

The United Kingdom Directors' Remuneration Report Regulations 2002

Bulletin 2002/2

This Bulletin includes updated examples of:

- an auditors' report; and
- a statement on the summary financial statement,

for a quoted company incorporated in Great Britain reflecting the requirements of the Directors' Remuneration Report Regulations 2002.

October 2002

THE AUDITING PRACTICES BOARD

Independent Regulation of the Accountancy Profession

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THE AUDITING PRACTICES BOARD
THE UNITED KINGDOM DIRECTORS'
REMUNERATION REPORT REGULATIONS 2002

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Introduction

1. With effect from 1 August 2002 the United Kingdom Government brought into force 'The Directors' Remuneration Report Regulations 2002'¹ (the Regulations) which will be effective for financial years ending on or after 31 December 2002². These Regulations require 'quoted companies' to prepare a Directors' Remuneration Report, for each financial year, that contains specified information, some of which is required to be audited.

The Directors' Remuneration Report

2. The directors of a 'quoted company' are required to produce for each financial year a Directors' Remuneration Report which is required to be approved by the board of directors and signed on behalf of the directors by a director or the secretary of the company. The required content of the Directors' Remuneration Report is set out in Schedule 7A to the Companies Act 1985 (the Act).
3. A 'quoted company' is defined as a company incorporated under the Act:
 - whose equity share capital has been included in the official list; or which
 - is officially listed in an EEA³ State; or which
 - is admitted to dealing on either the New York Stock Exchange or the exchange known as Nasdaq.

The definition does not include companies that have been admitted to trading on the Alternative Investment Market (AIM).

Requirements of Schedule 6 to the Companies Act 1985

4. Schedule 6 to the Act requires a company to produce certain information concerning directors' remuneration by way of notes to the company's financial statements. The Regulations exempt a quoted company from disclosing the information specified in paragraphs 2 to 14 in Part I of Schedule 6. A quoted company is, however, required to disclose the information specified in paragraph 1 in Part I of Schedule 6 in the notes to the company's financial statements.
5. Part I of Schedule 6 will continue to apply in its entirety to companies which are not quoted and Parts II and III of that Schedule will apply to both quoted and unquoted companies.
6. The table set out below shows which of the requirements of Schedules 6 and 7A apply to quoted and unquoted companies respectively and the requirements with respect to audit.

¹ These Regulations are set out in Statutory Instrument 2002 No. 1986 which can be downloaded from <http://www.legislation.hmso.gov.uk/si/si2002/20021986.htm>

² SI 2002/1986 applies to companies incorporated in Great Britain. Northern Ireland is responsible for its own companies legislation and it is expected that in due course the Companies (Northern Ireland) Order 1986 will be amended to introduce the same requirements as those set out in the Regulations

³ EEA is the European Economic Area

Requirement	Quoted companies	Unquoted Companies	Required to be Audited
Schedule 6 to the Companies Act 1985 Disclosure of Information: Emoluments and other Benefits of Directors and others (These disclosures are required to be made in the notes to the financial statements)			
Part I, paragraph 1	✓	✓	✓
Part I, paragraphs 2-14		✓	✓
Part II	✓	✓	✓
Part III	✓	✓	✓
Schedule 7A to the Companies Act 1985 Directors' Remuneration Report (These disclosures are required to be made in the Directors' Remuneration Report)			
Part 2 (relating to information about remuneration committees, performance related remuneration and liabilities in respect of directors' contracts)	✓		
Part 3 (relating to detailed information about directors' remuneration)	✓		✓

Requirements of auditors

7. In addition to reporting on the financial statements, the company's auditors are required, through an amendment to Section 235 of the Act, to report to the company's members as to whether the 'auditable part' of the Directors' Remuneration Report has been properly prepared in accordance with the Companies Act 1985. The 'auditable part' of the Directors' Remuneration Report is the part which contains the information required by Part 3 of Schedule 7A.
8. The auditors are also required to carry out such investigations as will enable them to form an opinion as to whether the auditable part of the Directors' Remuneration Report is in agreement with the accounting records and returns.
9. To the extent that the requirements of Schedule 6 or Part 3 of Schedule 7A are not complied with, the auditors are required to include in their report, so far as they are reasonably able to do so, a statement giving the required particulars.

Reporting on the Directors' Remuneration Report

10. The auditors have to report on the Directors' Remuneration Report within their report on the financial statements. To communicate the opinion required of the auditors in the most effective way the APB recommends that the opinion paragraph of the auditors' report for quoted companies be drafted along the following lines:

In our opinion:

- the financial statements give a true and fair view of the state of the [group's and the] company's affairs as at ... and of [the group's] [its] profit [loss] for the year then ended; and
- the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985.

11. An illustration of an auditors' report for a quoted company incorporated in Great Britain is set out in Appendix 1. In Appendix 1 the changes that need to be made to the example auditors' report illustrated in Appendix 1 to Bulletin 2001/2 are shown as marked up text.
12. As the auditors are not required to audit all of the information contained in the Directors' Remuneration Report they will need, in their report, to describe accurately which elements of the Directors' Remuneration Report they have audited.
13. Companies, therefore, need to make the disclosures that are required to be audited in such a way that it is clear which elements have been audited. One way of doing this would be for the audited disclosures to be set out in a discrete section under a suitable heading such as 'audited information'.
14. It would be unsatisfactory for auditors, in their report, to describe what they have audited in an uninformative manner such as 'the disclosures required by Part 3 of Schedule 7A to the Companies Act' as this would require readers of the auditors' report to have a detailed knowledge of the requirements.
15. The auditors assess whether the scope of their audit will be capable of being clearly described. If this cannot be achieved to their satisfaction by cross-reference, they set out the particulars that have been audited within the auditors' report.
16. The auditors make arrangements with the directors, well in advance of the year end, to ensure that the audited disclosures will be clearly distinguished from those that have not been audited. Illustrative terms of engagement are set out in Appendix 2 to this Bulletin.

Difference between the disclosures required by Schedule 6 and Schedule 7A

17. As described above the Regulations will continue to apply paragraph 1 of Schedule 6 to the Act to quoted companies. The consequence of this will be that the financial statements of quoted companies will disclose aggregate directors' emoluments that may differ from the aggregate directors' remuneration disclosed in the Directors' Remuneration Report. This arises because the Act's definition of 'emoluments' differs from its definition of 'remuneration'.

18. Both of these disclosures will be reported on by the auditors. Where both disclosures have been prepared in accordance with the relevant requirements of the Act any difference between the disclosures is not an ‘inconsistency’⁴ between the financial statements and the information in the Directors’ Remuneration Report. Where the difference between the disclosures of directors’ emoluments and remuneration are material the auditors encourage the directors to provide an explanation of the difference.

Disclosure requirements in the Listing Rules

19. Following the introduction of the Regulations the APB understands that the United Kingdom Listing Authority (the UKLA) is aware that a certain level of duplication exists between the requirements of the Regulations and the requirements of Listing Rule 12.43A (c) relating to directors’ remuneration. The UKLA is currently considering the most appropriate way of addressing this issue.
20. In the meantime additional care will need to be taken when auditing the disclosure of directors’ remuneration. This is because not all of the requirements of Listing Rule 12.43A (c) are duplicated in the Regulations.

The auditors’ responsibilities with respect to the unaudited part of the Directors’ Remuneration Report

21. Although the Regulations do not require the Directors’ Remuneration Report to be included in the Annual Report it is likely that many quoted companies will continue their practice of including directors’ remuneration disclosures in the Annual Report. As the information given in Part 2 of the Directors’ Remuneration Report is neither required to be audited nor reviewed by the auditors it constitutes ‘other information’. Statement of Auditing Standards 160 ‘Other information in documents containing audited financial statements’ requires auditors to read such ‘other information’ and if they become aware of any apparent misstatements or identify material inconsistencies with the financial statements to seek to resolve them.

Issuing the Directors’ Remuneration Report as a separate document

22. If a quoted company issues its Directors’ Remuneration Report as a separate document the scope of the auditors’ report included in the Annual Report will, nevertheless, be required to encompass the auditable part of the Directors’ Remuneration Report. For this reason, the requirements of SAS 160 apply to the content of a separate Directors’ Remuneration Report, notwithstanding the fact that the Report is not included in a document containing audited financial statements.
23. When the Directors’ Remuneration Report is issued as a separate document, although not required by the Act, the auditors:
- when their report is unqualified, encourage the directors to indicate within the Directors’ Remuneration Report where the auditors’ report, prepared in

⁴ SAS 160 ‘Other information in documents containing audited financial statements (Revised) at SAS 160.1 requires: **Auditors should read the other information. If as a result they ...identify any material inconsistency with the audited financial statements, they should seek to resolve them’.**

accordance with Section 235 of the Act, may be found; or

- when their report expresses either a qualified or adverse opinion or disclaims an opinion, which is relevant to the Directors' Remuneration Report, require the directors to reproduce the relevant parts of the auditors' report as part of the Directors' Remuneration Report. In the event that the directors do not agree to do so, the auditors consider whether to resign.

The auditors' statement on the Summary Financial Statement

24. Following the introduction of the Regulations the Government has amended the Companies (Summary Financial Statement) Regulations 1995⁵ to expand the disclosure required in a Summary Financial Statement in relation to directors' remuneration.
25. Certain of the companies which are permitted under section 251 of the Act to produce a Summary Financial Statement will fall within the category of companies required to produce a Directors' Remuneration Report (ie quoted companies). Such companies that prepare summarised financial statements will be required to include either the whole, or a summary, of certain information concerning directors' remuneration contained in the notes to the financial statements and in the Directors' Remuneration Report.
26. The relevant information is the aggregate amount of directors' emoluments (from the notes to the company's financial statements)⁶, a statement of the company's policy on directors' remuneration for the next following financial year and the performance graph (the last two items are required by the Regulations but are not required to be audited).
27. These requirements apply to companies and groups, whether or not they are banking or insurance companies and groups.
28. A revised illustrative example of the 'Auditors' Statement on the Summary Financial Statement' reflecting the requirements of the amended Companies (Summary Financial Statement) Regulations is set out as Appendix 3 to this Bulletin. In Appendix 3 the changes that need to be made to the example Statement on the summary financial statement illustrated in Appendix 5 to Bulletin 2001/2 are shown as marked up text.

Superseded guidance

29. With the publication of this Bulletin the following guidance issued by the APB is withdrawn:
 - Bulletin 1999/5 - Appendix 3
 - Bulletin 2001/2 - Appendices 1 and 5

⁵ These amendments are set out in Statutory Instrument 2002 No. 1780 which can be downloaded from <http://www.legislation.hmso.gov.uk/si/si2002/20021780.htm>

⁶ This is a summary of all the information required by paragraph 1(1) of Part I to Schedule 6 to the Act

ILLUSTRATIVE AUDITORS' REPORT FOR A QUOTED COMPANY INCORPORATED IN GREAT BRITAIN

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF XYZ PLC

We have audited the financial statements of (name of entity) for the year ended ... which comprise [state the primary financial statements such as the Profit and Loss Account, the Balance Sheet, the Cash Flow Statement, the Statement of Total Recognised Gains and Losses] and the related notes⁷. These financial statements have been prepared under the historical cost convention [as modified by the revaluation of certain fixed assets] and the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.⁸

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the financial statements in accordance with applicable law and United Kingdom Accounting Standards are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements, and United Kingdom Auditing Standards ~~and the Listing Rules of the Financial Services Authority~~.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Directors' Remuneration Report to be audited have been~~are~~ properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law ~~or the Listing Rules~~ regarding directors' remuneration and transactions with the company [and other members of the group] is not disclosed.

We review whether the Corporate Governance Statement reflects the company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules of the Financial Services Authority⁹, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the

⁷ Auditors' reports of entities that do not publish their financial statements on a web site or publish them using 'PDF' format may continue to refer to the financial statements by reference to page numbers.

⁸ Part 3 of Schedule 7A to the Companies Act 1985 sets out the information in the Directors' Remuneration Report that is subject to audit. Companies should describe clearly which disclosures within the Directors' Report have been audited.

⁹ The expression 'the Listing Rules of the United Kingdom Listing Authority' may also be used.

[company's] [group's] corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises only [the Directors' Report, [the unaudited part of the Directors' Remuneration Report](#), the Chairman's Statement, the Operating and Financial Review and the Corporate Governance Statement]¹⁰. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements [and the part of the Directors' Remuneration Report to be audited](#). It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate in the company's circumstances consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements [and the part of the Directors' Remuneration Report to be audited](#) are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements [and the part of the Directors' Remuneration Report to be audited](#).

Opinion

In our opinion:

- [the financial statements give a true and fair view of the state of the \[group's and the\] company's affairs as at ... and of \[the group's\] \[its\] profit \[loss\] for the year then ended;](#) and
- [the financial statements and the part of the Directors' Remuneration Report to be audited](#) have been properly prepared in accordance with the Companies Act 1985.

Registered auditors

Address

Date

The changes shown as marked up text show the changes that need to be made to the example auditors' report illustrated in Appendix 1 to Bulletin 2001/2

¹⁰ The other information that is 'read' is the content of the printed Annual Report other than the financial statements [and the part of the Directors' Remuneration Report to be audited](#). The description of the information that has been read is tailored to reflect the terms used in the Annual Report. [\(See also paragraphs 22 to 23 of this Bulletin for guidance when the Directors' Remuneration Report is issued as a separate document\)](#)

ILLUSTRATIVE TERMS OF ENGAGEMENT FOR A QUOTED COMPANY

Audit of directors' remuneration disclosures

The disclosures that quoted companies are required to make with respect to directors' remuneration are specified in:

- paragraph 1 in Part I of Schedule 6 to the Companies Act 1985; and
- Schedule 7A to the Companies Act 1985.

The disclosures specified by paragraph 1 of Part 1 of Schedule 6 are required to be given in notes to the annual accounts whereas the disclosures specified by Schedule 7A are required to be given in the Directors' Remuneration Report¹¹.

With respect to the disclosures specified by Schedule 7A we are only required to report on that part of the Directors' Remuneration Report which contains the information required by Part 3 of that Schedule. You have agreed that the disclosures in the Directors' Remuneration Report that are required to be audited will be clearly and unambiguously identified as such. If the disclosures are not capable of being clearly described to our satisfaction we will need to set out all the particulars that we have audited within the auditors' report.

The Companies Act requires that we include in our report any required particulars omitted by the directors if we are reasonably able to do so.

¹¹ Unquoted companies are required to make the disclosures specified by the whole of Part 1 of Schedule 6 of the Companies Act 1985 in the notes to the annual accounts. Schedule 7A does not apply to unquoted companies.

ILLUSTRATIVE STATEMENT ON THE SUMMARY FINANCIAL STATEMENT OF A QUOTED COMPANY INCORPORATED IN GREAT BRITAIN

INDEPENDENT AUDITORS' STATEMENT TO THE SHAREHOLDERS OF XYZ PLC

We have examined the summary financial statement of (name of entity)¹².

Respective responsibilities of directors and auditors

The directors are responsible for preparing the [*summarised Annual Report*] in accordance with applicable law.

Our responsibility is to report to you our opinion on the consistency of the summary financial statement within the [*summarised Annual Report*] with the full annual accounts, ~~and~~ the Directors' Report and the Directors' Remuneration Report, and its compliance with the relevant requirements of section 251 of the Companies Act 1985 and the regulations made thereunder. We also read the other information contained in the [*summarised Annual Report*] and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the summary financial statement.

Basis of opinion

We conducted our work in accordance with Bulletin 1999/6 'The auditors' statement on the summary financial statement' issued by the Auditing Practices Board for use in the United Kingdom.

Opinion

In our opinion the summary financial statement is consistent with the full annual accounts, ~~and~~ the Directors' Report and the Directors' Remuneration Report of XYZ plc for the year ended ... and complies with the applicable requirements of Section 251 of the Companies Act 1985 and the regulations made thereunder.

Registered auditors
Address

Date

The changes shown as marked up text show the changes that need to be made to the example Statement on the summary financial statement illustrated in Appendix 5 to Bulletin 2001/2

¹² Auditors' reports of entities that do not publish their summarised financial statements on a web site or publish them using 'PDF' format may continue to refer to the summarised financial statements by page number

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