

Making tomorrow a better place (strapline for Carillion plc's annual report)

by Peter Parry

In the last edition of TPI Malcolm Howard wrote about the recent debacle at Carillion. [There is more from Malcolm elsewhere in this issue, Ed.] The Annual Report and Accounts for 2016 was published in April with upbeat statements from the Chairman and directors only to be followed about two months later with an admission that, thanks to problems with a number of major contracts, the company was in dire financial straits. The share price crashed from over 190p to 57p. Malcolm's article questioned, amongst other things, what the auditors were doing at Carillion.



An UKSA member also asked whether the Policy team had made any representations to the FRC about Carillion and the failure of the auditors to raise concerns about some of the Company's major contracts. It is a pertinent question which has prompted me to summarise some of the work that the Policy team has been doing recently on financial reporting.

As far as the Carillion issue is concerned, we have not written to the FRC about it. The reason is that UKSA's relationship with the FRC is such that we are now working closely and regularly with the Regulator on a number of projects which address some of the wider issues surrounding reporting standards, investor information requirements and audit quality. Carillion has been discussed specifically in the context of at least two of these projects.

The Board and the Policy team have actively sought to build a closer working relationship with the FRC. This has included engaging in several Reporting Lab and other projects. Three recent and highly relevant examples are:

- **The FRC's project on Risk and Viability reporting:** Members had an opportunity to respond to an FRC survey in June canvassing their views on this topic. This was followed by interviews with investors (UKSA included) and a series of round table discussions with the FRC. Carillion was discussed quite extensively at the round table meetings. All present expressed concerns about the fact that only a month or two after Carillion had published an upbeat outlook in its annual report serious problems emerged which threatened the very viability of the Company. The Risk and Viability project is ongoing and we shall see what changes the FRC proposes on standards of reporting in this area. There will, however, be feedback on the membership survey at the event that the FRC is running for us at their offices on 21st November.
- **The FRC's consultation on its revised Guidance on the drafting of the Strategic Report:** A copy of the joint response from UKSA and ShareSoc to the consultation can be found on the UKSA website (<https://tinyurl.com/y8edm5av>). In Sections 7.24 and Appendix IV of the Guidance we referred specifically to the Carillion situation. It is worth mentioning that the FRC's update to its Guidance on the strategic report is essentially 'tweaking' to ensure that strategic reporting complies with the requirements of the Shareholder Rights Directive. The exercise has, however, opened a can of worms and has served to highlight the shambles that much strategic reporting represents. Information is scattered around in statements from the Chairman, the CEO, the CFO, and reports on the business model, the business strategy, sustainability issues and an analysis of key risks. Why can't we replace this often unhelpful, incoherent and repetitive jumble with something more like Warren Buffett's 'Letter to Investors'?

- **The Consultation by the FRC in June this year on its enforcement procedures and sanctions:** UKSA and ShareSoc responded comprehensively to this. A copy of the response and our covering letter can be accessed at <https://tinyurl.com/y8srqkyp>. Suffice it to say that we were not impressed by sanctions that relied on levying fines on auditors. Even quite large fines can represent small change for the major audit firms.

While the Board is keen to build a good relationship with the Regulator and contribute fully to the work that it does, we are aiming to build a relationship which is based on objectivity and constructive feedback. Sometimes that feedback needs to be critical. UKSA was a signatory to a recent position paper drafted by Natasha Landell-Mills at Sarasin and Partners. The paper expresses the serious concerns and reservations that we have about the funding and staffing of the FRC and the scope that this creates for 'regulatory capture'. Although the position paper (a form of open letter) does not pull its punches, we had no hesitation in signing up to it. The letter can be accessed via the UKSA website at <https://tinyurl.com/ybpw4awl>. The FRC strongly refuted the concerns expressed in the position paper at a meeting on 11th October. However, in a speech on 25th October, Stephen Haddrill (CEO of the FRC) struck a more contrite note, admitting that while corporate reporting standards had improved recently, they were still not as good as they could be. One would like to think that the tone and some of the content of this speech reflect the move by UKSA and other investors to hold the FRC to account. A transcript of the speech has been published on the FRC's website (<https://tinyurl.com/yah4rfge>).

The FRC held an event for UKSA and ShareSoc members on 21st November. This provided an excellent opportunity for members to raise questions about standards of reporting and auditing directly with the Regulator.

We are not aiming to 'make tomorrow a better place' – a mind-numbingly silly, arrogant and meaningless statement on the part of Carillion's board which in itself tells us quite a lot about the Company's culture. However, we are trying to work with the FRC and other investors to try and ensure that all investors enjoy better standards of financial reporting and auditing than they do today.



UKSA and ShareSoc have just taken part in an event at the Financial Reporting Council in London entitled 'Lifting the Lid on the FRC'.

This was the first time that the FRC had presented to individual shareholders.

Around 50 UKSA and ShareSoc members attended the event and took part in lively exchanges, including some robust questioning. It was hailed a success by shareholders and the FRC alike. A full report will appear in the next TPI.