FINANCIAL REPORTING WORKSHOP

Other Disclosures

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Key considerations

- What are these other disclosure?
- Are they important to you as:
  1. The organisation
  2. The regulators
  3. users of financial statements/annual report

Outline

1. Introduction
2. Value of other information
3. Status
4. Governance Disclosures
5. Corporate Social Responsibility Disclosures
6. Integrated Reporting
7. Fraud Disclosures

Introduction

- There is an increasing trend for businesses to produce information on **social, environmental and sustainable aspects** of their operations
- The disclosure of such non-financial information usually takes place through **Environmental and Sustainability or Corporate Social Responsibility reports**.
- Although guidelines exist for the production of such reporting, and legal requirements can be found in some countries, their **use is often optional**.
- *The Companies Act, 2015 requires listed companies to include a detailed Business Review.*

Introduction (cont…)

- Companies may find it in their interest to **disclose voluntarily** certain non-financial information, particularly if it is designed as part of a package **to improve their credibility and acceptance in key markets**, or if it enables them to undertake business more successfully.

- In sectors dominated by large multinational enterprises, disclosure of such information may be seen as an **important business driver.**

Value of other disclosures

1. Investment decision making
2. Legal requirements (CMA; CBK)
3. Risk mitigation
4. Avoiding unethical companies
5. PRI – United Nations Principles for responsible Investment (ESG information)
6. Improve company reputation/credibility
7. Improve transparency in reporting
8. Attract & retain top talent

Status

- In response to a 2013 survey conducted by Ernst & Young of more than **160 investors, analysts, and portfolio managers** around the globe, 90% respondents stated that nonfinancial performance had played a pivotal role in their investment decision-making in the past 12 months.
- The report concluded: "*This demonstrates that the analysis of nonfinancial issues can no longer be dismissed as a niche approach to investment.*"
- *EY, Tomorrow's Investment Rules: Global Survey of Institutional Investors on Non-Financial Performance (2014).*

Status (cont…)

- In response to PwC's survey in 2014 of institutional investors with $7.6 trillion in assets under management, **73%** said that **risk mitigation is the primary reason** they consider sustainability information. **55%** said that **avoiding unethical companies** is a reason for their interest, and **52%** said that **financial performance** is why they factor sustainability information into their investment decisions.

- Despite investor interest in nonfinancial information, companies are not providing the information that investors want. **61%** of investors stated that they are **dissatisfied** with corporate disclosures of social and environmental information by U.S. companies.

- *PwC, Sustainability Goes Mainstream: Insights Into Investor Views (May 2014).*

Governance Disclosures

- In Kenya, governance disclosures are guided by the requirements of the *companies Act 2015* and the CMA code of corporate governance practices for issuers of securities to the public 2015.

- Section 6 & 7 define the minimum disclosure requirements with regards to other information *(contained in the annual report)*.

Governance Disclosures (cont…)

Key disclosure components:

- **The Board structure** – independent & other non executive directors (2/3); minority shareholders representation; committees of the board; management and their mandate,
- **The Board responsibility** for preparing the annual report and accounts,
- **External auditor's responsibilities**, and appointment
- **Audit committee** – members, qualifications, independence and mandate *and activities during the year/period*

Governance Disclosures (cont...)

Key disclosure components cont….

- **Risk management policy** and internal controls
- **Company vision, mission**, values and strategic objectives
- **Compliance with Laws, Regulations** and Standards – audit; level of compliance; any departures.
- **Whistle blowing policy** whether its observed by all employees of the entity

Governance Disclosures (cont...)

- **Details about Board members –** names; qualification; selection; independence;
- **Ethical leadership and corporate citizenship –** e.g. CSR policy & conflicts of interest
- **Environmental , Social and Governance policies** – content & implementation
- **Performance** – key highlights for the financial performance; trends that may affect performance in the future.

Governance Disclosures (cont…)

- **Compliance with IFRS** and any departures (in extremely rare circumstances)
- **Key stakeholder groups** – Top ten direct shareholders and for a subsidiary, name of parent & ultimate parent
- **Statement of compliance with corporate governance principles** – aspects not applied; reasons, timelines and strategies towards application
- **Remuneration policies** – director emoluments; fees; share options ; director loans
- **Resignation of a serving board member** – reasons for the exit.

Corporate Social Responsibility Disclosures

- CSR (*also termed "Corporate Social Investment"*) disclosures can be used by a company to show **accountability** by indicating their vision for the future and accounting for past performance.

- Companies who communicate their social and environmental work can receive advantages of good **reputation** and build a relationship based on **trust** with the society in which they operate.

Corporate Social Responsibility Disclosures (cont...)

Key values of a CSR Report:

- Communicates the company's CSR efforts to stakeholders
- Relays information successes and challenges on CSR issues e.g. climate change, employee and supplier diversity initiatives, and community investments and partnerships.
- Enhances transparency and improves a company's reputation with certain stakeholders, e.g.; shareholders, employees, suppliers and communities within which the company operates.

Corporate Social Responsibility Disclosures (cont...)

Key values of a CSR Report (cont...):

- Effective outreach tool to improve shareholder relations which may deter activist shareholders from threatening litigation.

- Provides existing and potential investors with information to assist in analyzing investment decisions.

Corporate Social Responsibility Disclosures (cont...)

Common elements & Disclosures:

- ***CEO's brief*** *- noting the company's commitment to CSR issues and its willingness to discuss challenges and promote successes in CSR,*
- *The company's* ***CSR policy or mission statement****,*
- *Forward-looking statements*
- ***Most significant****, disclosures addressing issues most important to each of the company's key stakeholders*

Corporate Social Responsibility Disclosures (cont...)

Key stakeholders & relevant CSR information:

- **Shareholders**— Corporate governance, role of the board in risk management, sustainability reporting and evaluation of CSR performance.
- **Employees**—addressing diversity, health and safety, training and mentoring, employee relations, and wages and benefits.
- **Customers**—addressing customer service and privacy.

Corporate Social Responsibility Disclosures (cont...)

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Corporate Social Responsibility Disclosures (cont...)

The Global Reporting Initiative (GRI):
GRI is an International Independent Organization that helps businesses, governments and other organizations **understand and communicate the impact of business on critical sustainability issues** such as climate change, human rights, corruption and many others.

The GRI - G4 Guidelines outline additional recommended disclosures that may be included in a CSR report as below:-

- **Economic Considerations**—disclosing the company's impacts on the economic conditions of its stakeholders and on economic systems at local, national and global levels.

Corporate Social Responsibility Disclosures (cont...)

The Global Reporting Initiative (GRI). Cont….

- **Environmental Issues**—disclosing the company's impacts on living and non-living natural systems (land, air, water and ecosystems), including impacts related to inputs (such as energy and water), outputs (such as emissions, effluents and waste) as well as environmental compliance and expenditures.

- **Ethics and Integrity**—disclosing the company's values, principles and standards, and its internal and external mechanisms for ; seeking advice on ethical and lawful behavior and reporting concerns about unethical or unlawful behavior and matters of integrity.

Corporate Social Responsibility Disclosures (cont…)

The Global Reporting Initiative (GRI). Cont…

- **Social Impact**—disclosing the company's impacts on the social systems within which it operates, including those relating to human rights, society and product responsibility.

- **Stakeholder Engagement**—disclosing the company's stakeholder engagement during the reporting period and not limiting it solely to engagement conducted for purposes of preparing the CSR report.

Business Review

655 (3) The business review complies with this subsection if-

(a) it contains-

- *(i) a fair review under subsection (1) of the company's business; and*
- *(ii) a description of the principal risks and uncertainties facing the company, and*

(b) is a balanced and comprehensive analysis

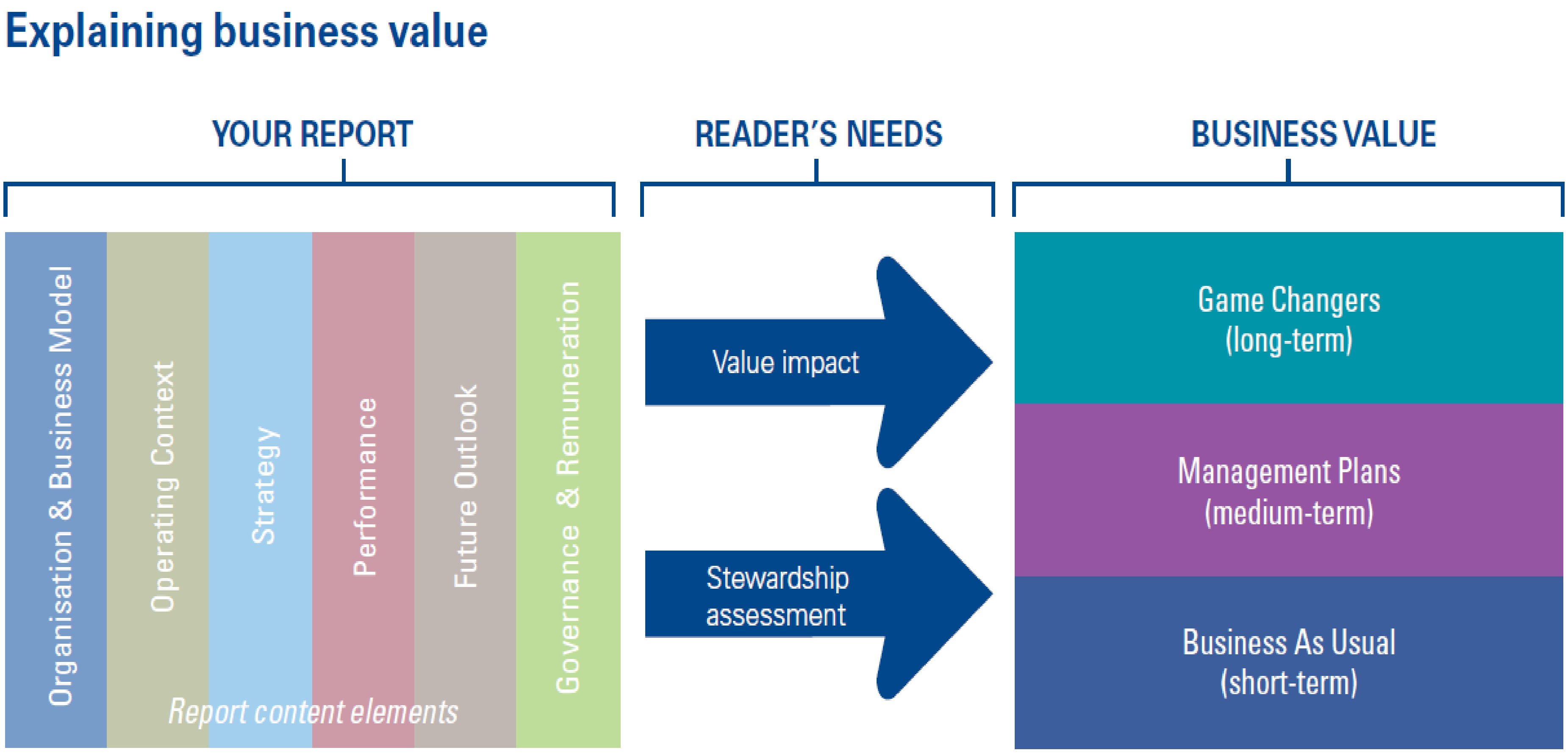
- *(i) the development and performance of the business of the company during the company's financial year; and*
- *(ii) the position of the company at the end of that year, consistent, with size 'and complexity of the business..*

Integrated Reporting

- *Integrated reporting is a process that brings together the material information about an organization's strategy, governance, performance and prospects in such a way that reflects its* ***commercial, social and environmental context*** *within which it operates. It provides a clear and concise representation of how an organization demonstrates stewardship and how it creates value, now and in the future*

- *(CMA Code of corporate governance 2015. Sec. 6.1.5)*

Integrated Reporting (cont…)



Fraud

ISA 240 – Fraud definition

- An **intentional act** by one or more individuals among management, those charged with governance, employees, or third parties, involving the **use of deception** to obtain an **unjust or illegal** advantage

Fraud Disclosures

a. How many organisations would disclose fraud?

b. Would you as the head of finance/audit committee encourage your organisation to disclose fraud??

c. What is the impact of such disclosures to the businesses???

d. What is the role of the auditor (internal and external) in disclosing fraud????

Fraud Disclosure (cont...)

Auditor's responsibility on reporting fraud:

- **ISA 260 - Communications to Management and Those Charged with Governance.** If the auditor has identified a fraud or has obtained information that indicates that a fraud may exist, the auditor shall communicate these matters on a timely basis to the **appropriate level of management** in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities.

- *Is fraud a **Key Audit Matter** for inclusion in the new auditor report (ISA 701)?*

Fraud Disclosure (cont…)

- Unless all of those charged with governance are involved in managing the entity, if the auditor has identified or suspects fraud involving:
  (a) Management;
  (b) employees who have significant roles in internal control; or
  (c) others where the fraud results in a material misstatement in the financial statements,
- The auditor shall communicate these matters to those charged with governance on a timely basis (ISA 240.40)

Fraud Disclosure (cont...)

- If the auditor suspects fraud involving management, the auditor shall communicate these suspicions to those **charged with governance** and discuss with them the nature, timing and extent of audit procedures necessary to complete the audit (ISA 240.41)
- 42. The auditor shall communicate with those charged with governance **any other matters related to fraud** that are, in the auditor's judgment, relevant to their responsibilities (ISA 240.42)

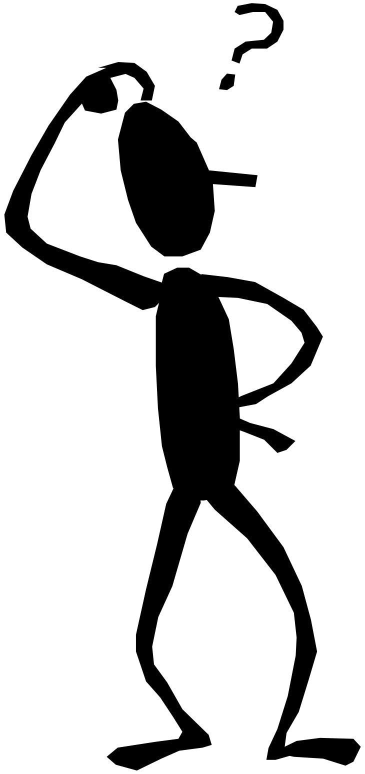
Fraud Disclosure (cont…)

Communications to Regulatory and Enforcement Authorities

- If the auditor has identified or suspects a fraud, the auditor shall determine whether there is a responsibility to report the occurrence or suspicion to a party outside the entity (ISA 240.43)

- Although the auditor's professional duty to maintain the confidentiality of client information may preclude such reporting, the auditor's legal responsibilities may override the duty of confidentiality in some circumstances – *Section 24 of the Banking Act, Anti Money Laundering Acts etc.*

Interactive Session



Wrap up

- Capital providers are continuously demanding entities to be more transparent
- Non financial information is gaining more traction as a tool to communicate the strategic objectives and performance of the entities = meeting needs of users
- Business review is now a statutory requirement
- Integrated Reporting continues to gain traction
- At what level of the pyramid is your organisation?
- Start today…

Presenter's Contact

Presenter's Contacts

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THANK YOU