3rd Floor, Anglo Mauritius House, Intendance Street, Port Louis

http://frc.govmu.org

Email: frc.mauritius@intnet.mu

Financial Reporting CounciL

**Bulletin on Review of Annual Reports for the six months ended 31 December 2017**

**I Introduction**

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Annual reports are documents submitted annually by companies to shareholders and key stakeholders. They outline the entities’ financial performance and other relevant material information such as business model, key risks, mission and achievements.

In order to ensure quality reporting, FRC reviews the annual reports of Public Interest Entities (PIEs) to ensure that these are in compliance with the requirements of IFRSs and the Code of Corporate Governance.

This bulletin describes the accounting and corporate reporting issues commonly identified during the six months ended 31 December 2017.

During the period under review, FRC reviewed the annual reports of 46 PIEs consisting of 28 group reviews, 13 full reviews and 5 follow-up reviews.

* 1. **Group Reviews and Full Reviews**

FRC carried out the review of annual reports of entities within groups and other individual entities.

With respect to the group reviews, FRC had reviewed the annual reports of 4 groups of companies which consisted of 28 PIEs. Also, FRC conducted full annual report reviews of 13 other individual entities for the period ended 31 December 2017.

The year ends of the annual reports reviewed were as follows:

* 1 annual report with reporting date December 2015;
* 16 annual reports with reporting date June 2016;
* 1 annual report with reporting date September 2016;
* 22 annual reports with reporting date December 2016; and
* 1 annual report with reporting date 31 March 2017.

The table below indicates the categories of PIEs and their corresponding sectors of business.

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Types of PIEs** | **Sectors** | | | | | | | | |
| **BIF** | **Commerce** | **Industry** | **Investment** | **Leisure & Hotels** | **Sugar** | **Transport** | **Others** | **Total** |
| Listed on SEM | 2 | - | 4 | 3 | 3 | 1 | 1 | 1 | 15 |
| Financial institutions regulated by BOM | 4 | - | - | - | - | - | - | - | 4 |
| Financial institutions regulated by FSC | 3 | - | - | 6 | - | - | - | - | 9 |
| Category 4 PIEs as per the Financial Reporting Act (“FRA”)[[1]](#footnote-1) | 2 | 2 | 3 | 1 | 2 | 2 | - | 1 | 13 |
| **Total** | **11** | **2** | **7** | **10** | **5** | **3** | **1** | **2** | **41** |

Details of Group reviews and full reviews conducted by FRC are described below:

1. **Group Reviews**

The objective for reviewing PIEs within the groups is to have a better understanding of the group structure and the businesses undertaken within the groups, which in turn provides deep insight in the disclosures made by these group of companies in their annual reports.

This type of review also helps to identify any irregular related party transactions among the entities within the groups, which might not be possible if an individual approach is adopted for these group of companies.

Group reviews were mainly based on focused areas of IFRSs significant to the business of the respective PIEs. In this regard, the objectives of the group review exercises are to:

1. assess the financial situation of the group and its subsidiaries (liquidity and financial performance of the group and its subsidiaries);
2. evaluate the accounting policies adopted by the group and its subsidiaries (For example exemption for consolidation (IFRS 10), Fair value (IFRS 13), Revenue Recognition (IAS 18));
3. focus on risky sectors such as construction, leisure and hotels, textile, insurance, and banking within the group; and
4. assess key IFRSs relevant to the activities of the Group.

For the six months ended 31 December 2017, FRC carried out the review of 4 groups with 28 PIEs as described below:

1. The first group (‘Group 1’) of companies selected for review, consisted of 3 companies which meet the definition of Public Interest Entities under the FRA.

This group of companies is involved in the provision of financial services, such as insurance, fund management and lease and deposit taking services. All the 3 entities within this group of companies are regulated by FSC.

1. The second group reviewed (‘Group 2’) had 7 entities classified as Public Interest Entities (“PIEs”) under the FRA. All the 6 PIEs within Group 2 were in the hotel industry. This group of companies consisted of 4 listed entities and 3 Category 4 PIEs.

The sectors under which the above PIEs carry out their business activities are as follows:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Types of PIEs** | **Sectors** | | | | | |
| **Commerce** | **Investment** | **Leisure & Hotels** | **Sugar** | **Others** | **Total** |
| Listed on SEM | - | 1 | 1 | 1 | 1 | 4 |
| Category 4 PIEs as per the FRA | 1 | - | 2 | - | - | 3 |
| **Total** | **1** | **1** | **3** | **1** | **1** | **7** |

1. FRC conducted the review of a third group of companies (‘Group 3’) which is involved in the provision of banking and financial services. This group of companies entailed 9 PIEs [1 listed company, 1 regulated by BOM, 6 regulated by FSC and 1 Category 4 PIE].

The table below describes the sector under which the above PIEs operate:

|  |  |  |  |
| --- | --- | --- | --- |
| **Types of PIEs** | **Sectors** | | |
| **BIF** | **Investment** | **Total** |
| Listed on SEM | 1 | - | 1 |
| Financial institutions regulated by BOM | 1 | - | 1 |
| Financial institutions regulated by FSC | 1 | 5 | 6 |
| Category 4 PIEs as per the FRA | 1 | - | 1 |
| **Total** | **4** | **5** | **9** |

1. FRC also carried out the review of a fourth group of companies (‘Group 4’) which had 9 PIEs.

The principal activity of the holding company of Group 4 is that of investment holding.

Group 4 is structured in 7 clusters with operations in:

1. Cane
2. Power
3. Brands
4. Property Management & Construction
5. Leisure
6. Finance
7. Investments

The table below illustrates the sectors under which the companies within Group 4 operate by type of PIEs:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Types of PIEs** | **Sectors** | | | | |  |
| **BIF** | **Commerce** | **Industry** | **Investment** | **Sugar** | **Total** |
| Listed on SEM | 1 | - | - | 2 | - | 3 |
| Category 4 PIEs as per the FRA | - | 1 | 3 | - | 2 | 6 |
| **Total** | **1** | **1** | **3** | **2** | **2** | **9** |

1. **Full reviews of other individual entities**

FRC also reviewed the annual reports of individual entities. The PIEs selected for the review exercise were:

* Entities which are listed on the Stock Exchange of Mauritius;
* Companies that scored Grade 3 in its previous review; and
* PIEs for which complaints were received.

For the six months ended 31 December 2017, FRC conducted the annual report reviews of 13 other individual entities. The table below illustrates categories of PIEs per sector:

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| **Types of PIEs** | **Sectors** | | | | | | |
| **BIF** | **Industry** | **Investment** | **Leisure & Hotels** | **Transport** | **Others** | **Total** |
| Listed on SEM | - | 4 | 1 | 1 | 1 | **-** | **7** |
| Financial institutions regulated by FSC | 2 | -- | - | - | - | **-** | **2** |
| Financial institutions regulated by FSC | - | - | 1 | - | - | **-** | **1** |
| Category 4 PIEs as per the FRA | 1 | - | 1 | - | - | **1** | **3** |
| **Total** | **3** | **4** | **3** | **1** | **1** | **1** | **13** |

* 1. **Follow up reviews**

FRC undertook follow-up reviews to assess the extent to which findings raised on previous reviews had been satisfactorily addressed by the PIEs. New issues such as the application of new standards, amendments to standards and regulations arising during the course of the follow-up reviews of the annual reports were also considered.

For the period under consideration, 5 follow up reviews were undertaken. These consisted of PIEs which had obtained Grade 2B or had other specific issues that were identified in the previous reviews.

The following table analyses the follow up reviews of PIEs by sectors:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Types of reviews** | **Sectors** | | | | | |
| **BIF** | **Commerce** | **Industry** | **Investment** | **Leisure & Hotels** | **Total** |
| Listed on SEM | 1 | - | - | - | 1 | **2** |
| Category 4 PIEs as per the FRA | - | 1 | 1 | 1 | - | **3** |
| **Total** | **1** | **1** | **1** | **1** | **1** | **5** |

**II Overview of findings from annual report reviews**

**\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

Section 75 of the FRA requires a Public Interest Entity to prepare its financial statements in compliance with IFRS and to adopt corporate governance in accordance with the National Code of Corporate Governance.

As mentioned above, FRC conducted group reviews of 4 groups of companies (which consisted of 28 PIEs), full reviews of 13 other individual entities and 5 follow up reviews for the six months ended 31 December 2017.

From these reviews, FRC noted that in most cases the PIEs had not complied fully with the requirements of the following IFRSs:

1. IAS 1, Presentation of Financial Statements
2. IAS 16, Property, Plant and Equipment
3. IAS 18, Revenue
4. IAS 24, Related Parties
5. IFRS 7, Financial Instruments: Disclosures
6. IFRS 13, Fair Value Measurement

Also, FRC had identified non-compliances with the National Code of Corporate Governance (‘Code’) and taken note of explanations provided by PIEs for not complying with the Code in the following areas, as part of the full reviews of individual PIEs:

1. Composition of the Board (section 2 of the Code);
2. Detailed directors’ remuneration (section 2 of the Code);
3. Information on board committees (section 3 of the Code); and
4. Risk management (section 5 of the Code).

Details of the non-compliances identified by FRC are provided at parts A and B below.

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[**PART A – Group Reviews and Full Reviews**](#_Hlk395610325)

1. Main findings from the group reviews
   1. [Compliances with regard to International Financial Reporting Standards (IFRSs)](#OLE_LINK1)
   2. [Other issues](#Other)

1.3 [Issues raised with auditors](#Issues)

2.0 Main findings from full reviews of other individual entities

2.1 [Compliances with regard to International Financial Reporting Standards (IFRSs)](#Compliances)

* 1. [Compliances with regard to corporate governance](#OLE_LINK4)
  2. Reporting by Auditors in compliance with Section 39(3) of the FRA

2.4 [Audit and non-audit fees](#AFees)

2.5 [Non-Financial information](#NonFinancial)

2.6 [Market Capitalisation](#Market)

**[PART B - Follow up reviews of Annual Reports](#_Hlk395610500" \s "1,36264,36309,0,,PART B - Follow up reviews of an)**

**PART C - Grading of Annual Report Reviews**

**[PART D - Conclusion](#_Hlk395610793" \s "1,43050,43070,0,,PART D - Conclusion)**

**PART A – Group Reviews and Full Reviews**

**\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

* 1. **Main findings from Group Reviews**

FRC had selected 28 PIEs for group reviews. These included 8 listed entities, 2 financial institutions regulated by BOM, 8 financial institutions regulated by FSC and 10 Category 4 PIEs.

The sectors under which they operate are illustrated in the table below

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Types of PIEs** | **Sectors** | | | | | | | |
| **BIF** | **Commerce** | **Industry** | **Investment** | **Leisure & Hotels** | **Others** | **Sugar** | **Total** |
| Listed on SEM | 2 | - | - | 2 | 2 | 1 | 1 | 8 |
| Financial institutions regulated by BOM | 2 | - | - | - | - | - | - | 2 |
| Financial institutions regulated by FSC | 3 | - | - | 5 | - | - | - | 8 |
| Category 4 PIEs as per the FRA | 1 | 2 | 3 | - | 2 | - | 2 | 10 |
| **Total** | **8** | **2** | **3** | **7** | **4** | **1** | **3** | **28** |

For the purpose of this review, FRC had focused on the following areas and IFRSs relevant to the group’s businesses:

* New accounting standards
* Business combinations
* Related parties transactions
* Asset valuations
* Estimates/judgment – reasonableness
* Operating segments
* Retirement benefit obligations (Pension schemes)
* Accounting policy for revenue
* Disclosure Initiative (IAS1) – relevancy of accounting policies
* Any other material issues affecting the PIEs

Based on the focused areas identified, the following main non-compliances had been noted from the group reviews:

* 1. **Compliances with International Financial Reporting Standards (IFRSs)**

1. IAS 1, Presentation of Financial Statements

**FRC informed 9 PIEs** [3 listed (1 Investment and 2 Sugar), 3 regulated by FSC and 3 PIEs in Category 4] **within the groups** **of non-compliances in respect of the following requirements of IAS 1:**

* Accounting policies on non-current assets held for sale, deferred tax, loan, finance lease, trade receivables and financial assets;
* Description of nature of entity’s operations;
* Detailed information on trade receivables, other income and rental income;
* Disclosures on par value of shares; and
* Information on capital risk management.

1. IAS 16, Property, Plant and Equipment

**FRC observed that 4 PIEs** [3 listed (1 Leisure and Hotel, 1 Sugar and 1 Others) and 1 Category 4 PIE] **within the groups** **had not carried out the revaluation exercise of their land and buildings with sufficient regularity.**

1. IAS 18, Revenue

**FRC noted that 3 PIEs** [1 listed PIE in Investment and 2 PIEs in Category 4] **within the groups** **had not complied with the following requirements of IAS 17:**

* Accounting policies on interest income; and
* Disclosures of the category of revenue recognised during the year.

1. IAS 19, Employee Benefits

**FRC informed 5 PIEs** [3 listed PIEs (1 Leisure & Hotels, 1 Sugar and 1 Others) and 2 PIEs in Category 4] **within groups that they had not provided a description of the risks to which they were exposed through their defined benefit pension plans.**

1. IAS 24, Related Parties

**FRC informed 6 PIEs in the groups** [1 listed in Others, 1 regulated by FSC and 4 PIEs in Category 4] **of issues relating to IAS 24 requirements:**

* Classification of key management compensation;
  + Terms and conditions of related parties’ outstanding balances including whether they are secured, and the nature of consideration to be provided in settlement; and
  + Information about related party transactions and outstanding balances.

1. IFRS 7, Financial Instruments: Disclosures

**FRC informed 3 PIEs** [1 listed in BIF and 2 regulated by FSC] **within the groups, of their non-compliances with the following requirements of IFRS 7**:

* Information on Cash Flow Hedges;
* Accounting policy on financial assets at fair value through profit or loss; and
* Disclosure on fair value of 'loans and receivables' and 'held-to-maturity financial assets’.

(g) IFRS 13, Fair Value Measurement

**During the group reviews of 10 PIEs** [4 listed (1 Industry, 1 Leisure & Hotel, 1 Others and 1 Sugar), 1 regulated by BOM, 3 regulated by FSC and 2 PIEs in Category 4]**, FRC identified issues which related to the following requirements of IFRS 13:**

* The level of the fair value hierarchy within which the fair value measurements of assets and liabilities are categorised in their entirety; and
* Description of the valuation technique(s) and the inputs used in fair value measurement.

* 1. **Issues raised with auditors**

FRC also monitored the services provided by the auditors as well as other issues involving the work of the auditor.

**During the course of its review, FRC informed the auditors of 4 PIEs** **within the groups** [2 listed (1 BIF and 1 Others) and 2 Category 4 PIEs] **of the following issues:**

1. Provision of other services

1 listed in BIF within the groups had provided other services which may impinge on the independence of its auditor.

1. Going concern risk

3 PIEs [2 listed (1 BIF and 1 Others) and 1 Category 4 PIE] in the groups had indicators of going concern risks that may cast doubt on the entities’ ability to continue as a going concern.

1. **Main findings from Full Reviews of individual entities**

With respect to the 13 individual PIEs reviewed, FRC identified issues relating to the following areas of corporate reporting during the six months ended 31 December 2017:

* 1. **Compliances with International Financial Reporting Standards (IFRSs)**

1. IAS 19, Employee Benefits

**With regard to IAS 19, FRC queried 3 PIEs** [1 listed in Industry and 2 Category 4 PIEs] **in respect of the following:**

* Description of risks to which the entities were exposed through their defined benefit plans;
* Amount recognised as an expense for defined contribution plans; and
* Description of any funding arrangements and funding policy that affect future contributions, the expected contributions to the plans for the next annual reporting period.

1. IFRS 7, Financial Instruments: Disclosures

**From the review exercise, FRC observed that 2 PIEs** [1 regulated by FSC and 1 Category 4 PIE] **had partly complied with IFRS 7.**

The following disclosures as per IFRS 7 were found missing:

* Management of financial risks;
* Information on credit risk;
* An analysis of the age of financial assets that are past due as at the end of the reporting period but not impaired; and
* Fair value and terms and conditions of collaterals.
  1. **Compliances with corporate governance**

The National Code of Corporate Governance aims at establishing principles for good corporate governance leading to transparency, accountability and a long-term perspective.

Section 75(2) of the FRA stipulates that every PIE shall adopt corporate governance in accordance with the Code of Corporate Governance (‘Code’). The ‘comply or explain’ principle forms the basis of this Code. Through this principle, companies that depart from the relevant corporate Governance Code are required to explain in their corporate governance statements which parts of the Code they depart from and the reasons for doing so.

From the annual report review of the 13 individual entities, FRC noted that all these entities had submitted a corporate governance report.

Out of the above 13 PIEs, 2 PIEs had partly complied with the Code. The non-compliances raised for those PIEs that had partial compliances, related to the following:

1. Requirement of having a non-executive (independent) chairpersons on the Board of directors (part (a)(iii) below also refers); and
2. Risk management (part (d) below also refers).
3. Information on the Board of Directors

As per the Code of Corporate Governance of Mauritius, a company should have appropriate balance of executive, non-executive and independent directors. The chairperson should also be a non-executive director. This enables the company to make sound decision with competent and independent board members having proper level of qualifications and experience.

During the course of the annual report reviews, FRC noted the following in respect of board composition:

1. Minimum requirement of having at least 2 independent directors on the board of directors

As depicted in table below, out of the 13 individual PIEs, 12 entities had at least 2 independent directors on their boards in line with section 2.2.2 of the Code of Corporate Governance. The remaining entity explained the reason for not having independent directors.

|  |  |  |  |
| --- | --- | --- | --- |
| **PIEs** | **Section 2.2.2** | | |
| **Met the requirement that all companies should have at least two independent directors on their boards** | **Explanations provided for not meeting the requirement of the Code** | **Total** |
| Listed on SEM | 8 | - | **8** |
| Financial institutions regulated by BOM | 2 | - | **2** |
| Financial institutions regulated by FSC | 1 | - | **1** |
| Category 4 PIEs as per the FRA | 1 | 1 | **2** |
| **Total** | **12** | **1** | **13** |

The explanation provided by the PIE that did not meet the requirement of having at least 2 independent directors was that the current board composition was considered appropriate for the company given that the latter had no operations and it solely derived its income from dividend.

1. The minimum requirement of having 2 executive directors in the board of directors

The table below indicates the level of compliance with the minimum requirement of having 2 executive directors in the boards.

|  |  |  |  |
| --- | --- | --- | --- |
| **PIEs** | **Section 2.2.3** | | |
| **Met the requirement that all companies should have at least two executive directors on their boards** | **Explanations provided for not meeting the requirement of the Code** | **Total** |
| Listed on SEM | 4 | 3 | **7** |
| Financial institutions regulated by BOM | 1 | 1 | **2** |
| Financial institutions regulated by FSC | 1 | - | **1** |
| Category 4 PIEs as per the FRA | 1 | 2 | **3** |
| **Total** | **7** | **6** | **13** |

6 out of the 13 PIEs met the minimum requirement of having 2 executive directors on board as per the Code of Corporate Governance. The remaining explained the reasons for not having executive directors on their boards.

The explanations provided by the PIEs are described below:

* The Board was of view that given the small size of the Company and the Board, most Corporate Governance and other functions could be discharged by the Board of Directors as a unit and that the composition of the Board included members with appropriate experiences.
* The Board was of the view that the active participation of the General Manager at all Board meetings and the participation of senior executives to sub-committees of the Board met with the spirit of the Code of Corporate Governance for Mauritius.
* The Board believed that the involvement of senior executives at the level of Board sub committees and management committees satisfied the requirements of interactions at decisional level.
* The Board of the company considered that the current board composition was appropriate for the company given it had no operations and it solely derived its income from dividend.

1. Requirement of having a non-executive (independent) chairperson on the Board of directors

As illustrated in the table below, most PIEs had non-executive (independent) chairpersons on their Boards. Only 1 listed PIE had not complied with this requirement of the Code as it had a chairperson who was also an executive director during the period under review.

|  |  |  |  |
| --- | --- | --- | --- |
| **PIEs** | **Section 2.5.5** | | |
| **Met the requirement that all companies should have non-executive (independent) chairpersons on their boards** | **Not met the requirement that all companies should have non-executive (independent) chairpersons on their boards and no explanations provided** | **Total** |
| Listed on SEM | 7 | 1 | **8** |
| Financial institutions regulated by BOM | 2 | - | **2** |
| Financial institutions regulated by FSC | 1 | - | **1** |
| Category 4 PIEs as per the FRA | 2 | - | **2** |
| **Total** | **12** | **1** | **13** |

1. Information on Board Committees

Board committees are a mechanism to assist the board and its directors in discharging their duties through a more comprehensive evaluation of specific issues. As per the Code of Corporate Governance, all companies should have, at a minimum, an audit committee and a corporate governance committee except for, subsidiary companies which would not be expected to have separate sets of board committees.

From the table below, 10 out of 13 PIEs had at a minimum an audit committee and a corporate governance committee as per section 3 of the Code. The remaining 3 PIEs provided explanations for not complying with this requirement.

|  |  |  |  |
| --- | --- | --- | --- |
| **PIEs** | **Section 3** | | |
| **Met the requirement that all companies should have, at a minimum, an audit committee and a corporate governance committee** | **Explanations provided for not meeting the requirement of the Code** | **Total** |
| Listed on SEM | 7 | 1 | **8** |
| Financial institutions regulated by BOM | 1 | 1 | **2** |
| Financial institutions regulated by FSC | 1 | - | **1** |
| Category 4 PIEs as per the FRA | 1 | 1 | **2** |
| **Total** | **10** | **3** | **13** |

The 3 PIEs explained the following:

* All corporate governance matters were taken up at board level.
* The Board was of the opinion that given the small size of the company and the Board, most corporate governance and other functions had been discharged by the Board of Directors as a unit and that the composition of the Board included members with appropriate experiences.
* The corporate governance matters had been dealt with by the Corporate Governance’s committee set up at subsidiary level whilst the audit function had been taken up at Board level.

1. Detailed directors’ remuneration

Disclosures on directors’ remuneration provide a control mechanism that seeks to ensure that there is alignment of directors’ interests with that of shareholders. The table below indicates the level of compliance in respect of individual remuneration of directors.

|  |  |  |  |
| --- | --- | --- | --- |
| **PIEs** | **Section 2.8.2** | | |
| **Met the requirement to disclose individual remuneration of directors** | **Explanations provided for not meeting the requirement of the Code** | **Total** |
| Listed on SEM | 6 | 2 | **8** |
| Financial institutions Regulated by BOM | 2 | - | **2** |
| Financial institutions regulated by FSC | 1 | - | **1** |
| Category 4 PIEs as per the FRA | 2 | - | **2** |
| **Total** | **11** | **2** | **13** |

From the above, it is noted that the majority of PIEs either disclose individual remuneration of directors or explain the reason for not disclosing information on individual remuneration of directors.

2 PIEs provided explanations for not disclosing detailed remuneration of directors on an individual basis. These PIEs explained that the directors' fees and remuneration were sensitive information in the competitive market.

1. Risk management

Risk management reduces the probability that the attainment of an organisation’s objectives are jeopardised by unforeseen events. It ensures that management is capable of identifying circumstances which represent an opportunity or can be turned to competitive advantage. The operation of controls and internal audit form part of the process of risk management

The table below shows details of the PIEs complying with this section of the Code of corporate governance.

|  |  |  |  |
| --- | --- | --- | --- |
| **PIEs** | **Sections 5.1.7 / 8.4** | | |
| **Met the requirement that companies should disclose consideration and management of key risks** | **Not met the requirement on consideration and management of key risks** | **Total** |
| Listed on SEM | 6 | 1 | **7** |
| Financial institutions regulated by BOM | 1 | - | 1 |
| Financial institutions regulated by FSC | 2 | - | 2 |
| Category 4 PIEs as per the FRA | 3 | - | **3** |
| **Total** | **12** | **1** | **13** |

As shown in the table above, FRC noted that 12 out of the 13 PIEs reviewed, had reported on consideration and management of key risks. Only one PIE had not met this requirement.

* 1. **Reporting by Auditors in compliance with Section 39(3) of the FRA**

Section 39(3) of the FRA requires an auditor to report whether the disclosures made in the corporate governance report are consistent with the Code. The format of this report on corporate governance by auditors is laid out in the Guidelines on compliance with corporate governance – Government Gazette No. 64 of 20 July 2013, General Notice No. 1819.

**It was good to note that the auditors of the 13 PactIEs reviewed had reported on the consistency of the requirements of the Code.**

* 1. **Audit and non-audit fees**

From the annual report reviews, FRC observed that some licensed auditors had provided non-audit services to PIEs such as tax services.

In accordance with legal requirements and under the Code of Corporate Governance, PIEs are required to disclose the following information for the non-audit services rendered by their external auditors in their annual reports:

1. Separate disclosure of the amount paid for non-audit services as opposed to audit services (section 221 of the Companies Act 2001 *Contents of annual report* refers).
2. Description of non-audit services rendered by the external auditor in their annual reports stating particulars of the nature of the services and amounts paid for each nature of services.

With respect to audit and non-audit fees, the following observations were made for the 13 reviews:

* **7 PIEs** [4 listed (3 Industry and 1 Investment), 2 regulated by BOM and 1 PIE in Category 4] **had paid fees for audit services only.**
* **6 PIEs** [3 listed (1 Industry, 1 Leisure & Hotel and 1 Transport), 1 PIE regulated by FSC and 2 PIEs in Category 4] **had disclosed fees paid for audit services as well as ‘other services’ provided by the same firms of external auditors. The ‘other services’ rendered by the auditors consisted mainly of taxation services.**

* 1. **[Non-financial information](#Non)**

A good annual report always addresses all the required relevant information in respect of the entities’ activities, objectives and strategic plans, firms’ values and principles, factors affecting its environment and its performance.

From the 13 annual reports reviewed, FRC made the following observations:

* 31% of companies discussed their corporate strategies
* 31% of the entities made disclosures regarding their business objectives;
* 31% of firms discussed values and principles;
* 85% of the PIEs provided a description of their businesses and scope; and
* 15% mentioned the external forces affecting the entities such as customer, suppliers and competitors

FRC encourages PIEs to report on relevant non-financial information which will help users of accounts to interpret the financial information provided in the annual reports.

* 1. **Market Capitalisation**

Market capitalisation is calculated by multiplying a company's shares outstanding by the current market price of one share. This figure is used to determine a company's size, provides an indication of its value and its net worth.

From the review of the individual entities, FRC noted that 7 listed companies had market capitalisation which approximately totalled Rs 3,907,723,500 for the six months ended 31 December 2017.

The PIEs with the highest market capitalisation were involved in industry and transport. The PIEs with the lowest market capitalisation were engaged in industry and leisure & hotels.

**PART** **B - Follow up reviews of Annual Reports**

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As mentioned above, FRC has carried out 5 follow up reviews for the six months ended 31 December 2017. During these follow-up reviews, FRC considered whether the issues previously raised in previous full annual report reviews had been properly addressed in the PIEs’ latest annual reports and whether there are still recurrent issues from previous reviews. This would ensure that PIEs had taken corrective actions subsequent to FRC’s previous letters of observations.

From the follow up review exercise, FRC observed the following issues:

1. Recurrent non-compliances

**1 PIE** **in Category 4 had not properly addressed the following IFRS issues in its annual report:**

* Amount of inventories recognised as expense (IAS 2).
* Reconciliation of the summarised financial information to the carrying amount of its interest in associate (IFRS 12).

1. Other non-compliances arising from the follow-up reviews

**FRC informed 4 PIEs** [2 listed (1 BIF and 1 Leisure & Hotels) and 2 PIEs in Category 4] **of the following new IFRS issues arising from their follow up reviews:**

* Description of risks to which the entities’ defined benefit plans are exposed (IAS 19).
* General description of the lessee’s material leasing arrangements including the existence and terms of renewal or purchase options and escalation clauses (IAS 17).
* Presentation of EPS on the face of statement of comprehensive income (IAS 33).
* The level of the fair value hierarchy within which the fair value measurements of assets are categorised (IFRS 13).

**PART C - Grading of Annual Report Reviews**

**\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

As part of the review process, FRC assigns grades to PIEs which provide guidance to categorise the quality of reporting by PIEs. Grades are assigned to the PIEs after considering the comments from the PIEs on the findings of the reviews. Out of the 46 annual reports reviewed (41 group reviews and full reviews and 5 follow-up reviews), FRC had graded the quality of the 42 annual reports reviewed (38 group and full reviews and 4 follow up reviews) for the six months ended 31 December 2017.

The grading allocated to the PIEs was based on the following four levels:

* Good (Grade 1)
* Acceptable with limited improvements required (Grade 2A)
* Acceptable overall with improvements required (Grade 2B)
* Significant improvements required (Grade 3)

The grades of the annual report review were determined mainly by the nature of non-compliances raised with respect to IFRS, auditors’ report, corporate governance and other issues arising such as non-compliances with regulations, going concern problem and independence of auditors amongst others. This would highlight areas in which there is room for improvement and helps drive quality reporting.

For the 42 PIEs which were graded, FRC noted that:

* 13 PIEs received a grade 1;
* 25 PIEs were granted a grade of 2A; and
* 4 PIEs had obtained grade 2B.

Those with grade 2A have no significant non-compliances whilst those having grade 2B had various non-compliances.

The table below shows an analysis of the grading obtained by types of PIEs.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Types of PIEs** | **Full Reviews** | | | **Follow-up Review** | **Total** |
| **Grade 1** | **Grade 2A** | **Grade 2B** | **Grade 2A** |  |
| Listed on SEM | 6 | 8 | 1 | 1 | **16** |
| Regulated by BOM | 1 | 2 | - | - | **3** |
| Regulated by FSC | 3 | 4 | 2 | - | **9** |
| Category 4 PIEs as per the FRA | 3 | 7 | 1 | 3 | **14** |
| **Total** | **13** | **21** | **4** | **4** | **42** |

**PART D -** **Conclusion**

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From the annual report reviews, FRC noted that most PIEs responded well to issues previously raised and made improvements to the disclosures in their annual reports.

FRC expects the PIEs to cooperate with FRC to ensure that there is continuing improvement in the quality of financial reporting.

Also, PIEs are advised to provide qualitative disclosures regarding the impact of newly applicable IFRSs and regulations in their forthcoming annual reports.

**Financial Reporting Council**

**February 2018**

1. ‘*Category 4 PIEs’ comprises any company or group of companies having, during 2 consecutive preceding years, at least 2 of the following –*

   * *an annual revenue exceeding 200 million rupees;*
   * *total assets value exceeding 500 million rupees;*
   * *a number of employees exceeding 50.*

   *The definition of PIE under this category has been amended through Regulations published in Government Gazette No 105 of 3 December 2016 which is effective as from July 2017.* [↑](#footnote-ref-1)