The Hundred Group
of Finance Directors

Investor Relations and Markets Committee

By email: sharman.secretariat@frc.org.uk

The Sharman Secretariat
c/o Financial Reporting Council
Aldwych House
71-91 Aldwych
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30 June 2011

Dear Sir

Going concern and liquidity risks: Lessons for companies and auditors

We are pleased to submit evidence to the above inquiry. In our response, we have not sought to answer all the questions raised. We have focused in our responses on our experiences as preparers of financial statements, including our interactions with investors and other stakeholders.

Who we are

The Hundred Group is a non-political, not-for-profit organisation which represents the finance directors of the UK's largest companies, with membership drawn mainly, but not entirely, from the constituents of the FTSE100 Index. Our aim is to contribute positively to the development of UK and International policy and practice on matters that affect our businesses, including taxation, financial reporting, corporate governance and capital market regulation. Whilst this letter expresses the view of The Hundred Group of Finance Directors as a whole, they are not necessarily those of our individual members or their respective employers.

Our views

1. We have followed the views expressed from various quarters that a wholesale reform of the disclosure regime around the going concern assumption is necessary.

2. In our view, the current UK framework arising from the requirements of company law, accounting standards and listing rules is appropriate and the FRC's guidance on going concern and liquidity risk is a useful supplement to assess and report on the risks faced by a company. In particular we welcome the fact that the guidance is not prescriptive and consequently does not seek to impose a 'one size fits all' approach to an area where individual circumstances are so important and vary so widely.

3. Over recent years, we have observed a steady increase in the disclosure requirements imposed by accounting standards and other regulations and we would be concerned if this trend were to be perpetuated by a requirement to disclose additional information on going concern and liquidity risks. Indeed there is an argument that financial statements have become so cluttered with incremental disclosures that the ability of a reader to 'see

the wood from the trees' has become compromised leading to an inability to properly assess the information being presented.

4. We would also observe that in our experience, the imposition of prescriptive disclosure requirements, particularly ones that describe a process undertaken by management, has resulted in 'boiler plate' wording which does not provide helpful or relevant information to a reader of the financial statements.

5. We do, however, recognise that there is an expectation gap between the users of financial statements and ourselves the preparers, with the former interpreting the going concern disclosure as a barometer of the financial health of the company, rather than an assessment of the Company's ability to continue as a going concern for the foreseeable future. What is key is for the user to be able to understand the quality of the going concern statement.

6. In order to improve understanding in this area, we would recommend that the FRC's guidance is supplemented to promote a more coherent presentation of the existing disclosures relevant to the understanding of the going concern assumption, including a brief overview of the key risks (both insolvency and illiquidity) and the sensitivities that management has taken into account in making their assessment. However, three important considerations should be taken into account in formulating any recommendations in this regard:

    - commercial constraints exist over the disclosure of detailed forward-looking strategy, and the need for investors to fully understand the uncertainties, presumptions and sensitivities inherent in future financial projections must be offset by the damage that could result from the release of what could be commercially sensitive information;
    - there is a risk that information disclosed in relation to a company's going concern, particularly if it is unexpected or if a company is known to be suffering from liquidity problems, may be self fulfilling in that it will unduly impact investor and market sentiment; and
    - it is important that any changes to the current UK disclosure regime do not adversely impact the relative competitiveness of UK companies

7. We would further recommend that a full analysis is undertaken of a cross section of recent corporate failures and companies known to have signalled or experienced going concern issues, to facilitate a proper focus on the nature and extent of the disclosure deficiency that is thought to exist. This analysis would include an assessment of the adequacy of the disclosures in the most recent financial statement in the light of the events that subsequently transpired, whether leading to a failure or not. In making this assessment, it would be important take proper account of the benefit of hindsight, particularly given that the sudden and unprecedented contraction to available credit during 2008 was a liquidity event which few could have anticipated.

8. In relation to capital adequacy disclosures, there is currently an IFRS requirement which in our view is sufficient. However its relevance is limited, in that the concept of capital adequacy is only really meaningful in the context of the banking sector. Outside of the banking sector, a more meaningful representation of the risks to going concern arise from disclosures around principal risks, sources of funding and the ability of the provider to withdraw credit, maturity of liabilities and future financial commitments. It is of course, already a requirement of the Board to assess those risks and adequately portray them in the annual report.

Please feel free to contact me if you wish to discuss the views expressed in this letter.

Yours sincerely

Robin Freestone
Chairman
Hundred Group – Investor Relations & Markets Committee