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Submitted by email: riskreview@frc.org.uk

RESPONSE TO THE FRC'S DRAFT GUIDANCE ON RISK MANAGEMENT, INTERNAL CONTROL AND THE GOING CONCERN BASIS OF ACCOUNTING AND ASSOCIATED CHANGES TO THE UK CORPORATE GOVERNANCE CODE

Dear Ms. Woods,

Thank you for the opportunity to provide comments on the Financial Reporting Council's (FRC) Draft Guidance on the *"Risk Management, Internal Control and the Going Concern Basis of Accounting"* (Draft Guidance) and associated proposed changes to the UK Corporate Governance Code (UK Code).

GSK is supportive of initiatives, such as this one, which promote effective risk management and internal control and improve transparency of our operations for the benefit of our shareholders and other stakeholders. We are also pleased that the FRC has listened to feedback on its revised going concern consultation exercise in January 2013, and support its decision to drop its original proposal to introduce a dual going concern test.

We agree with the general direction taken by the FRC of integrating its current guidance on going concern and internal and risk management and making some associated changes to the UK Code. The Draft Guidance is comprehensive in nature, and we support the emphasis on the ongoing monitoring of a company's risk management and internal control systems.

However, although we are generally supportive of the ambition of the Draft Guidance, we do have three particular concerns which are set out below.

In addition, we have set out our responses on the specific questions posed by the FRC in the consultation paper in the table that is attached to this letter.

1. Statement on risk management and internal control

We support the timely disclosure of material information to the market as soon as possible as required under the Financial Conduct Authority's (FCA) Disclosure and Transparency Rules. The Rules provide a reliable mechanism to disclose material, significant failings to shareholders and the market in a timely manner. By contrast, we believe the proposed guidance for the Board to *"explain [in the annual report] what actions have been or are being taken to remedy any significant failings or weaknesses identified from [an internal control assessment] review"* creates an ambiguity when compared to the Board's obligation to timely report a material failing or weakness, in compliance with the FCA Disclosure and Transparency Rules.

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We would suggest the Guidance be clarified to state that the Board's explanation of any actions being undertaken to remedy a material failing or weakness in the company's Annual Report is based on the FCA disclosure requirements. In addition, depending on the timing of when a significant failing or weakness is identified, it should be acknowledged in the Guidance that the Board may be unable to provide a clear view on the actions being taken at the time the material failing or weakness is reported.

Separately, the Draft Guidance in this area would create uncertainty for GSK and other dual UK/US listed filers in relation to its treatment in Form 20-F filings which we have discussed in more detail in the attachment to this letter.

2. Practical application

The current Draft Guidance focuses on ***what*** Boards are expected to do. We believe the Draft Guidance would be considerably strengthened with further explanation added of ***how*** these expectations should be implemented in practice. This would be most useful in intangible/qualitative areas such as measuring the effectiveness of an organisation's risk culture. Further use of examples in the Guidance would improve the likelihood of effectively incorporating these activities into normal business operations and it is suggested that it would be preferably in the objectives for the Guidance.

3. Board and management oversight responsibilities

In our view, there needs to be a clear distinction between the workloads and responsibilities of the Board on the one hand and Management on the other, with further emphasis and differentiation placed throughout the Guidance on the respective roles of the Board, the Audit Committees and Management given their various responsibilities for managing risk. There is a need to complement the work of the Board and its supporting Committees and not duplicate the work undertaken by Management.

Please contact Victoria Whyte, who is the Secretary to the Audit & Risk Committee, (Email:victoria.a.whyte@gsk.com) in the first instance should you wish to discuss any aspect our response in greater detail.

Yours sincerely

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Risk Management, Internal Control and the Going Concern Basis of Accounting Consultation Paper

Reference	FRC welcome views on the following questions	GSK's Responses
Question 1: page 3	*The FRC would welcome views on whether the revised Draft Guidance achieves these objectives, and on the structure of, and level of detail in, the draft revised guidance.*	Our general responses are provided in our covering letter. As we note in our letter, we believe the Draft Guidance is comprehensive in nature, and we support the emphasis on the ongoing monitoring of a company's risk management and internal control systems.
Question 2: page 3	*Do you agree [that the current sections 2 and 3 [and proposed guidance sections 5 and 6] ("Maintaining a sound system of internal control" and "Reviewing the effectiveness of internal control" are fit for purpose] or are more substantive changes to these sections required?*	We generally agree that the sections cover the important expectations. We suggest that this guidance could be structured in a simpler manner and should provide further clarity on certain points as described below. While the sections articulate expectations for the board generally, we would support further emphasis on the important role played by audit and risk committees and accountability for the day-to-day management of principal risks on company management throughout the Draft Guidance. We encourage the FRC to re-examine the positioning of accountabilities in the Draft Guidance to further clarify these roles. The Draft Guidance could be improved by noting the importance of applying risk management and internal control throughout the organisational hierarchy and how assurance is provided to the board that the framework is operating effectively. For example, further explanation could be provided on how the compliance, risk management or internal audit groups that operate independently from business operations can provide unbiased feedback to the board on the effectiveness of risk management and internal control. We would also support further guidance on the scope of principal risks in the context of the traditional focus of risk management (e.g. legal, compliance, operational) and risks associated with business challenges and opportunities. This will promote better alignment of principal risk oversight and reporting across companies.

		We would support further distinguishing the attributes, distinctions and important relationships between the risk management and internal control systems. This would drive a common understanding and alignment on these areas. As an example, section 4 focuses on identification of principal risks, while sections 5 and 6 cover establishing and reviewing risk management and internal control. Risk identification is an important element of an effective risk management system. We would support further clarity on how to implement qualitative elements of the Draft Guidance and effectively assess and measure those elements. For example, *"the culture of the company and the extent to which the desired culture has been instilled"* is an important but intangible attribute that is difficult to measure. Additionally, the risk appetite for principal risks can be articulated in a general or specific manner dependent on the nature of the risk. Further clarity could be provided on how this can be implemented in practice and measured to drive intended behaviours. We would support further emphasis on the need for a *"speak-up"* culture and effective *"whistle-blower"* program as key elements of the risk management and internal control system. We believe these are essential to ensure potential exceptions and issues are identified and reported in a timely manner. We suggest the Draft Guidance clarifies that the scope of a company's risk management and internal control system should consider risks associated with third-party relationships and the need to have effective third-party oversight in place.
Question 3: page 4	*The FRC therefore proposes to amend the guidance [(that companies should "confirm that any necessary actions have been or are being taken to remedy any significant failings or weaknesses identified from [the] review [of internal controls)]" to recommend more explicitly*	We are in general agreement with the Draft Guidance that, *"…The board should explain what actions have been or are being taken to remedy any significant failings or weaknesses identified from that review, including the process it has applied to deal with material risk management or internal control aspects of any significant problems disclosed in the annual report and accounts."* We recommend further clarification is provided regarding the level of detail to be disclosed on the actions and how significant failings or weaknesses are defined. We would not recommend disclosing a listing of all general or non-material failings or weaknesses that occurred during a reporting year. This may add a burdensome and unhelpful reporting expectation that would only result in a retrospective list of company

	that the board should "explain what actions have been or are being taken to remedy any significant failings or weaknesses identified from that review".] and would welcome views on this proposed change.	challenges that may have already been disclosed at the time they occurred in a more appropriate format, such as in a company press release to shareholders and the external community. This guidance could also introduce confusion over definitions of material disclosures that require immediate announcements and the disclosure of significant failings or weaknesses that are identified in a company's annual report but fall short of requiring immediate disclosure through a Stock Exchange Announcement, in compliance with the FCA's Disclosure and Transparency Rules. From a Form 20-F disclosure perspective for dual UK/US filers such as GSK, the draft guidance does not directly correspond to comparable principles under the US disclosure regime. As a result, there may be a judgment to include this disclosure in the Form 20-F in order to be comfortable that the market has not been selectively informed. Therefore, dual filers may find themselves in an unusual situation of being obligated under the revised draft guidance of making disclosures about their internal controls on financial reporting that are not required under US laws and regulation.
Question 4: page 4	*Appendices D and E contain questions which boards may wish to consider in applying the guidance, and indicators that may assist them in assessing how they are carrying out their responsibilities, the culture of the company, and the effectiveness of the risk management and internal control system. The FRC would welcome views on whether these appendices are of use to directors and, if so, how they might be improved.*	We appreciate the insights presented in Appendix D that represent useful guidelines for board consideration. However, we suggest removing Appendix E as we feel many of these can be implied from the questions set out in Appendix D. We suggest the Draft Guidance could be better structured around a common core of attributes that make up the risk management and internal control system. For example, section 5 notes that this system consists of control activities, information and communication processes, and processes for monitoring its continued effectiveness. We suggest further defining these attributes and specific elements of each and then using this framework consistently throughout the document (including appendices) to detail how to establish, review and communicate the system of risk management and internal control.

Question 5: page 6	*Do you believe that the approach taken to require "consideration of solvency and liquidity over longer periods" and not to take forward the "high level of confidence threshold" and "foreseeable future" terms from the FRC's consultation on revised going concern guidance issued in January 2013 in Appendix B of the new revised Draft Guidance is appropriate? If not, how should it be amended and why?*	We believe the approach taken in appendix B to assess the principal solvency and liquidity risks and the decision not to take forward the "*high level of confidence threshold*" and *"foreseeable future"* terms in the revised Draft Guidance are appropriate.
Question 6: page 7	*Do you agree with the guidance in Appendix C of the revised Draft Guidance [that removes the more prescriptive thresholds and retains the term "a high level of confidence" only in situations when severe distress has occurred or will occur in the next twelve months from approval of the financial statements?] If not, how should it be amended and why?*	This section remains largely unchanged from the FRC's previous consultation in this area *("Implementation of the recommendations of the Sharman Panel: Revised Guidance on Going Concern and Revised International Standards on Auditing (UK and Ireland)")* issued in January 2013 and we agree with the revised Draft Guidance. We note that some items in this section are replications of guidance included in accounting standards and any attempt to replicate current GAAP could potentially lead to difficulties in the future if such GAAP is amended.
Question 7: page 7	*Do you agree with the revised Draft Guidance [that provides supplemental guidance for banks in a standalone document called, "Guidance for the*	The supplemental guidance does not apply as GSK is a pharmaceutical company. We therefore do not offer a view on this question.

	Directors of Banks: Solvency and Liquidity Risks and the Going Concern Basis of Accounting"?] If not, what needs to be amended and why?	
Question 8: page 7	*Do you agree with the draft revised auditing standards [that require the auditor to report if they have "anything material" to add concerning solvency and liquidity risks]? If not, what should be changed and why?*	We remain comfortable with the proposed amendments which are largely carried forward from the FRC's January 2013 consultation document. However the amended test of *"anything material"* to add may still require further interpretation. There also continues to be a wider question concerning whether this proposed unilateral change in international auditing and reporting standards can be sufficiently justified in the circumstances.
Question 9: page 10	*The proposed revisions to Sections C.1 and C.2 of the UK Code are set out opposite. The FRC would welcome views on whether the additions are required and, if so, on the detailed wording; and on whether the existing Provision C.1.3 (on the going concern statement) should be removed.*	~~C.1.3. The directors should report in annual and half-yearly financial statements that the business is a going concern, with supporting assumptions or qualifications as necessary.~~ We agree with the proposed deletion. ***C.2 Main Principle****: The board is responsible for determining the nature and extent of the ~~significant~~* ***principal*** *risks it is willing to take in achieving its strategic objectives. The board should maintain sound risk management and internal control systems.* We agree with the proposed change. ***C.2.1 (New):*** *The board should carry out a robust assessment of the principal risks facing the company, including those that would threaten its solvency or liquidity. In the annual report the directors should confirm that they have carried out such an assessment and explain how the principal risks are being managed or mitigated. They should indicate which, if any, are material uncertainties in relation to the company' s ability to continue to adopt the going concern basis of accounting.* We agree that when assessing principal risks, implications on potential solvency and

		liquidity should be one of the assessment criteria. By nature, principal risks are the most significant to the company and it may not provide additional value to further specify which principal risks or uncertainties would impact the ability to adopt the going concern basis of accounting in this section of the annual report. If a company is in severe distress, this should be highlighted prominently in the Strategic Report with further detail on solvency and liquidity risk in the financial statements. Further linkage to the principal risks may not simplify or improve understanding related to these important disclosures. We have raised previously in discussions with the FRC the challenges that GSK and other dual UK/US listed companies face over the obligation to explain how risks *"are being managed or mitigated"*. This is because the US Securities & Exchange Commission (SEC) does not recommend disclosure of risk mitigating activities alongside description of principal risks in a company's Annual Report. Therefore, we would encourage the FRC to develop their Draft Guidance further in this area with specific recommendations to dual filers and also to liaise with their counterparts in the SEC, to assist dual listed companies in bridging the gap between these competing requirements. ***C.2.2 (Revised)*** - *The board should monitor the company's risk management and internal control and, at least annually, carry out a review of their effectiveness, and report to shareholders that they have done so. The monitoring and review should cover all material controls, including financial, operational and compliance controls.* We agree with the proposed change.