

Thematic Review - Alternative performance measures (“APMs”)

The FRC will conduct a second thematic review into the use of APMs in annual reports and accounts, following on from its review into their use in interim statements for periods ended 30 June 2016, published in November 2016. The second review will focus on those matters which gave cause for concern in the earlier review and also those issues which were noted in the ‘Annual Review of Corporate Reporting 2015/2016’ (“the Annual Review”), published in October 2016, especially but not exclusively in the context of companies’ strategic reports.

As in the earlier study, the new review will also aim to establish the extent to which the reports and accounts are consistent with the ‘Guidelines on Alternative Performance Measures’ (“the Guidelines”) issued by the European Securities and Markets Authority (“ESMA”). Listed companies are required to make every effort to comply with the Guidelines which apply to all regulated information, including annual reports, published after 3 July 2016. In its reviews of reports and accounts, the FRC takes into account any material inconsistencies with the Guidelines when deciding whether to question if strategic reports are fair, balanced and comprehensive.

The FRC has identified the following specific areas where improvements can be made. It expects:

- Good explanations to be given supporting the use of particular APMs; that is, why an APM is useful, helpful or more meaningful rather than simply asserting that this is the case or that it is used internally.
- Where an APM is used internally, why it is so used, by whom and for what purpose; for example, if it relates to measures used for Directors’ remuneration.
- The narrative in strategic reports to give no greater emphasis to APMs or proforma information prepared on a non-IFRS basis than the discussion of the IFRS results. The Guidelines state that APMs should not be displayed with more prominence, emphasis or authority than measures directly stemming from the financial statements.
- Definitions of APMs to be presented for each APM together with reconciliations to IFRS equivalents, which can be by way of cross-reference to where definitions or reconciliations can be found.
- Companies to explain why an APM definition has changed compared to the previous year.
- Companies to be clear about when a measure is an APM, for example, not referring to “profit before tax” when the amount shown is actually calculated on a non-IFRS basis.
- Companies to consider carefully when they give long lists of items which are excluded from adjusted profit (or similar measures) and, in particular, to consider whether all such items are properly excluded; for example, “non-recurring” restructuring costs that appear to recur, share-based payments or legal costs.

Where companies rely on amounts that directly stem from the income statement, we draw companies’ attention to the press notice issued by the FRC in December 2013 ‘FRC seeks consistency in the reporting of exceptional items’, the principles of which remain valid.

Notes:

1. The Guidelines may be found at <https://www.esma.europa.eu/press-news/esma-news/esma-publishes-final-guidelines-alternative-performance-measures>
2. The press notice 'FRC seeks consistency in the reporting of exceptional items' may be found at <https://frc.org.uk/News-and-Events/FRC-Press/Press/2013/December/FRC-seeks-consistency-in-the-reporting-of-exceptional-items.aspx>
3. The required contents of a strategic report are described in section 414C of the Companies Act 2006. Paragraph 2 (a) requires the report to contain a fair review of the company's business. Paragraph 3 requires the review to be a balanced and comprehensive analysis of the development and performance of the company's business during the financial year, and the position of the company's business at the end of that year.