

24 March 2011

Mr S Haddrill  
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Financial Reporting Council  
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By email: [effectivestewardship@frc.org.uk](mailto:effectivestewardship@frc.org.uk)

Dear Mr Haddrill

## **EFFECTIVE COMPANY STEWARDSHIP – ENHANCING CORPORATE REPORTING AND AUDIT**

I write on behalf of Standard Life plc, a major UK FTSE 100 listed company, and its subsidiary companies. We are supportive of the Financial Reporting Council's ('FRC') aims to consider how the effectiveness of the stewardship role of Boards and Audit Committees can be enhanced through corporate reporting and audit and we are keen to support the FRC in its plans to consult with stakeholders, pilot some of the initiatives and consult further on specific proposals to be taken forward. Overall we support the aims the FRC has laid out in the consultation paper and we are keen to work with the FRC towards achieving them as long as there are evidenced cost benefits and the interests of all shareholders are recognised. We have added comments on particular recommendations as follows:

### **Narrative Reporting – Key points**

- a. **The Annual Report should communicate high quality and relevant narrative and financial information to the market.**
  - b. **Directors should take full responsibility for ensuring that an Annual Report, viewed as a whole provides a fair and balanced report on their stewardship of the business.**
  - c. **Directors should describe in more detail the steps they have taken to ensure:**
    - i. **the reliability of the information on which the management of a company, and therefore the directors' stewardship, is based; and**
    - ii. **transparency about the activities of the business and any associated risks.**
  - d. **Companies should take advantage of technological developments to increase the accessibility of the annual report and its components.**
- a. Standard Life plc has a significant retail shareholder base (99% of our total shareholders) and the Board recognises that while a full Annual Report and Accounts ('ARA') (275 pages) is available to all of them, it may not be the most effective means of communicating with them. Therefore, every year since the Company listed, the Board has approved an innovative publication called "Shareholder News" which summarises the financial highlights, the key corporate developments in the past year and encourages shareholder participation in the AGM process. This is issued to all shareholders together with a set of summary financial statements. Research from 2008 showed that Shareholder News was the most popular document received by our shareholders and we continue to receive positive feedback on it.

- c. ii The Board takes Risk Management very seriously. During 2010, the Board established a Risk and Capital Committee and so the 2010 ARA will contain the first report on the Committee's activities since it was established. This provides shareholders with new information on the areas the Committee has focused on. This is complemented by detailed disclosure on the elements of the Group's Enterprise Risk Management Framework elsewhere in the Corporate Governance report. The Framework disclosure is complemented by further detailed disclosure in the Risk Management section of the Business Review which discusses the key risks facing the Group, and this is further complemented by the fully detailed risk management note to the Group financial statements. While this combination requires some effort by shareholders to access and pull it together, this information and the systems which generate it provide the information the directors (and, in turn, the Company's shareholders) need to understand the risks the Company is running and how these are changing and being managed.
- d. We are supportive of the move to strengthen the requirements regarding the use of technology. The Company has 1.5m retail shareholders. Should every one of them take advantage of the right to receive a full ARA, the costs of producing and mailing these would be significant for the company, and the view of the shareholders may be that this was an inefficient use of both cash and product resources. By considering the most efficient ways to distribute the ARA, and making it available on-line as the alternative to a hard-copy document, we are able to demonstrate the Board's commitment to the effective use of both cash and paper resources. Equally, we make strong efforts to make sure that the means of accessing and searching the on-line version of the ARA is clear and accessible.

The Board remains very aware of the challenges to effective narrative reporting. The amount of the information which must be disclosed and the complexities of financial services reporting in particular, both the terminology and the need to understand the difference in e.g. IFRS and EEV measures, mean that the length and content of the narrative reports produced remain daunting for the average investor.

#### **Assuring integrity – key points**

- a. **Investors need to have confidence in the integrity of the narrative and financial information they receive in the Annual Report.**
  - b. **Confidence in corporate reporting should be reinforced by a more effective and transparent assurance regime that involves:**
    - i. **a quality audit of the financial statements;**
    - ii. **the revision of auditing standards to expand the nature and extent of the report provided by auditors to Audit Committees;**
    - iii. **fuller reports by Audit Committees explaining how they have discharged their responsibilities for the integrity of the Annual Report and other aspects of their remit (such as their oversight of the external audit process and appointment of external auditors) and**
    - iv. **an expanded audit report that includes:**
      - i. **a separate new section on the completeness and reasonableness of the Audit Committee report; and**
      - ii. **identification of any matters in the Annual Report that the auditors believe are incorrect or inconsistent, with the information contained in the financial statements or obtained in the course of their audit.**
  - c. **There should be greater investor involvement in the process by which auditors are appointed.**
- b. ii We believe that revising auditing standards to expand the content of the formal reports provided by auditors to Audit Committee would be positive. However, we believe that the proposed areas where the auditors' views would be reported should already be part of the current reporting process, although we recognise that currently this is an informal requirement arising from the quality of the external audit process rather than an auditing standard. However, should the Audit Committee disagree with the auditors' views on a matter (but the view of the auditor has not been sufficient to lead to a qualification in the Audit Report) it is not clear how the Audit Committee would take the difference forward with the Board and we encourage the FRC to explore this via the consultation process.

- b. iii We have reservations on the proposal that the report from the Audit Committee should be expanded to cover all the areas noted. The ARA is already substantial and increasing disclosure is not necessarily in the spirit of making narrative reporting more effective. Equally, we believe that it would be challenging to draft some of the proposed disclosures to avoid “boiler plate” statements (e.g. how the Committee arranged for certain key areas to be addressed) and, therefore, counter to the FRC’s stated aims. We already report on the review of the effectiveness of the external audit, the provision of non-audit services, and the process to consider the re-appointment of the external auditor. Equally, there is already significant disclosure in the notes to the financial statements on “key areas of sensitivity or risk”, all of which have been discussed in advance by the Audit Committee, having been highlighted by management and commented on by the auditors. The Audit Committee performs a cross-check to make sure that there are no differences between the two lines of reporting. We do not believe that additional disclosure of this process would enhance the Committee’s report and would encourage the FSA to consider this further before finalising its views.

It is also difficult to foresee a “matter of material significance” which has been “identified by the auditors in their report to the Committee” but which has “not been addressed elsewhere in the Annual Report” and which “should be known to users” to ensure the Annual Report is “fair and balanced”. If the Directors are fulfilling their role effectively, we believe that such matters would be clearly disclosed in the ARA, and should not need to be found only as an item in the report of the Audit Committee’s activities. It is also not clear which matters would be disclosed regarding “the audit committee’s dialogue with investors related to any material audit related issues (not covered elsewhere in the report)”. We believe that any material audit related issues would be covered elsewhere in the Annual Report. Equally we believe that if there has been dialogue with investors “in relation to any material audit related issues”, for listed companies, these issues would need to have been considered as potential Inside Information issues and may well already have been fully disclosed to the Market.

- c. We have reservations over the proposal that there should be more involvement of investors in the process to appoint or re-appoint auditors. We note the proposal that this should be limited to “a number of principal investors” and support this, as in our own case, it would not be practical or cost-effective to involve retail shareholders in this process. Equally, we recommend that the FSA should clarify that “involvement” does not extend to sharing any documentation related to the tender or selection process. Furthermore, we believe that it is not clear what the response of the Audit Committee would be should any of the Company’s “principal investors” disagree with the approach taken by the Company and encourage the FRC to consider what steps should be taken if this were to arise.

We would also note that all investors have the opportunity to express their views and/or ask questions regarding the processes to appoint auditors both through voting at the AGM on the relevant resolution and using the rights granted to them under the Shareholder Rights Directive to ask any reasonable questions on such topics. We suggest that the FRC should encourage investors to exercise these rights and use the AGM as a forum for discussion, and perhaps this could be embedded in the Stewardship Code as it evolves.

## **Fostering Quality**

**The FRC’s responsibilities should be developed to enable it to support and oversee the effective implementation of its proposals.**

**The FRC should establish a market participants group to advise it on market developments and international initiatives in the area of corporate reporting and the role of assurance and on promoting best practice.**

We believe that it would be useful for the FRC to continue to develop its proposals to create Practitioners Forums to discuss current issues, as well as a means to explore new models. However, as the additional costs involved in these initiatives would need to be passed on via levies to listed companies, the results of the FRC's initiatives in these areas would need to bring demonstrable benefit to shareholders.

**Conclusion**

We hope that these points will inform the FRC's continuing discussions as it continues to pursue its stated aims and we look forward to participating in the upcoming consultation process.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Malcolm Wood', written in a cursive style.

PP Malcolm Wood  
Group Company Secretary and General Counsel