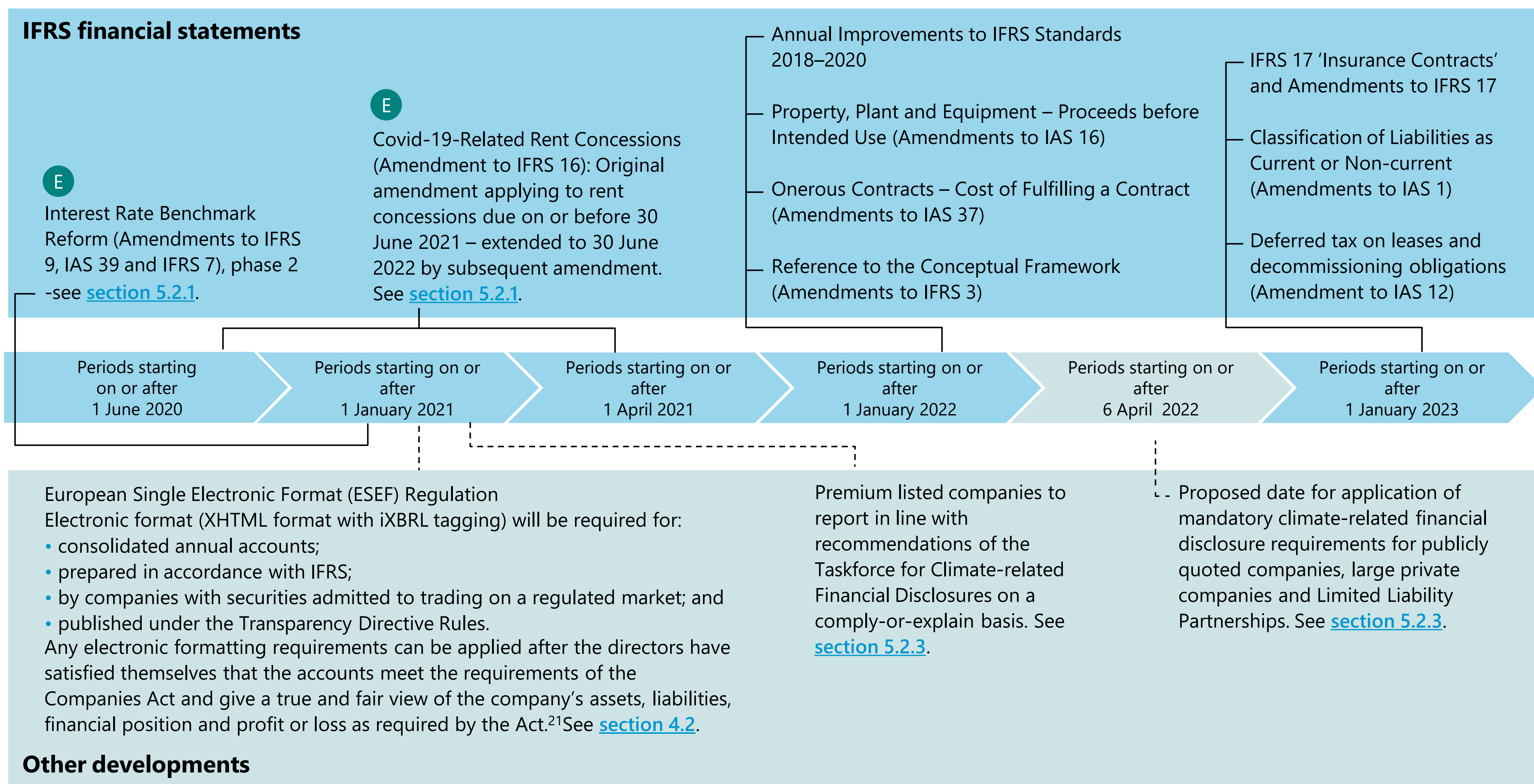
... APMs not to be given greater prominence or authority than amounts stemming from the financial statements and the basis for classifying amounts as adjusting, 'non-underlying' or 'non-core' explained.

... information that meets the disclosure objectives of the relevant accounting standards, as well as the specific disclosure requirements.

... material information that is not obscured by immaterial items.

5.2 Developments in corporate reporting

There are few changes in IFRS standards coming into effect in 2021-22, but a number of developments are in train for future years. Not all have yet been endorsed by the UK Endorsement Board (the UKEB). Companies should assess the relevance of these to their specific business and consider any systems or process changes needed to implement the new requirements.



Key: E indicates standards that have been endorsed by the UKEB at the date of this publication. However, please check the latest status[22]

21 Please see The UK government's position on the effect of the ESEF Regulation on the directors' sign-off of accounts of UK-incorporated users, June 2020
22 The status of the UK adoption is available on the UK Endorsement Board website: https://www.endorsement-board.uk/adoption-status-report

5.2.1 Developments in corporate reporting: IFRS

UK endorsement of IFRS

At the end of the Transition Period, SI 2019/685 brought the International Accounting Standards (IAS) already endorsed in the EU into UK law as 'UK-adopted international accounting standards'. During May 2021, the Secretary of State delegated certain IAS-related statutory functions to a newly-formed independent body, the UK Endorsement Board. Its statutory functions include adoption of any new or amended IFRS standards for use in the UK; and influencing the development of international financial reporting.

The UK Endorsement Board's Terms of Reference require that its technical decision making is independent of the FRC and other stakeholders in the market. The FRC is charged with oversight of the UK Endorsement Board's adherence to its due process, as well as providing operational support. At a high level, its process for adoption of a new or amended standard must comply with legislation and include the following:

- assessment of new IASB standards and amendments against the adoption criteria in the Regulations;
- gather evidence by consulting UK stakeholders, representative of those with an interest in the quality and availability of accounts, including users and preparers of accounts; and
- making the draft Endorsement Criteria Assessment available for public comment.

The input received informs the finalisation of the Endorsement Criteria Assessment before a formal adoption decision is made. The UK Endorsement Board will also publish a Feedback Statement summarising the main comments received and how they were incorporated into the final advice.

The transition from EU-adopted IAS to UK-adopted IAS will affect all UK companies that apply EU-adopted IAS in their consolidated or individual accounts.

- Entities with financial years beginning on or before 31 December 2020, but ending on or after that date, continue to apply EU-adopted IAS as at 31 December 2020 in their year-end financial statements. In addition, they have the option to early adopt any UK-adopted IAS.
- Entities with financial years beginning after 31 December 2020 apply UK-adopted IAS.
- Entities with financial years ending before 31 December 2020 but for which the end of the period for filing the accounts falls after that date continue to apply EU-adopted IAS as at 31 December 2020 and, in addition, have the option to early adopt any UK-adopted IAS.

Further information about UK endorsement is available on the Endorsement Board website.

UK Adoption status reports and the text of all UK-adopted IAS is also available on the UK Endorsement Board website.

During the year, the CRR Technical Director was appointed as the FRC's observer on the UKEB, which provides a conduit for issues identified by CRR regarding the application of extant IFRS standards, and potential issues relating to any proposed changes to IAS, to be fed into the UKEB activities. For any major proposed changes to IFRS standards there is usually also an opportunity to engage directly with the IASB staff, as part of their outreach activities.

5.2.1 Developments in corporate reporting: IFRS (continued)

The following Amendments have been endorsed by the UK Endorsement Board (UKEB) during the 2020/21 cycle.

Title of the Amendment	Effective for periods beginning	When endorsed by the UKEB?	Is early application permitted?
Interest Rate Benchmark Reform - Phase 2	On or after 1 January 2021	January 2021	Yes
Covid-19-Related Rent Concessions beyond 30 June 2021	On or after 1 April 2021	May 2021	Yes
Extension of the Temporary Exemption from Applying IFRS 9	Before 1 January 2023	January 2021	-

Interest Rate Benchmark Reform, phase 2

As explained on page 32 of **last year's CRR Annual Report**, Phase 2 affects all entities with a LIBOR-referenced contract. Phase 2 amendments address issues that might affect financial reporting during the reform of an interest rate benchmark, including the effects of changes to contractual cash flows or hedging relationships arising from the replacement of an interest rate benchmark with an alternative benchmark rate (replacement issues).

The Amendments affect financial instruments standards (IFRS 9, IAS 39[23] and IFRS 7), IFRS 4 'Insurance Contracts' and IFRS 16 and address:

- changes in the basis for determining contractual cash flows of financial assets, financial liabilities and lease liabilities;
- hedge accounting; and
- disclosures.

Covid-19 Related Rent Concessions beyond 30 June 2021

In March 2021, the IASB issued 'Covid-19-Related Rent Concessions beyond 30 June 2021 (Amendment to IFRS 16)'. The Amendment increases the eligibility period for the application of the practical expedient under the previous amendment issued in May 2020, from 30 June 2021 to 30 June 2022.

The Amendment provides a practical expedient that permits lessees not to assess whether rent concessions that occur as a direct consequence of the Covid-19 pandemic and meet specified conditions are lease modifications and, instead, to account for those rent concessions as if they were not lease modifications.

Where companies use this expedient, they should disclose this in the notes to their financial statements together with the amount recognised in profit or loss for the reporting period to reflect changes in lease payments that arise from rent concessions to which the expedient has been applied.

Extension of the Temporary Exemption from Applying IFRS 9

These Amendments for insurers defer the date of application of IFRS 17 and change the fixed date of the temporary exemption in IFRS 4 from applying IFRS 9, from 1 January 2021 to January 2023 (when specified criteria are met).

23 When entities continue to apply IAS 39 for hedging

5.2.2 Developments in corporate reporting: UK GAAP

Current amendments to FRS 100 to 105

Effective for accounting periods beginning on or after	1 January 2021

[UK exit from the European Union](#)
Amendments have been made to FRSs 100 to 105 for changes in legislation following the UK's exit from the European Union that came into effect at the end of the Transition Period. The Amendments were limited to those necessary to ensure consistency with UK company law and largely updated legal references and terminology used in the standards. Early application was permitted for UK entities in certain circumstances.

[Interest rate benchmark reform (Phase 2)](#)
Amendments have been made to FRS 102, providing relief in the accounting for financial instruments and hedge accounting, to avoid unnecessary disruption as agreements are modified in order to transition to alternative benchmark rates as interest rate benchmarks are being reformed.

[Covid-19-related rent concessions beyond 30 June 2021](#)
Amendments have been made to FRS 102 and FRS 105 which extend by one year the application of requirements originally introduced in October 2020 that cover the accounting treatment of temporary rent concessions occurring as a direct consequence of the Covid-19 pandemic. The requirements now apply to rent concessions that reduce lease payments originally due on or before 30 June 2022, provided the other conditions for applying the requirements are met.

[Going concern assessments in interim accounts](#)
Amendments have been made to FRS 104 clarifying the requirement to assess the going concern basis of accounting, and requiring the disclosure of any related material uncertainties, when preparing interim financial statements in accordance with FRS 104.

Available for financial statements approved on or after	21 May 2021

[Amendments to FRS 101 – 2020/21 cycle](#)
Amendments were made to FRS 101 predominantly to provide a disclosure exemption in relation to IAS 16 and maintain consistency with IAS 1.

Upcoming developments in UK GAAP

The next periodic review of UK and Republic of Ireland accounting standards is underway; a request for views to inform the review closed on 31 October 2021. Proposed changes to the standards will be subject to public consultation, and are currently expected to be effective for accounting periods beginning on or after 1 January 2024.

The review of FRS 101 – 2021/22 cycle is in progress.

5.2.3 Developments in corporate reporting: climate-related disclosures

Comply-or-explain TCFD reporting for listed companies

For accounting periods beginning on or after 1 January 2021, commercial companies with a UK premium listing must include a statement in their annual financial report setting out:

- whether they have made disclosures consistent with the recommendations of the Taskforce for Climate-related Financial Disclosures (TCFD) in their annual financial report;
- where they have included some, or all, of the disclosures in a document other than the annual financial report, an explanation of why and a reference to where the disclosures can be found; and
- where disclosures have not been made, an explanation of why, and a description of any steps taken or planned to be able to make consistent disclosures in the future – including relevant time frames.

The FCA has consulted on proposals to extend the application of the rule to issuers of standard listed equity shares (excluding standard listed investment entities and shell companies).

They also proposed to introduce climate-related disclosure requirements aligned with the TCFD's recommendations for:

- asset managers;
- life insurers; and
- FCA-regulated pension providers.

The consultations are now closed. The FCA will publish feedback and issue a Policy Statement once they have reviewed the consultation responses.

Mandatory climate-related financial disclosure requirements for publicly quoted companies, large private companies and Limited Liability Partnerships

The Department for Business, Energy & Industrial Strategy has consulted on proposals to mandate climate-related financial disclosures by publicly quoted companies, large private companies and Limited Liability Partnerships (LLPs). It is proposed that these requirements will apply to:

- all UK companies that are currently required to produce a non-financial information statement, being UK companies that have more than 500 employees and have transferable securities admitted to trading on a UK regulated market, banking companies or insurance companies (Relevant Public Interest Entities (PIEs));
- UK registered companies with securities admitted to AIM with more than 500 employees;
- UK registered companies, that are not included in the categories above, with more than 500 employees and a turnover of more than £500m; and
- LLPs with more than 500 employees and a turnover of more than £500m.

These entities will be required to disclose climate-related financial information in line with the four overarching pillars of the TCFD recommendations (Governance, Strategy, Risk Management, Metrics & Targets) on a mandatory basis.

It is proposed that regulations will be made by the end of 2021, coming into force on 6 April 2022, and applicable for accounting periods starting on or after that date.

6.1 How we perform our reviews

Stage	What we do
Review[24,25]	• We select companies based on a risk assessment from across the main market and AIM, with an additional selection on a rotational basis for the FTSE 350. A small number of other entities within our scope (such as large private companies and LLPs) are also selected for review. • We perform desktop reviews of published information. • In routine cases, CRR reviews all areas of the annual report that are within scope for the selected companies. • Full or targeted reviews are performed in response to complaints indicating a potential breach (please see section 6.2 for details). • Thematic reviews focus on areas of particular stakeholder interest, looking at just a single aspect of reporting in a selected sample of annual or interim reports where there may be room for improvement. Section 4.1 contains summaries of the 2021/22 thematic reviews.
Correspondence	• If there is a question as to whether there is, or may be, a breach of the relevant reporting requirements, CRR writes to the company to obtain sufficient information to determine whether there is in fact a breach or an opportunity for improvement. • Otherwise, we may highlight areas for improvement without asking for a substantive response.
Engagement	• Most companies with whom we engage want to do the 'right thing' and engage with CRR on a voluntary basis, with a view to improving their corporate reporting (please see Appendix II for a summary of best practice for responding to our queries). • We rarely have to invoke the FRC's statutory power, under the Companies Act 2006, to require companies, their officers or their auditors to provide any information and explanations required to carry out our function. • We did not use the power to obtain information in 2020/21, (2019/20: used the power once at the company's request). • We did not form a Review Group for any case in 2020/21 or in 2019/20. The Financial Reporting Review Panel was stood down in January 2021 when the revised FRC Corporate Reporting Operating Procedures were published. The Supervision Committee is now responsible for considering whether to invoke the FRC's statutory powers. See section 6.5.
Outcome	• Our enquiries may lead to the company volunteering or agreeing to correct numerical errors, restate comparative figures in subsequent accounts, or improve narrative disclosures. • For information on published case summaries and more significant outcomes in the period, see section 6.3. • We always follow up to ensure companies fulfil their undertakings to make specific improvements in subsequent reports.

24 Please see Appendix I for scope of our work.
25 For developments in our scale, transparency and scope of reviews, please see 'Transforming the FRC' (section 6.5).

6.2 Review activities for the year

Number of reviews for the year

We performed 246 reviews in 2020/21, which represents a 14% increase on the number performed in the prior year. The break-down by type of review is as follows:

	FTSE 100	FTSE 250	Other	Total
Full scope reviews[26]	26	50	39	**115**
Thematic reviews	45	56	30	**131**
	71	**106**	**69**	**246**

This compares to the prior year as follows:

	FTSE 100	FTSE 250	Other	Total
Full scope reviews[26]	19	52	40	**111**
Thematic reviews	38	35	32	**105**
	57	**87**	**72**	**216**

As in prior years, our focus continues to be on FTSE 350 companies:

	2020/21	2019/20	2018/19
FTSE 350, as percentage of total reviews	72%	67%	65%

A 'no issues' letter informs the company that we have performed a review and identified no issues of sufficient significance to draw to the company's attention. 'Appendix only' letters convey less significant matters where the company may not have complied with the relevant legal, accounting or reporting requirements or where there is opportunity for enhancing the general quality of reporting, but no substantive queries have been raised.

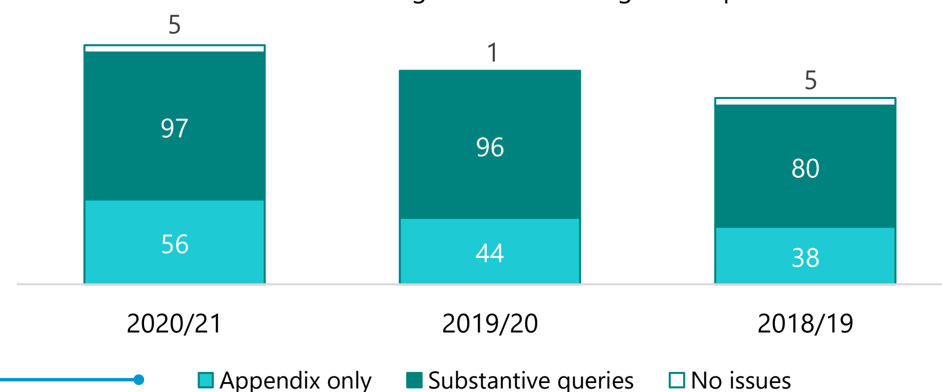
Complaints

A substantial amount of time is often absorbed considering complaints. We welcome complaints that are well informed and provide additional insight that may not be observable from a review of the accounts. All complaints about reports and accounts that are within our remit are reviewed by staff in the CRR team. If there is, or may be, a question of whether a report complies with relevant accounting or reporting requirements, we will write to the company seeking further information and explanations.[27]

	2020/21	2019/20	2018/19
Total number of complaints received	21	29	28
Approach made to company	11	19	18

Queries raised with companies

We wrote to 97 companies with substantive queries for which a response was sought (2019/20: 96; 2018/19: 80). This represents a 'write-rate' of 39% (2019/20: 44%; 2018/19: 39%). The reduction in the rate reflects an increase in the proportion of thematic reviews performed during the year. However, we consider each case on its own merits and do not have a target rate for writing to companies.



26 Includes 11 complaints in 2020/21 (19 complaints in 2019/20)
27 Further information on how we address complaints and referrals is available on our website. Further information in relation to the complains received during the year is available on page 35 of the FRC Annual Report and Accounts.

6.2 Review activities for the year (continued)

Response times

Companies are asked to respond to our initial letters within 28 days, so that potential matters are addressed promptly. Reasonable requests for extensions are granted; we would always prefer companies to take more time where necessary to produce a high quality, well-considered response that has been discussed with the auditors. Considerable time can be wasted if an initial response is subsequently found to be inaccurate or incomplete. Appendix A.2 summarises best practice for responding to our queries.

We aim to respond to companies' letters within 28 days, although the response time may be higher on more complex cases.

Companies' average response time: 32 days (2019/20: 32 days)

FRC average response time: 25 days (2019/20: 25 days)

Cases completed

We aim to close our correspondence with companies in time for agreed improvements to be reflected in their next annual report and accounts, ensuring that better quality information is in the public domain at the earliest opportunity.

97% of 2020/21 reviews were completed by the date of this publication (2019/20: 97%; 2017/18: 96%).

94% of these completed cases (2019/20: 94%; 2018/19: 93%) were completed before the next annual report and accounts was due for publication.

Working with other parts of the FRC

Where scheduling and considerations of legal privilege allow, we work with colleagues from the FRC's Audit Quality Review team (AQR) to identify and consider matters relevant to our reviews. In addition, we accept referrals from AQR when accounting issues are identified from its audit reviews.

During the year, we also undertook a pilot with our Corporate Governance and Stewardship team (CG&S) as part of our response to the government's consultation into restoring trust in audit and corporate governance. This consisted of our colleagues from CG&S reviewing corporate governance disclosures of a selection of companies against the requirements of the 2018 UK Corporate Governance Code (the Code) in parallel with our review of the companies' corporate reporting. In an appendix to our letters, we drew companies' attention to any areas of potential improvement in their corporate governance statements. We were pleased to note that a high proportion of companies responded satisfactorily to the matters raised. We are repeating the exercise in 2021/22 with a larger sample size.

Working with other regulators

Regular meetings are held between the FRC and the Financial Conduct Authority (the FCA) to share the outcome of our work on regulated companies and discuss ongoing matters of joint interest. Where the work relates to interim reporting or the reports of non-UK companies, our findings are passed to the FCA under the Companies (Audit, Investigations and Community Enterprise) Act 2004 for further consideration. The FCA may refer corporate reporting matters to the FRC when it is best suited to investigate further.

We liaise with the Prudential Regulation Authority (the PRA) on matters of mutual interest regarding financial institutions and may share information, e.g. on complaints that affect both corporate and prudential reporting.

The FRC, together with the PRA and FCA, sponsors the Taskforce on Disclosures about Expected Credit Losses (DECL) to build on the existing credit risk disclosures in IFRS 7 and develop further guidance on high quality disclosures by banks.

We discuss developments in corporate reporting with HM Revenue and Customs (HMRC) and it may refer matters within our regulatory scope to us.

We may co-operate with the US Securities and Exchanges Commission (the SEC) in relation to entities with dual UK and US listing when, amongst other things, the FRC staff view on an IFRS matter could result in a significant change to the issuer's financial statements.

6.3 Publication of CRR interaction

Case summaries

The Government's consultation 'Restoring trust in audit and corporate governance', issued this year, contained a proposal to give the FRC a statutory power to publish a summary of the findings of its individual reviews of company reports and accounts.

As an interim step towards greater transparency of its corporate reporting review function, since March 2021, the FRC has published summaries of its findings of recently closed cases that resulted in substantive enquiries.

As, currently, we are subject to existing legal restrictions on disclosing confidential information received from companies, the summaries can only be disclosed with the consent of the relevant companies.

So far, only two companies have not consented to the publication of their case summaries.

We also list the names of those companies whose reports and accounts we have recently reviewed without raising a substantive enquiry. As, in these cases, there are no matters to summarise, consent is not sought.

Company names

We publish the names of those companies whose reports and accounts have been reviewed on our website, once the company has issued its next set.

6.3 Publication of CRR interaction (continued)

Required references

In some cases, we may ask a company to refer to its discussions with us in the report and accounts in which it makes a change to a significant aspect of its reporting following our enquiries.

Such references may relate to a material error affecting the primary statements, an omission of disclosure with a material impact, or multiple omissions of relevant information or the provision of poor quality information.

The 15 required references this year are outlined below. Information in this section has been anonymised where the company concerned has not yet published its annual report and accounts.

	2020/21	2019/20	2018/19
Number of required references	15	14	11

Cash flow statements

Errors relating to cash flow statements remained the most common reason for required references in 2020/21.

IWG plc restated its cash flow statement as follows:

- Interest payments on lease liabilities were reclassified from financing to operating activities. This brought the treatment of interest payments in line with the company's existing policy.
- Cash flows in relation to lease incentives were restated to ensure gross presentation. The amounts received in respect of the lease incentives were previously netted off against lease repayments, which is not permitted under IAS 7.[28]

City of London Investment Group plc restated comparative amounts in its cash flow statement to reclassify acquisition-related costs as operating rather than investing cash flows.

Anexo Group plc made the following restatements:

- An invoice discounting facility, which was always in a liability position, was removed from cash and cash equivalents in the cash flow statement. This is because borrowings are generally considered financing, unless the balance fluctuates from being positive to negative.[29]
- The non-cash acquisition of assets on new leases was removed from the cash flow statement. The company previously presented assets obtained on hire purchase as an inflow of cash within financing activities and an outflow of cash within investing activities.

Intermediate Capital Group PLC restated its parent company cash flow statement to reclassify certain intercompany cash flows between financing and investing activities and to present on a gross basis a number of cash flows originally presented net.

Hilton Food Group plc restated its parent company cash flow statement to reclassify the cash outflow on the issue of an intercompany loan as an investing activity, rather than financing.

Wizz Air Holdings Plc revised its accounting policy for cash and cash equivalents to ensure that only deposits that are short term, highly liquid and subject to insignificant changes in value, and that are being held for the purpose of meeting short-term cash commitments, are classified as cash equivalents. The change in accounting policy resulted in a prior year reclassification of deposits with an original maturity of more than three months from cash and cash equivalents to other assets. The company also restated its cash flow statement to show amounts that did not meet the revised accounting policy definition of cash and cash equivalents as a cash outflow from investing activities.

PZ Cussons plc restated its cash flow statement to show the proceeds of the disposal of a business within investing activities (previously it was presented within operating activities).

28 IAS 7, paragraph 22
29 IAS 7, paragraph 8

6.3 Publication of CRR interaction (continued)

Kier Group plc reclassified loan repayments from joint ventures to investing activities rather than financing.

Presentation of financial statements

Great Portland Estates plc restated its income statement to remove the duplication of line items and to present line items on a gross basis without offsetting.

Telecom Plus Plc restated its statement of comprehensive income to show an expected credit loss impairment charge on the face of the statement.[30]

Intermediate Capital Group PLC made the following restatements:

- The group statement of changes in equity was restated to correct the amounts reported on net settlement of PAYE liabilities upon exercise of share options.
- The parent company balance sheet was restated to reclassify certain amounts receivable from group undertakings as non-current to reflect the period over which they were expected to be repaid, as required by IAS 1.[31]

St James House PLC restated its income statement and current liabilities to include a charge for legal costs, which was settled in shares after the year-end for the year. No accrual for the expense had previously been made as at the year-end.

Financial instruments: presentation

Oxford Instruments plc revised the net presentation of positive bank balances and overdrafts held under a group cash-pooling arrangements. While the group had a legally enforceable right to offset these balances, it could not demonstrate an intention to settle them on a net basis, which is another criterion for offset under IAS 32.[32] The company restated its financial statements to present the balances on a gross basis.

Financial instruments: classification and measurement

St James House PLC reclassified a financial asset from amortised cost to fair value through profit or loss, to take account of variability in the amount and timing of cash flows receivable. The carrying amounts of the asset at inception and the period end were also restated as a result of applying a higher discount rate that better represented the risk profile of the counterparty. The company also enhanced its disclosure of the assumptions used by management.

Revenue recognition

Co-operative Group Limited agreed to change its revenue recognition policy in relation to its prepaid funeral plans. Previously, the company treated the proceeds from whole-of-life insurance policies, in which payments from customers were invested, as variable consideration from contracts with customers. The company also treated fair value gains and losses on revaluing these insurance policies as changes to deferred revenue; that is, on the balance sheet rather than in the income statement. The company now treats the amounts initially received from customers as revenue, in accordance with IFRS 15. As these amounts are received in advance of the performance of the funeral, it defers the revenue and increases this liability by recognising an effective interest charge in the income statement until the plan is redeemed. Under the revised policy it recognises fair value movements on life insurance policies in the income statement in accordance with IFRS 9.

Eden Research plc revisited the principal versus agent considerations of IFRS 15 in relation to its sales to an associate. As a result, the company restated its financial statements to replace the gross presentation of sales and cost of sales with the relevant margin only.

30 IAS 1, paragraph 82(ba)
31 IAS 1, paragraph 66
32 IAS 32, paragraph 42(b) and IFRIC March 2016 Agenda decision

6.3 Publication of CRR interaction (continued)

Consolidation

Co-operative Group Limited concluded that it had neither power over, nor exposure or rights to, variable returns from the Reclaim Fund and agreed to deconsolidate it.

Discontinued operations

PZ Cussons plc excluded a gain made on disposal of a business from the results of the discontinued operations in the income statement, contrary to the requirements of IFRS 5 'Non-current assets held for sale and discontinued operations'.

Earnings per share (EPS)

Mothercare plc revised its disclosure of diluted EPS. IAS 33 requires potential ordinary shares to be treated as dilutive when their conversion would decrease earnings per share or increase loss per share from continuing operations. The company made a profit from discontinued operations and an overall profit for the year but made a loss from continuing operations. In this situation, the standard requires the loss from continuing operations to be used as the control number to establish whether potential ordinary shares are dilutive or antidilutive. Therefore, in this case, the diluted EPS reported should have been the same as the basic EPS, as the potential ordinary shares were antidilutive.

St James House PLC restated its EPS to correct its calculation of earnings from continuing operations and to reflect the impact of a post-year-end share consolidation on its EPS calculations.

APMs

PZ Cussons plc restated its EBITDA to add back amortisation charges.

Press Notices

At the conclusion of our most significant cases, we may issue a press notice in order to bring the matter to the attention of a wider audience.

This is usually restricted to those cases where there is a particularly material change, such as to a primary statement or the content of the strategic report.

	2020/21	2019/20	2018/19
Number of Press Notices issued	-	1	-

6.4 Post-review survey

CRR aims for continuous improvement not only in corporate reporting but also in its own practices. In accordance with the Regulators' Code (2014), we seek to provide simple and straightforward ways to engage with those we regulate and to hear their views.

CRR collects anonymous feedback from company directors and key staff on their experience of an enquiry through an online survey. The requested feedback covers the majority of the reviews completed in 2020/21 that led to substantive questions being raised. From 2021/22 we will also send surveys to recipients of 'appendix only' letters (see section 6.2).

The anonymised responses indicated that we have received views representing a wide range of companies and roles.

We ask the Chairman, CFO, Audit Committee Chair, and anyone else with primary responsibility for responding to our letters three questions:[33]

- Did you consider the matters raised to be clear and understandable?

2020/21: Yes - 100%

2019/20: Yes - 98%

- Were the matters raised in our review relevant to your company?

2020/21: Yes - 100%

2019/20: Yes - 95%

- Were the outcomes of our review proportionate?

2020/21: Yes - 98%

2019/20: Yes - 95%

We also ask for respondents' views about the usefulness of our annual publications.

The responses show that our main publications – the Annual Review, thematic reviews, and the FRC Key matters document (previously known as 'FRC year-end advice letter') – are well received, with 90% (2019/20: 84%) rating them as 'very' or 'somewhat' useful.

We invite comments on the survey questions and consider them carefully alongside the standard responses. Where respondents choose to identify themselves, we may engage with them to better understand their views and identify potential improvements to our processes and approach.

We continue to focus on the timing of correspondence, aiming to write to companies well before the next balance sheet date, so as to allow sufficient time for incorporating changes in the next accounts.

33 Results are from responses received to 31 March 2021

6.5 Transforming the FRC

In March 2021, the Department for Business, Energy and Industrial Strategy (BEIS) issued the consultation 'Restoring Trust in Audit and Corporate Governance', which included proposals to transform the FRC into a new regulator, the Audit, Reporting and Governance Authority (ARGA). The consultation period is now closed. Several of these proposals increase the scope and powers of the FRC's CRR function and are based primarily on the recommendations of Sir John Kingman's "Independent Review of the Financing Reporting Council" in 2018.

Where primary legislation has not been necessary to implement the recommendations, the FRC has taken interim steps to make the necessary changes. The table below explains the changes already made and those that are proposed in the consultation document and are pending legislative changes.

Changes implemented so far	Future changes proposed
The FRC implemented a new, streamlined governance structure in January 2021. The Supervision Committee is responsible for overseeing the FRC's delegated statutory supervisory and oversight functions, which includes CRR. This includes consideration of any potential decision to apply to court for a direction that a company's accounts are defective and should be amended. An FRC-wide Advisory Panel has also been constituted. These arrangements were introduced following the standing-down of the Financial Reporting Review Panel.	The consultation proposes giving the regulator the power to direct companies to make changes to their report and accounts without having to apply for a court order.
CRR has started publishing case summaries each quarter, setting out the principal findings from its completed reviews and the outcome of its engagement with companies. Pending a change in law, it must contact each company in advance to obtain consent for publication.	The consultation proposes amending the current statutory restrictions to allow CRR to publish case summaries without the relevant company's consent, subject to commercial confidentiality considerations.
CRR is in the second year of a pilot scheme to raise matters on areas outside its current statutory enforcement powers. Where appropriate, we are drawing companies' attention to potential opportunities for improvement in areas such as reporting against the UK Corporate Governance Code.	The consultation proposes giving the regulator expanded statutory powers to obtain information and explanations, and direct changes to all parts of an annual review and accounts, including those currently out of scope.
For a risk-based sample of 2020/21 cases, CRR reviewed the preliminary announcements of full-year results and the related presentation of information to investors and analysts, to identify any material inconsistency with disclosures in the annual report and accounts. The findings of this work have been shared with the FCA and are informing whether further powers are necessary in this area.	The consultation proposes giving ARGA the power to request an expert review of aspects of a company's corporate reporting. This may be necessary where the regulator has not been able to obtain the information or explanations it requires directly from a company or its auditors.

"The improved capacity, capability and processes that we delivered in 2020/21 have moved us towards becoming the fit-for-purpose regulator that Kingman envisaged and provides a firm foundation on which to build further. We need to continue to build our resilience, provide quality standards, supervision and support to stakeholders and the regulated community, and to increase the pace of change to deliver on the package of reforms that Government has put forward in its White Paper."

Sir Jon Thomson,
Chief Executive,
FRC Annual Report 2021

Appendix I: Scope of CRR's work

CRR is responsible for reviewing parts of the annual reports of public and large private UK companies, as well as some public overseas companies that prepare their accounts under IFRS or UK GAAP. We are also responsible for monitoring interim reports of entities with securities listed on a regulated market.

CRR Operating Procedures can be found on the FRC website.

CRR's statutory function is assessing compliance with legal requirements and relevant accounting standards in:

- the strategic report, including the Section 172 statement and non-financial information statement;
- the directors' report; and
- the annual accounts (financial statements).

CRR focuses on the quality of reporting, often suggesting ways in which a company could improve communication with investors. This is consistent with its philosophy of continuous improvement. Our 2020/21 review cycle considered annual reports and accounts of companies with year-ends ranging from May 2019 to October 2020.

We recognise that others with more detailed understanding of a company's business – auditors and audit committees – may also have recommendations for future improvement. We encourage companies to consider these.

Please see section 6.5 for possible future changes in our scope.

Appendix II: How to deal with a CRR query

Company responses to our letters

We are often asked how companies should deal with a letter from us that requests additional information and explanations. In our experience, the good practices that tend to result in earlier closure of the matters under review include:

A response letter that ...

- ❑ clearly identifies the question that is being answered
- ❑ addresses all questions included in the main body of our letter (substantive questions)
- ❑ clearly states if the issue at hand is not material and why
- ❑ raises our understanding of the issue to the level of management
- ❑ explains fully the Board's judgements and how they comply with the financial reporting requirements
- ❑ candidly addresses the issues raised and that:
    - ❑ clearly addresses the issue – vague responses only prompt further questions
    - ❑ admits a deficiency in reporting and suggests a way of putting it right
    - ❑ doesn't argue a lost cause
    - ❑ volunteers other helpful explanations to aid our understanding
- ❑ is clear to what extent the board, audit committee and auditors have been involved

It is also helpful to:

- acknowledge receipt;
- use email, rather than post;
- call us if you don't understand the question;
- be realistic about the timing – a 28 day turnaround is expected, but we would always prefer companies to take more time where necessary to produce a high quality, well-considered response;
- engage with the auditors and the audit committee at an early stage; and
- review relevant discussions, decisions and documentation to help inform the response.

Financial
Reporting Council
8th Floor
125 London Wall
London EC2Y 5AS

+44 (0)20 7492 2300
www.frc.org.uk