

 Regulatory Policy Committee	Opinion
Impact Assessment (IA)	Non-financial reporting
Lead Department/Agency	Department for Business, Innovation and Skills
Stage	Consultation
IA Number	n/a
Origin	European
Expected date of implementation	6 December 2016 (SNR12)
Date submitted to RPC	14 January 2015
RPC Opinion date and reference	25 February 2015 RPC15-BIS-2314
Overall Assessment	GREEN
RPC comments	
<p>The IA is fit for purpose.</p> <p>The IA clearly explains the rationale for the proposals – to address a problem of information asymmetry between users of non-financial information and company directors, by standardising the level of disclosures. The IA identifies the main costs and benefits to business resulting from the proposals and it includes indicative costs, which the Department proposes to test at consultation.</p> <p>The proposal is of European origin. While the preferred option, Option 2, goes beyond Option 4 because it maintains existing UK reporting requirements, it is considered out of scope of ‘One-in, Two-out’. This is in line with past interpretations of paragraph 1.9.8.ii of the Better Regulation Framework Manual.</p>	
Background (extracts from IA)	
What is the problem under consideration? Why is government intervention necessary?	
<p><i>“Annual reports provide shareholders and investors with information on companies’ financial and non-financial performance. Non-financial information comprises quantitative and qualitative data on business operations, policies pursued and their impact. Increasingly, investors are using reported non-financial information to inform their decisions. However the current quality and quantity of non-financial reporting does not adequately address the asymmetry of non-financial information that exists between companies and investors. Additionally there is no standard reporting framework across the EU to allow consistent comparison of companies. Finally, there is insufficient diversity in company board membership, in terms of gender and skills. Insufficient transparency about diversity policies could be contributing to this. To address these issues a regulatory intervention at EU level is necessary to set minimum non-financial reporting requirements that are in line with other European countries. The policy options affect ‘public interest entities’ (PIEs), which are companies whose activities are likely to have a significant impact on the economy and society.”</i></p>	

What are the policy objectives and the intended effects?

“The policy objective is to enhance PIEs’ overall effectiveness. (PIEs are either: listed companies whose transferable securities are admitted to trading on an EU-regulated market; or credit institutions; or insurance undertakings). This is to be achieved through encouraging a better assessment of non-financial risks and opportunities by companies, which is then incorporated into their business strategies and models: these are then disseminated in company annual reports, thus contributing to increased transparency, and enhanced companies’ accountability. The increased transparency will help investors to make more informed investment decisions. Finally the policy should make companies consider the composition of their boards, and improve their diversity. Diversity should help boards provide better management and leadership by improving the quality of discussion and challenge at board meetings.”

Identification of costs and benefits, and the impacts on business, civil society organisations, the public sector and individuals, and reflection of these in the choice of options

The Department proposes to reform and strengthen the non-financial reporting requirements as laid out in the Non-Financial Reporting (NFR) Directive (2014/95/EU).

The IA explains clearly the rationale for the proposal. It explains that there is a problem of information asymmetry between companies and their shareholders, which can affect investment decisions. There have also been growing concerns expressed about the quality and quantity of NFR and this proposal seeks to standardise the level of disclosures. Under the proposals, a company would be required to provide information on areas such as its environmental policy, how it approaches human rights issues, and its diversity policy.

Options being considered

The Department is considering four options –

1. Do nothing.
2. Implement the EU non-financial reporting directive (NFRD) for PIEs with more than 500 employees.
3. Extend the EU non-financial reporting (NFR) requirements to all companies listed in an EU-regulated market (regardless of the number of employees).
4. Adopt Option 2 and dis-apply the current UK reporting requirements for all companies outside the scope of the EU NFRD.

The Department’s preferred option is Option 2. This option will maintain the current UK reporting requirements and, therefore, appears to go further than Option 4. The Department will need to provide an explanation of the differences between the two options at final stage, including the reasons for maintaining the existing standards.

Impact on business

The Department estimates that 609 public interest entities would incur full costs to file NFR. A further 11,000 subsidiaries would incur some costs from providing information to their parent companies. Under Option 2, only those PIEs with an average of 500 or more employees in the last financial year are expected to be affected by the proposal.

The IA provides best estimates of the main potential costs and benefits to business resulting from the proposal. The Department explains that assessing the full costs of NFR has been difficult as industry has provided only limited information to date. The IA, therefore, includes indicative costs for each of the options being considered, which the Department proposes to test at consultation. For its favoured option, Option 2, the Department estimates that businesses will incur one-off costs of between £1.54 million and £2.34 million (with a best estimate of £1.54 million). This results from, for example, introducing new systems or processes and becoming familiar with the revised regulations. On-going costs to business are estimated to total between £552,000 and £863,000 (with a best estimate of £571,000) each year. The Department estimates that 11 small businesses, which are parent companies, will incur £56,000 in one-off costs as a result of the proposal.

In addition, the Financial Reporting Council (FRC) is expected to incur a cost of £200,000 to amend its guidance. Given that the FRC is funded by industry, any additional costs incurred by it should be treated as direct costs to business and included within the estimated annual net cost to business (EANCB).

The Department expects UK investors to be the main beneficiaries of the proposal, on the basis that consistent, high quality non-financial information could help them make more informed decisions. This would affect 700 asset managers and over 4,000 institutional investors. Other stakeholder groups, such as non-governmental organisations and civil society organisations, are also expected to benefit from the increased transparency of non-financial information, as it would help them monitor company activity and increase engagement with companies. At final stage, the Department will need to strengthen its evidence base to show clearly how these groups will benefit from the proposals.

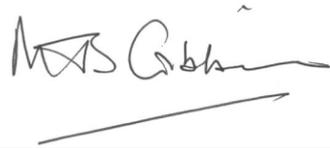
Comments on the robustness of the Small & Micro Business Assessment (SaMBA)

The proposal is of European origin. A SaMBA is, therefore, not required.

Comments on the robustness of the OITO assessment.

The proposal is of European origin. While the preferred option, Option 2 goes beyond Option 4 because it maintains existing UK reporting requirements, it is considered out of scope of 'One-in, Two-out'. This is in line with past interpretations of paragraph 1.9.8.ii of the Better Regulation Framework Manual. To support balanced reporting of overall EU burdens in the Statement of New Regulation, the final stage IA should include an estimated EANCB figure, with supporting evidence, for RPC validation.

Signed

A handwritten signature in black ink, appearing to read "Michael Gibbons". The signature is written in a cursive style with a long horizontal stroke at the end. There is a small mark above the letter 'i' in "Gibbons".

Michael Gibbons, Chairman