

Welcome

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Technical update for NEDs and Audit Committee members January 2025





Priorities for 2024/25 reporting



Upcoming changes to FRS 102



2024 UK Corporate Governance Code



Sustainability reporting update



IFRS 18 accounting standard



Other developments and consultations



Q&A

Priorities

for

2024/2025

reporting

Priority areas from FRC annual reviews

CRRT letters: questions on front half

- Fair, balanced and comprehensive strategic reports, including:
 - issues not discussed;
 - o prominence of APMs; and
 - undue focus on particular aspects of business.
- TCFD and climate change
 - issues with LR statement of consistency;
 - challenges on underlying consistency with TCFD;
 - potential inconsistency with financial statements (e.g. impairment notes); and
 - greenwashing.

Corporate governance reporting review

- Large fall in the number of companies explaining departures from Code provisions (72% of the companies looked at reported full compliance, up from 37%).
- Still areas of non-compliance, but that is the intention of the Code:
 - Status and tenure of chair.
- Quality of explanations is still key.

"Without context, it is almost impossible to support ... an explanation... [I]t may be difficult to understand why the company has selected non-compliance with the Code, and it may fail to persuade the readers ... that this is necessary or beneficial for the company".

Specific areas to focus on include:

- Culture, purpose and values, including their link to strategy and the outcomes they create through the actions of the board.
- Engagement with shareholders and other stakeholders, especially outcomes.
- Clarity on matters such as overboarding and diversity policy (what it covers, objectives and targets and progress on them).
- Viability, given withdrawal of resilience statement.

FRC annual review of corporate reporting 23/24



Overall observations



Top issues and findings



Expectations

Quality of FTSE 350 maintained, but a widening gap between other companies

Impairment

Stand back to ensure a consistent and coherent story throughout the annual report

Inconsistencies within the annual report are the main reason for FRC inquiry

Cash flow statements

Pre-issuance checks to review common challenges

2024/25 reporting season - not a year of change

But look out for...

- Non-financial and sustainability information statement (UK incorporated).
- FRC Audit Committees
 Minimum Standard
 (FTSE 350).
- Changes to Listing Rule references.

... and private company governance reporting

Reminder of thresholds:

EITHER:

2,000 employees

OR

£200m turnover and £2bn B/S assets

Looks to be significant under-reporting in this area.

FRC Review of reporting against the Wates Principles (Aug 2024)

"Of the 1,812 companies that were analysed, 1,237 companies discussed their corporate governance practices within a specific corporate governance statement... The remaining 562 companies did not provide any information about their corporate governance arrangements although they were deemed likely to fall within the scope of the Regulation".

Other focus areas for December 2024 year end reporting

1

Offsetting (or netting) in the financial statements

2

Structured entities unconsolidated SPEs might exist that should be consolidated 3

Classification of liabilities as current or non-current and with covenants (IAS 1)

4

Fair value measurement and disclosure of recurring Level 3 measurements

Upcoming changes

to FRS 102

Overview

FRC issued comprehensive improvements to FRS 102 in March 2024.



The amendments to the standards will in most cases be effective for accounting periods beginning on or after 1 January 2026.



The most significant changes apply to leases and revenue recognition to align with the international financial reporting standards.

Section 20: Leases

Key changes

FRS 102 no longer distinguishes between operating and finance leases for lessees. Therefore, more leases will be required to be recognised on-balance sheet with an asset and liability.

Exemptions will be permitted for short-term leases and leases of low-value assets.

Simplifications compared to IFRS 16

- More leases will meet the definition of low-value than under IFRS 16.
- Additional discount rate option: lessee's obtainable borrowing rate.
- Reducing the number of situations in which a lease modification requires the determination of a revised discount rate.
- Offering the option of a simpler approach to recognising gains and losses on sale and leaseback transactions, similar to the approach in the previous edition of FRS 102.

Transition

- Comparative periods shall not be restated.
- An IFRS group reporter is permitted to measure lease liabilities and right-of-use assets on initial application at the value used for IFRS 16 for group reporting.
- Otherwise, on initial application:
 - Measure the lease liability using the discount rate on the date of initial application; and
 - Measure the right-of-use asset equal to the lease liability on transition.



Key practical implementation challenges

Identifying all leases

→ and locating the contracts!

Systems set up

→ lease accounting software vs inhouse solutions

Establishing discount rate

→ remember there is an additional, simpler, option under FRS 102, but it still

Establishing lease terms

→ more rigour needed than for off balance sheet operating leases

Potential effect on covenants

→ are they based on frozen GAAP?

Section 23: Revenue from contracts with customers

Key changes

Introduces a single comprehensive five-step model for revenue recognition for all contracts with customers

Based on identifying the distinct goods or services promised to the customer and the amount of consideration to which the entity will be entitled in exchange.

More guidance including:

- variable consideration;
- licensing;
- contract modifications; and
- payments to customers.

Simplifications compared to IFRS 15

- no adjustments required for the effects of time value of money on payments received in advance;
- flexibility in allocating discounts or variable consideration;
- a policy choice on whether an entity capitalises its costs to obtain a contract with a customer; and
- less disclosure requirements.

Transition

An entity can either:

- apply fully retrospectively (i.e.; restate comparatives per Section 10 of FRS 102) or;
- apply retrospectively with the cumulative effect recognised in the current year.

The latter approach is similar to the 'cumulative catch-up' transition method in IFRS 15 in that it does not require an entity to restate comparatives or consider completed contracts.



Key practical implementation challenges

Understanding your customer contracts and identifying all the key contractual terms which might need to be considered under revised FRS 102

Analysing whether contracts are similar enough in nature to be able to group them together to account on a portfolio basis or not

Understanding the nature of goods and services being provided - should they be combined? Or are they distinct? How does value transfer to the customer and what does this mean in terms of whether revenue is recognised over-time or at a point in time?

Dealing with new areas of judgment, for example if variable consideration is present, what process will you put in place to estimate the amount to include, and assess whether the 'highly probable' threshold has been met?

Broader practical implications - for example impact on KPIs, required updates for systems, training for finance and sales/ commercial teams

Other incremental improvements and clarifications to FRS 102

Effective on or after 1 January 2026

Section 1A Small Entities

Greater clarity
for small entities
in the UK
applying Section
1A regarding
which
disclosures
need to be
provided in
order to give a
true and fair
view.

Section 2
Concepts and
Pervasive
Principles

A revised Section 2 (Concepts and Pervasive Principles), updated to reflect the IASB's Conceptual Framework for Financial Reporting, issued in 2018. Section 2A Fair Value Measurement

A new Section 2A (Fair Value Measurement), replacing the Appendix to Section 2 and updated to reflect the principles of IFRS 13. Section 7
Statement of
Cash Flows

New disclosure requirements about supplier finance arrangements (effective 1 January 2025). Section 26 Share-based Payment

Additional guidance on measurement of cash settled awards and equity awards settled net of tax.

Section 29 Income Tax

Introduction of guidance on accounting for uncertain tax positions.

Section 34 Specialised Activities

Various improvements and clarifications to existing requirements and consequential changes to reflect other amendments.

2024 UK

Corporate

Governance

Code

FRC revised UK Corporate Governance Code 2024 - summary

Headline change is Provision 29: formal declaration by the board on the effectiveness of the material controls as at the balance sheet date

Effective date: years beginning on or after 1 January 2025, other than the declaration on material controls which is a year later

Supported by revised FRC Guidance, replacing three existing sets of Guidance (on audit committees, risk management and internal control, and board effectiveness)

Code makes the Audit Committees and the External Audit: Minimum Standard part of the responsibilities of the audit committee (on a comply-or-explain basis)

Other changes: new Principle on the nature and quality of governance reporting, and a number of detailed changes on culture, diversity and remuneration



Risk management and internal control - on or after 1 January 2026

Provision 29

The board should monitor the company's risk management and internal control framework and, at least annually, carry out a review of its effectiveness. The monitoring and review should cover all material controls, including financial, operational, reporting and compliance controls. The board should provide in the annual report:



• a description of how the board has monitored and reviewed the effectiveness of the framework;



• a declaration of effectiveness of the material controls as at the balance sheet date; and



• a description of any material controls which have not operated effectively as at the balance sheet date, the action taken, or proposed, to improve them and any action taken to address previously reported issues.

Supports the change to **Principle O**: the board is responsible for maintaining the effectiveness of, as well as establishing, the risk management and internal control framework.

Main changes to the Code Audit committee and reporting - on or after 1 January 2025

Provisions 25 & 26

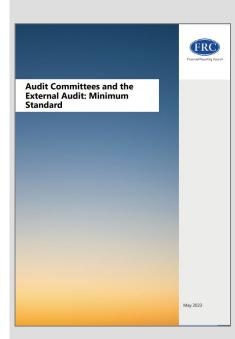
Updates to the responsibilities and reporting of the audit committee to reflect the FRC Audit Committees and the External Audit: Minimum Standard:

• Will widen the applicability of the Minimum Standard beyond FTSE 350 - at least on a comply-or-explain basis.

Principle C

Governance reporting should focus on board decisions and their outcomes in the context of the company's strategy and objectives. Where the board reports on departures from the Code's provisions, it should provide a clear explanation.

Brings 'applied corporate governance reporting' into the body of the Code.



Other changes to the Code

Culture, diversity and remuneration - on or after 1 January 2025

Provision 2

Now calls for directors to look at "how the desired culture has been embedded" - in effect brings message from existing Guidance into the Code itself.

Principle J

Has been amended to promote diversity, inclusion and equal opportunity, without referencing specific groups: the previous list of diversity characteristics has been removed to indicate that diversity policies can be wide ranging.

Provision 38

The annual report now needs to contain a description of malus and clawback provisions including: the circumstances in which malus and clawback could be used; a description of the period for malus and clawback and why it is appropriate; and whether the provisions were used in the last reporting period and, if so, the reasons.

Provision 40

The list of characteristics that the remuneration policy should address (clarity, simplicity, risk, predictability, proportionality and alignment to culture) has been removed.

Changes to the FRC Guidance



Accessibility

Three existing sets of Guidance brought together and hyperlinked from the Code (Guidance on audit committees, risk and internal control and board effectiveness).



Re-ordering and re-drafting

The subject matter of the Guidance has not changed substantially, but it has been revised to shorten it generally and to reflect the changes to Section 4 (audit committee and risk management and internal control). Guidance relating to the make-up and general approach of board committees also included.



Structure and approach to risk management and internal control

Guidance in this area reflects the structure of Code principle O: establishment of the framework (including governance arrangements and risk assessment) is distinguished from maintaining its effectiveness (including board monitoring and review of effectiveness).



Material controls (the focus of Provision 29)

Defined as controls over principal risks (that could threaten the business model, future performance, solvency or liquidity and reputation, and potentially controls over price sensitive external reporting, fraud and aspects of information and technology.



Guidance on the directors' declaration

Part of a section on reporting and includes commentary on what to report if a control did not operate effectively at the balance sheet date.

What are the FRC's intentions around risk and internal control?



[Extracts from policy update pre finalisation of 2024 Code]

Update on Code consultation: The FRC will "take forward only a small number of the original 18 proposals we set out in the consultation and ... stop development of the remainder". Some also not "taken forward as a result of the **Government's ... decision to withdraw its Statutory Instrument** relating to an audit and assurance policy, reporting on distributable profits and resilience statement requirements".

On internal controls specifically: The decision has been made to ensure "a more targeted and proportionate Code revision", with more time for implementation so that "the UK approach clearly differentiates from the much more intrusive approach adopted in the US".

In our review of the UK Corporate Governance Code we prioritised the important change related to internal **controls** but **scaled back** several other proposals. We also reframed the discussion around 'comply or explain' by being clear with businesses that explanations are acceptable against the Code's provisions where this better aligns with their business model and is set out in a transparent and cogent manner. Finally, we reduced the amount of guidance associated with the Code by 20% in order to avoid this being seen as a layering of regulatory expectations on Boards. An overarching objective of our revisions to the Code is to empower Boards to think for themselves and feel confident in owning their judgements. These changes were well received by businesses and investors.

> [Extracts from Jan '25 letter to Government on how the FRC is addressing its responsibility to prioritise growth in the UK economy]

To build on existing requirements

Revised Provision 29 and Guidance largely reflect existing Code and Guidance, but with the formal declaration (or conclusion) now in the Code itself - and some more specific instructions...

2024 Code Provision 29	Existing (2018) Code Provision 29/ Guidance
The board should monitor the company's risk management and internal control framework and, at least annually, carry out a review of its effectiveness. The monitoring and review should cover all material controls, including financial, operational, reporting and compliance controls. The board should provide in the annual report:	[Prov 29] The board should monitor the company's risk management and internal control systems and, at least annually, carry out a review of their effectiveness and report on that review in the annual report. The monitoring and review should cover all material controls, including financial, operational and compliance controls.
A description of how the board has monitored and reviewed the effectiveness of the framework;	[GRM para 58] The board should summarise the process it has applied in reviewing the effectiveness of the system of risk management and internal control.
a declaration of effectiveness of the material controls as at the balance sheet date; and	[GRM 58] The board should explain what actions have been or are being taken to remedy any significant failings or weaknesses. [GRM = FRC Guidance on risk management, internal control and related financial and business reporting (2014)]
a description of any material controls which have not operated effectively as at the balance sheet date, the action taken, or proposed, to improve them and any action taken to address previously reported issues.	

To emphasise the role of the board

Company management

Day-to-day systems and assurance

Company management

Monitoring and assurance

Three lines of defence

Monitoring Review of effectiveness

Primary focus of Provision 29, including the related reporting

Many boards and committees will want to consider their arrangements across this chain

procedures

To make material controls a key focus - and a matter of judgement

What is meant by a material control



Effectiveness and material controls



- Controls over risks that could threaten the company's business model, future performance, solvency or liquidity and reputation (i.e. principal risks).
- Controls over external reporting that is price sensitive or that could lead investors to make investment decisions.
- Fraud, including override of controls.
- Information and technology risks including cybersecurity, data protection and new technologies.

[FRC Guidance, paragraph 272]

Identifying these controls is primarily a matter for the judgement of the board and its committees, based on the underlying systems and processes and the information provided to them. Where a risk or similar issue is covered by more than one material control, and one of those material control is found not to have operated at the balance sheet date, the control framework in that area could still be effective.

Again, this will be a matter for the judgement of the board or its committees - and reporting should reflect the outcome.



Sustainability in a complex political and regulatory landscape

Political headwinds and regulatory delays continue to create uncertainty for investors and market participants...

- US "anti-ESG" sentiment
- Departures from major climate alliances
- Regulatory uncertainty and transposition delays

...but sustainable financial products continue to see global net inflows as the **urgency** to act intensifies

- Sustainable funds saw net inflows in 2024
 Europe makes up 84% of global sustainable funds and European inflows far outweigh US outflows.
- Recent events have heightened the sense of urgency
 Moody's projects insured losses as a result of the LA wildfires to
 run into the billions of dollars and have highlighted the need for
 financial institutions to better assess climate risk.
- Investor demand for action continues

PwC's 2024 Global Investor Survey found that 50% of investors think it very or extremely important that companies change the way they create, deliver and capture value in response to climate change.

Sustainability reporting landscape headlines

Europe:

- **CSRD** in the European Union is now effective for the first tranche of reporters (despite certain Member States not yet transposing the legislation).
- Related reporting standards the European Sustainability Reporting Standards (ESRS) finalised 2023.
- First wave of reporters in 2025 for Dec 2024 year ends.
- SFDR reporting continues for financial products with updates expected in 2025.

International:

• In June 2023, the first two IFRS Sustainability Disclosure <u>Standards</u> were issued by the <u>International Sustainability Standards Board (ISSB)</u>.

United States:

- In October 2023, four landmark sustainability disclosure bills were signed into **California law**, three of which require climate-related disclosures.
- In March 2024, the **SEC** adopted <u>final rules</u> to enhance public company climate disclosures
- In May 2024, SEC stayed climate disclosure rules to "facilitate the orderly judicial resolution" of pending legal challenges.









Update on sustainability reporting: **EU CSRD**

EU Corporate Sustainability Reporting Directive (CSRD)

- A number of UK groups are moving towards reporting on the EU CSRD:
 - Mainly in 2025 because they have large businesses in the EU.
 - Can also be benefits for businesses.
- Key emerging issues:
 - Role of double materiality assessment, and resulting number of standards and data points in scope.
 - Placement of sustainability information in UK reporting.
 - Meaning of 'limited assurance' in this area in practice.



Signs of uncertainty (US)

Blackrock quits climate group

"In December the Republican-led U.S. House of Representatives Judiciary Committee sought information from BlackRock and dozens of other asset managers involved with Net Zero Asset Managers Initiative. In November BlackRock and rivals were sued by Texas and 10 other Republican-led states that claimed their activism cut coal production and boosted energy prices.

BlackRock has denied wrongdoing and said the lawsuit "discourages investments in the companies consumers rely on."

JPMorgan becomes latest U.S. lender to quit Net-Zero Banking Alliance

LONDON, Jan 7 (Reuters) - JPMorgan

JP Morgan said on Tuesday it was leaving the Net-Zero Banking Alliance, the latest U.S. lender to quit the sector's biggest climate coalition amid rising U.S. political pressure.



Signs of uncertainty (EU)

Revisions to Corporate Sustainability Due Diligence Directive

- Initially CS3D designed to apply to EU companies with a minimum of 500 employees and a turnover of €150 million.
- Revised text increased the thresholds to a minimum of 1,000 employees and a net turnover of €450 million, taking (reportedly) almost 70% out of scope.
- Specific targeting of businesses with a higher risk of environmental or social harm also dropped.

Omnibus 'simplification package' initiative

- EC now plans to publish a proposal for an Omnibus Initiative aimed at simplifying sustainability reporting requirements on 26 February 2025. While specific details about the package are not yet available, it is expected to address the CSRD, CS3D, and the Taxonomy Regulation.
- Strong German influence: Scholz letter to EC:
 - German industry highlighting need for action regarding the burdens imposed by the CSRD, the EU Taxonomy, and CSDDD.
 - Called for a two-year delay of the CSRD implementation for wave 2 companies and an increase of the threshold values for turnover and employee numbers to avoid overburdening companies.

Update on UK position

UK developments

- Technical Advisory Committee issued advice on UK implementation of (the two) ISSB standards in December 2024:
 - UK standards due to be available in Q1 2025 and applicable from 1 January 2026.
- Many known unknowns remain for instance:
 - How equivalence with CSRD will be determined and the strategic relevance of this.
 - Content of standards for non-EU reporters.

FRC Assurance of Sustainability Assurance Market Study (Oct 2024) extract from Key emerging findings

Stakeholders collectively agreed that there was a clear need for transparency and clarity on likely future regulatory requirements, or at least the direction of travel, to enable adequate planning, investment and future compliance.

Many stakeholders would like any UK regulatory requirements to be fully interoperable with other international regulations.

Jersey's Sustainable Finance Action Plan

In November 2024 Government of Jersey launched the Sustainable Finance Action Plan, which sets out ten priorities for the finance industry across three action areas: risk and governance; market incentives; and international engagement. As NEDs, three priorities are key to stay abreast of:

- Corporate Sustainability Disclosures: Jersey intends to bring in sustainability reporting requirements for certain entities from 2027. We expect the roll-out will begin with the largest on-island corporates, with likely exemptions for investment entities. Requirements are expected to be interoperable with the ISSB's IFRS Sustainability Standards and the EU's ESRS.
- Sustainability Risk Management: the intention is to embed sustainability risk management
 obligations into the regulatory framework in order to better manage sustainability risk exposure. This
 will likely create additional obligations for boards of Jersey companies in terms of ongoing climate
 risk management.
- **ESG Integrity Risk**: expansion of anti-greenwashing principles for both products and corporates to ensure sustainability-related marketing/claims are substantiated currently timetabled for 2026.

What are the implications for CI entities?

- Understand group structure and exposure to various jurisdictions at corporate/fund/portco level, particularly the EU and CSRD - value chain impact and assurance requirement!
- Continued SFDR reporting obligations for funds marketed to EU investors under NPPR - look out for expected amendments to this regulation.
- Understanding the application of the UK's endorsement of the ISSB standards (S1 and S2)
 - How the UK's SDR will be extended to overseas funds.
 - The FCA's approach to updating the Listing Rules (for listed products).
- GFSC/ JFSC local endorsement regime and interoperability.

What does this mean from a governance perspective?

- Understanding the evolving regulatory landscape and your reporting obligations, now and in the future.
- Responsibility for ESG data, evidence required, level of oversight.
- What are the assurance expectations.
- Roles and responsibilities with respect to the strategy and reporting.
- Engagement and understanding stakeholder needs/ requirements.

IFRS 18

accounting

standard

IFRS 18: The headlines!

Major new IFRS Standard issued in response to investor demands for better and more transparent information

- Replaces IAS 1 as the new standard on the presentation of financial statements
- Effective for annual financial reporting periods beginning on or after 1 January 2027

Key changes:

- 1 Structure of the statement of profit or loss
 - Introduction of operating, investing and financing categories.
 - Mandatory sub-totals, including operating profit.

- Management-defined performance measures
 - · Defined subset of APMs.
 - Mandatory disclosure requirements, including reconciliations.

- Aggregation and disaggregation principles
 - Judgement based on characteristics of items.



Changes to statement of profit or loss

Entities will be required to allocate income and expenses between three major categories

Operating

- Residual category.
- Income and expenses from an entity's main business activity.
- Includes volatile and unusual income and expenses.
- Presented by nature or by function.

Investing

Income and expenses from:

- Associates and JV's.
- Cash and cash equivalents.
- Assets that generate a return individually and largely independently of other assets.

Financing

- All income and expenses from liabilities that involve only the raising of finance.
- Interest expense and the effects of changes in interest rates from other liabilities.

Classification differs in some cases for entities that provide financing to customers or invest in assets as a main business activity.

January 2025

What is a 'management-defined performance measure'?

A management-defined performance measure is a subtotal of income and expenses that:



Used in public communications outside financial statements



Communicates management's view of an aspect of the financial performance of the entity as a whole



Not specifically excluded from being an MPM, or specifically required to be presented or disclosed by IFRS Accounting Standards

Other

developments

and

consultations

Overview of the changes to the UK Listing Rules (UKLR)



The previous Standard and Premium market segments have been combined into a single segment – **Equity Shares** (Commercial Companies) (ES(CC)).



For **Significant Transactions** by ES(CC) listed companies, a Significant Transaction notification **disclosure regime** has replaced the previous **shareholder circular** and vote. A vote is still required for reverse takeovers.



The **eligibility requirements for IPOs** have been relaxed.



Greater flexibility has been introduced to allow dual class share structures with weighted voting rights.



A new **procedures**, **systems and controls form** has been introduced for new applicants.



Changes have been made to the **Sponsor** regime.



Some other recent developments - for awareness

BVCA updates Walker Guidelines on private equity reporting

Portfolio companies now **in scope** where enterprise value of a transaction exceeded £500m AND the company generates annual revenues of more than £200m (at least 50% in the UK) OR has more than 1,000 UK full-time equivalent employees (smoothing arrangements to follow).

FTSE 250 reporting remains the benchmark, with specific emphasis on risk, climate and diversity reporting.

Voluntary, but condition of BVCA membership.

Government on size thresholds

50% increase in monetary thresholds for small/ medium size regime and deletion of certain directors' report disclosures from 6 April 2025:

 Including stakeholder engagement, as well as financial instruments, post balance sheet events and more.

Separate consultation on wider future of non-financial reporting early in 2025, including employee numbers threshold to 500 and exemption from strategic report for medium sized companies.

IoD Code of Conduct for Directors

Six principles:

 Leading by example, integrity, transparency, accountability, fairness, responsible business.

Includes guidance on applying the Code.

No legal force or enforcement regime.

Suggested reference in annual report where applied.



Recent FRC consultations and discussion papers

FRC Stewardship Code (consultation to 19 Feb '25)

New two-part reporting structure, with Policy & Context on three year cycle, unless there are changes.

Revised stewardship definition, emphasising that stewardship "may lead to wider benefits for the economy, the environment and society" but this is not the primary goal.

Briefer principles with quite specific prompts 'how to report'.

More guidance to come.

FRC Update to guidance on going concern (consultation)

One set of guidance for all in scope.

No fundamental issues but could be clearer on:

- the necessary period of assessment (and how this relates to risks); and
- the respective roles of directors and auditors.

Viability statement dealt with in main FRC Guidance - away from going concern.

FRC, etc. Future of digital reporting (discussion paper)

Largely focused on questions around use of taxonomies and tagging.

But also touches on future of wider reporting framework.

Is it time for a proper reassessment of that?



Thank you

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