

The essentials unravelled

A guide for non-executive directors on the issues impacting private and non-listed companies



Introduction

Grant Thornton's guide for non-executive directors addresses issues for private and non listed companies which will be topical during the current reporting cycle as well as wider business concerns.

This summary covers aspects of current legislation, regulation, tax and financial reporting which have been identified as areas non-executive directors may need to address and suggests a series of questions to be taken up with the Board.

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Governance

In May 2010 the Financial Reporting Council (FRC) issued the newly retitled UK Corporate Governance Code (the Code) to replace the Combined Code 2008. The Code applies to all companies with a Premium Listing of equity shares on the London Stock Exchange. However other companies who wish to follow best practice in this area may choose to voluntarily apply certain aspects of the Code.

Changes have been made both to the structure and content of the Code including new and amended principles and provisions.

For companies which choose to establish an audit committee, recent changes have been made to the Financial Reporting Council's Audit Committee Guidance. In respect of the provision of non-audit services by the company's external auditor, the role of the audit committee has been updated.

Considerations

The main principle on board balance and independence has been revised to emphasise the need for a balance of skills, experience, independence and knowledge of the company. Further, the supporting principles on board appointments now include an explicit requirement to have due regard '...for the benefits of diversity on the board, including gender.'

Companies need to include in the annual report an explanation of the business model and the strategy for delivering the objectives of the company.

The board is responsible for determining the nature and extent of the significant risks it is willing to take in achieving its strategic objectives, and should maintain sound risk management (and internal control) systems.

Performance-related components of executive directors' remuneration should be stretching and designed to promote the long-term success of the company.

The Bribery Act 2010

The UK Bribery Act is expected to come into force in 2011, three months after the Government publishes final guidance on a new corporate offence.

The legislation:

- introduces the corporate offence of failure to prevent bribery by “associated persons” working on a commercial organisation’s behalf, but it can avoid conviction if it can show that it has **adequate procedures** in place to prevent bribery
- makes it a criminal offence to give, promise or offer a bribe and to request, agree to receive or accept a bribe either at home or abroad. A separate offence covers the bribery of a foreign public official
- sets the maximum penalty for individuals for bribery at ten years imprisonment, with an unlimited fine, which also applies to companies.

The Government has a statutory obligation to provide guidance on what constitutes ‘adequate procedures’. The Ministry of Justice published draft guidance last year, which outlined six principles of good practice, and the final guidance is expected to amplify this but also address certain difficult issues.

Adequate procedures and the six guiding principles

- 1 A corruption risk assessment should be performed.
- 2 Top level commitment: an organisation must make a clear and unambiguous commitment to establishing a culture in which bribery is unacceptable.
- 3 Good due diligence - you must be able to demonstrate that you know who you do business with.
- 4 Clear practical and accessible policies and procedures.
- 5 Policies and procedures must be effectively implemented.
- 6 There must be monitoring and review of the effectiveness of anti-bribery controls with consideration of the need for external audit.

Considerations

It takes longer than realised to respond to the Act and organisations should act now in response.

It may be the first time the business performs a corruption risk assessment and it may require external help to understand the unique risks involved.

Policies and procedures should be introduced, revised or aligned to mitigate the risks identified.

Training of staff most exposed to corruption risk is essential.

Enhanced due diligence of associated persons is key.

Pensions Auto Enrolment

The Government confirmed on 27 October 2010 that the requirement to automatically enrol staff into a pension plan will go ahead. The start date for auto enrolment will be phased according to employee numbers. Employees are able to opt out of the arrangement, but cannot be encouraged to do so.

The largest employers will be included from 1 October 2012 with all employers covered by 1 September 2016. All employers with 50 or more staff need to comply by 1 July 2014. While it is good news for employees who do not have a pension scheme, employers will face a significant administrative burden as well as the cost of the contributions.

Employers can use their own pension schemes or the National Employment Savings Trust (NEST). The requirements placed on employers are complex with a system of fines in place for non-compliance.

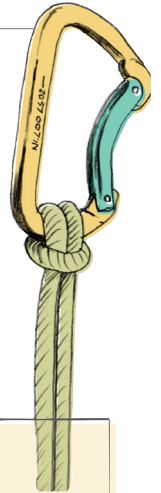
Considerations

Employers will need to:

- identify the actions that need to be taken to comply with these changes and the associated costs
- establish how auto enrolment will impact upon current benefits and the pension offering
- consider whether to maintain existing pension scheme contribution rates
- identify increased administration requirements and whether new systems are needed.

All employers will need to take some action on this issue to ensure that they are ready to meet their auto enrolment deadlines. These plans will increase costs for the majority of employers who face a significant administrative burden as well as the cost of the contributions.

Employers will not need to enter employees into a pension plan until they have completed three months' service. This will help employers with staff on short term or seasonal contracts, or employers who typically have a high level of staff turnover.



iXBRL

HMRC will require companies to file their corporate tax returns online, along with accompanying computations and accounts, in iXBRL format (Inline Extensible Business Reporting Language), from 1 April 2011 for any accounting period ending after 31 March 2010.

iXBRL is a new electronic format for business information, which HMRC expects to provide benefits in the preparation, analysis and communication of business and financial data.

At this stage, companies will not be required to file their accounts at Companies House in iXBRL format although this is expected to be required from 2013.



Considerations

The iXBRL market is very new. As a result, creating accounts in iXBRL format is particularly complex and creates additional work in the accounts production process, therefore there is a cost to companies to meet this requirement.

There are some solutions to consider when planning for this change:

- purchasing/upgrading software and training in house staff
- outsourcing to a dedicated tagging solution provider which could be your accountancy firm.

Financial Reporting Review Panel (FRRP) key areas of interest

The FRRP seeks to ensure that the annual accounts of public companies and large private companies comply with the requirements of the Companies Act 2006 and applicable accounting standards.

The remit of the FRRP also extends to directors' reports. The FRRP can ask directors to explain apparent departures from the requirements. If the FRRP is not satisfied by the directors' explanations it aims to persuade the directors to adopt a more appropriate accounting treatment.

The FRRP publish an annual report based on findings from their reviews of accounts.

Considerations

Business review. The Companies Act 2006 requires all business reviews to contain a fair review of the company's business and a description of the principal risks and uncertainties facing the company.

FRS 18 Accounting Policies requires disclosure of a description of each of the accounting policies that is material in the context of the financial statements.



Financial Reporting Standard for Medium-sized Entities (FRSME)



The Accounting Standards Board has proposed replacing existing UK GAAP with the Financial Reporting Standard for Medium-sized Entities (FRSME) for UK companies that are not publicly accountable.

This change is planned for annual periods commencing 1 July 2013. The FRSME is based on the International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs), amended to be suitable for use in the UK.

The proposed adoption of the FRSME would lead to changes to the:

- format of the financial statements and the disclosures required
- recognition criteria for various assets and liabilities
- basis on which many items are measured and the treatment of certain gains and losses.

Considerations

There are many differences between the proposed FRSME and existing UK GAAP which need to be considered. For large groups, the cost of conversion to the FRSME may be significant.

Changes in the recognition and measurement of assets, liabilities, income and expenses may have an impact on:

- loan terms and covenants
- remuneration and reward
- the ability to pay dividends.

Questions for the Board to consider

Governance

- Has the composition of the Board been considered and are changes necessary to the existing Board membership?
- Has the nature and extent of the Board's attitude to significant risk been documented and communicated?
- Is a review of executive remuneration policies and service contracts required?
- Do the terms of reference of the audit committee require revision?

The Bribery Act 2010

- Have we performed a Corruption Risk Assessment (CRA)? Are policies and procedures for our bribery strategy bespoke or aligned to the CRA?
- Do we clearly and regularly communicate the organisation's policies to all staff?
- Do our policies and procedures fully address facilitation payments, gifts, entertainment, corporate hospitality, or political donations on a global basis?
- Is there an anti-corruption training programme for the Board, all managers and staff?
- Is there one individual within the organisation responsible for implementing the requirements of the Act, investigating reports of corruption and employing appropriate sanctions?
- Do we have an effective compliance monitoring programme which provides the requisite assurance?

Pensions Auto Enrolment

- Have we identified the impact on our current benefits and/or pensions offering?
- Do we know what actions need to be taken to comply with these changes and the associated costs?
- How do we intend to fund this exercise?
- How do we communicate this as a positive benefit to staff?

Tax considerations

- Do we have a written policy on our approach to tax planning?
- What is our current relationship with Her Majesty's Revenue & Customs (HMRC)? Are we considered a 'low risk' taxpayer? What is our current link with our HMRC 'Customer Relationship Manager'?
- Do we have a clear understanding of our corporate tax liability exposure and any international implications?
- Have we given sufficient thought to the way we reward our best people in a way that both incentivises and is tax efficient?

Questions for the Board to consider

iXBRL

- Will the potential software upgrade and processes to address this change meet the 1 April 2011 deadline?
- Have we planned how we will provide the required iXBRL accounts?

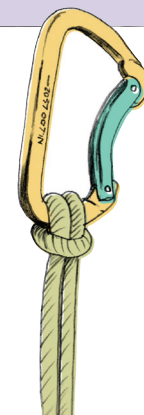
Financial Reporting Review Panel (FRRP)

- Does the business review address only those risks and uncertainties that are key to the business?
- Does the business review explain why the risks and uncertainties are key to the business, the steps taken to mitigate their impact and the current circumstances which give rise to the threat?
- In respect of turnover, has an appropriate policy been given for each main income stream clearly identifying the recognition and measurement criteria?

Financial Reporting Standard for Medium-sized Entities (FRSME)

- What are the internal and external cost and resource implications of conversion to the FRSME?
- Which of the following wider business issues do we need to consider?
 - funding arrangements
 - banking covenants
 - contract terms
 - bonus schemes
 - corporation tax
 - systems and training
 - dividend strategy
 - group structure

If you have any questions or would like to discuss any of the topics covered in this publication please contact your Grant Thornton representative. Alternatively, please contact your local Grant Thornton office directly for assistance.



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