

26 April 2013

Marek Grabowski Esq.
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Our Ref: SJG

Dear Marek

Consultation on Implementing the Recommendations of the Sharman Panel

Thank you for the opportunity to contribute to the above consultation. On the attached sheet we have answered the specific questions in the consultation document but we would offer the following comments as a summary:

- (a) We are not convinced of the need for re-writing the 2009 guidance and re-defining going concern and related concepts
- (b) Requiring an assessment based on a "high level of confidence" will result in many standard emphases of matter paragraphs produced by auditors, which will undermine financial reporting in the UK
- (c) The new distinctions concerning solvency and liquidity, the 'foreseeable future', and 'in the ordinary course of business or otherwise', do not make positive contributions to, and advance, the guidance beyond that produced in 2009
- (d) We are concerned that considerations, based on an interpretation of the UK Corporate Governance Code, are being extended to all corporate reporting (including SMEs) without any clear benefit in doing so.
- (e) The FRC has not provided a cost benefit analysis of these proposals.

Yours sincerely



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Area for comment	Crowe Clark Whitehill response
Question 1: Do you agree that the Guidance appropriately provides the clarification recommended by the Panel as to the purposes of the going concern assessment and reporting and is appropriate? If not, why not, and what changes should be made to the Guidance?	We do not agree that the guidance provides the clarification recommended by the Panel. There is no indication of consensus in the international accounting community either fundamentally reconsidering the going concern assessment and disclosure process nor of moving towards a more significant recognition of the stewardship role.
Question 2: Do you agree with the description in the Guidance of when a Company should be judged to be a going concern? Do you agree in particular that this should take full account of all actions (whether within or outside the normal course of business) that the board would consider taking and that would be available to it; and that, if the underlying risks were to crystallise, there should be a high level of confidence that these actions would be effective in addressing them? Is the term ‘a high level of confidence’ sufficiently understandable? If not, why not, and how should the description or term be modified?	<p>We have significant reservations over the description contained within the Guidance. In particular, our concern is that the “high level of confidence” threshold that a company will have the necessary liquid resources to meet its liabilities as they fall due for the foreseeable future is too high and unrealistic. The renewal of banking facilities is not a decision that is within the control of the company’s directors and so to require them to express a high level of confidence that their banking facilities would be renewed in the future seems inappropriate. Of course the directors can take action to ensure that there is the best possible chance that facilities will be renewed and that might be sufficient for them to be able to express that they have a “reasonable expectation” that there will be a successful renewal but a high level of confidence is an altogether different test.</p> <p>We are concerned that persisting with the high level of confidence test will result in many ‘standard’ modifications to auditors’ reports, which would undermine financial reporting.</p>
Question 3: Do you agree with the approach the Guidance takes to the implications and nature of actions within or outside the normal course of business? Do you consider that the Guidance explains their nature sufficiently clearly? If not, why not and what changes should be made to the Guidance?	No. The distinction of within or outside the normal course of business does not positively contribute to the assessment and disclosure of going concern and is a further issue that lacks clear definition.

Area for comment	Crowe Clark Whitehill response
<p>Question 4: Do you agree with the approach taken to interpreting the foreseeable future and is this sufficiently clear in the Guidance? If not, why not and how should the Guidance be changed?</p>	<p>No. Defining the foreseeable future is difficult and we are concerned that a wide range of interpretations are possible. In one sense, a company with a stock-turn of six times a year has a business cycle of two months and in another sense, a company that has a ten year lease of the premises from which it trades may be considered to have a ten year cycle. This will introduce so much judgement that comparability between financial statements will not be feasible.</p>
<p>Question 5: Do you agree that the use of the term 'going concern' in the phrase 'going concern basis of accounting' is sufficiently clearly distinguished in the Guidance from its use in the Code requirement for a statement that the company 'is a going concern' and from its use in the accounting and auditing standards in the context of material uncertainties about the company's 'ability to continue as a going concern'? Is it clear from the Guidance that the statement the directors are required to make under the Code (that the Company is a going concern) should reflect the board's judgement and is not intended to be absolute? If not, why not and what changes should be made to the Guidance or the Code requirement?</p>	<p>No. This appears to us to be unnecessary in making the distinctions referred to. It has the capacity of creating further confusion.</p>
<p>Question 6: Do you agree that the judgemental approach in the Guidance to determining when there are material uncertainties to be disclosed is the appropriate interpretation of the relevant accounting standards? Do you agree that the factors and circumstances highlighted respectively in paragraphs 2.30 and 2.31 are appropriate? If not, why not and what changes should be made to the Guidance?</p>	<p>Confirming that the going concern assumption is valid has always been a matter of judgement. However, the Guidance is unclear that in fact liquidity considerations are a subset of the solvency considerations. Further, a 'high level of confidence' over the 'foreseeable future' will require almost all companies to disclose such uncertainties with many auditors' reports being modified. This will become standard and so common that it will be to the detriment of financial reporting.</p>

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<p>Question 7: Do you agree that the interpretations adopted in the Guidance in implementing Recommendation 2(b) are consistent with FRS 18 and ISA (UK and Ireland) 570? If not, why not and what changes should be made to the Guidance or those standards?</p>	<p>We do not believe it appropriate to make changes to accounting standards or ISA (UK&I) 570 before there is common international understanding of the issue, especially if the FRC wishes to include a stewardship function and to redefine the ‘foreseeable future’.</p>
<p>Question 8: Do you agree that Section 2 of the Guidance appropriately implements Recommendation 3? Do you agree with the approach to stress tests and the application of prudence in conducting them? Do you agree with the approach to identifying significant solvency and liquidity risks? Do you agree with the description of solvency and liquidity risks? If not, why not and what changes should be made to the Guidance?</p>	<p>Whilst we would welcome a more integrated approach to financial reporting in annual reports and financial statements, improving the reporting of risks, uncertainties and responses thereto, section 2 introduces unnecessary distinctions (which lack clarity of definition) which do not further the integration.</p>
<p>Question 9: Do you agree that the approach taken in Section 4 of the Guidance in implementing the disclosures in Recommendation 4 is appropriate? Is the term ‘robustness of the going concern assessment process and its outcome’ sufficiently clear? Do you agree that the approach the board should adopt in obtaining assurance about these matters is appropriately reflected in Section 3 of the Guidance? Do you agree that the board should set out how it has interpreted the foreseeable future for the purposes of its assessment? If not, why not and what changes should be made to the Guidance?</p>	<p>No, we do not agree with the approach. In essence, we are concerned that auditors’ risk management policies and procedures will render the auditor’s comments into standard wording (boilerplate) which will fail to meet the objective. We have commented separately on the proposals for auditors’ reports.</p>

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Question 10: Do you agree that the proposed amendments to the auditing standards appropriately implement the enhanced role of the auditor envisaged in Recommendations 4 and 5? If not, why not and what changes should be made to the auditing standards?	No. We believe international consensus should be achieved first. We are also concerned with the implications as indicated in our previous answer.
Question 11: Do you agree that it is appropriate for the Supplement to confirm that central bank support for a solvent and viable bank does not necessarily constitute a material uncertainty? In particular, do you agree that central bank support (including under ELA) may be regarded as in the normal course of business where the bank is judged to be solvent and viable? Do you agree that the approach set out in the Supplement to assessing whether there is a material uncertainty is appropriate and consistent with the general approach in the Guidance? If not, why not and what changes should be made to the Supplement to the Guidance?	We do not audit banks and have no view to offer.
Question 12: Do you consider the proposed implementation date to be appropriate? If not, why not and what date should the application date be?	No. There is a long way to go yet in developing this Guidance and the implementation date would impact 31 December 2013 year ends and 30 June 2013 interims. This will not allow preparers of financial statements and auditors sufficient time to plan and implement the changes necessary to comply.

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<p>Question 13: Do you believe that the Guidance will deliver the intended benefits? If not, why not? Do you believe that the Guidance will give rise to additional costs or any inappropriate consequences? For example, as compared with the 2009 Guidance, do you believe that the Guidance will give rise to fewer companies being judged to be a going concern and/or more companies disclosing material uncertainties? If so, what are the key drivers and can you give an estimate or indication of the likely cost or impact? Do you believe that such additional costs or impact would be justified by the benefits?</p>	<p>We are concerned that the Guidance will result in a greatly increased number of auditors' reports with modifications. The concepts, and lack of definition of those concepts, will cause large variations in reporting practice, inculcate confusion in users of financial statements, downgrading of credit ratings in UK companies, considerable divergence with international practice and create confusion among international financiers and credit providers to the detriment of UK companies.</p> <p>We expected the FRC to have provided a cost benefit analysis and impact assessment in developing the Guidance.</p>
<p>Question 14: Do you agree with the approach to SMEs in the Guidance? If not, why not and what changes should be made to the Guidance?</p>	<p>Some of our deepest reservations are concerned with the potential impact on SMEs which account for the greatest part of the economy.</p> <p>The Guidance purports to be for all companies yet much of the guidance refers back to the UK Governance Code. For many small and medium-sized companies the Code is irrelevant and even small and mid-cap companies are not required to follow the Code. It will be very difficult for SMEs to understand and implement the guidance as it is currently promulgated.</p> <p>If the FRC really wanted guidance that would cover all UK corporate entities then this should have been developed with the SMEs in mind first and then added requirements that would appropriate first for small to mid-cap companies and finally the large listed companies.</p> <p>As far as SMEs are concerned, we consider the 2009 guidance to be much more appropriate in terms of style and content.</p>
<p>Question 15: Are there any other matters which the FRC should consider in relation to the Guidance and the Supplement? If so, what are they and what changes, if any, should be made to address them?</p>	<p>The guidance refers to companies. Limited liability partnerships (LLPs) are also subject to broadly the same financial reporting requirements as companies. We can see no reason why a limited liability partnership should not be subject to the same regime. LLPs are most closely aligned with SMEs so if they were to be included in future guidance the requirements should be as for SMEs.</p>