



Going Concern and Financial Reporting IoD Response to FRC Consultation

Going Concern and Financial Reporting: Proposals to Revise the Guidance for Directors of Listed Companies

24 November 2008

Dear Sir,

Thank you for giving the Institute of Directors (IoD) the opportunity to respond to *Going Concern and Financial Reporting: Proposals to Revise the Guidance for Directors of Listed Companies* in September 2008. This paper presents our response.

About the IoD

The IoD was founded in 1903 and obtained a Royal Charter in 1906. It is an independent, non-party political organisation of approximately 51,000 individual members. Its aim is to serve, support, represent and set standards for directors to enable them to fulfil their leadership responsibilities in creating wealth for the benefit of business and society as a whole. The membership is drawn from right across the business spectrum. 83% of FTSE 100 companies and 64% of FTSE 350 companies have IoD members on their boards, but the majority of members, some 71%, comprise directors of small and medium-sized enterprises (SMEs), ranging from long-established businesses to start-up companies.

IoD response: summary

The IoD supports the FRC's updating of director's guidance in respect of going concern disclosure. The annual disclosure by directors of their going concern status is an important contribution to corporate transparency. Furthermore, it is timely for the FRC to update the guidance at the current time, given the more challenging nature of the overall business environment.

However, we wish to express reservations regarding the introduction of a new category of going concern status (paragraph 47). The new disclosure category – through which directors may indicate “material uncertainties that may cast significant doubt about the ability of the company to continue as a going concern” – does not add a great deal to the currently available disclosure categories, one of which already signals the existence of factors that “cast doubt on the ability of the company to continue in operational existence”. In our view, the need for directors to distinguish between these two categories of “doubt” in respect of their going concern status will add unnecessary complexity and subjectivity to the disclosure, while not contributing a great deal to investor understanding.

We recognise that international accounting standards have given rise to additional disclosure requirements in respect of going concern status. However, we are not convinced that this necessitates the creation of a new disclosure category in the guidance. Firms can satisfactorily signal their uncertainty about future prospects through the existing three disclosure categories. More detailed discussion of the specifics of their circumstances can be provided in the Business Review and Accounts.

Consequently, in the interests of clarity and transparency, we believe that it is preferable to retain the existing threefold categorisation of going concern status.

Our responses to your specific questions are as follows:

Question 1: In the light of these developments, do you believe that there is a continuing need for separate Guidance for Directors about Going Concern?

Yes. It is important that the going concern assumption is kept under review by the board as a whole. It should not be regarded as a technical accounting issue that is primarily the concern of the finance director. Consequently, we support the continued publication of separate guidance for directors by the FRC (in addition to the treatment of the issue by accounting standards).

Question 2: Do you believe that the proposed amendments are sufficient and appropriate? If not, what alternative amendments do you believe need to be made and why?

On the whole, we are supportive of the proposed amendments. As discussed above, our main reservation relates to the proposed creation of a new category of going concern status.

We would prefer to retain the following three options for director's disclosure on going concern status:

- 1) The directors have a reasonable expectation that the company will continue in operational existence for the foreseeable future and have therefore used the going concern basis in preparing the financial statements;
- 2) The directors have identified factors which cast doubt on the ability of the company to continue in operational existence for the foreseeable future but they consider that it is appropriate to use the going concern basis in preparing the financial statements. These factors may or may not require additional disclosures according to international accounting standards;
- 3) The directors consider that the company is unlikely to continue in operational existence for the foreseeable future and therefore the going concern basis is not an appropriate one on which to draw up the financial statements.

Question 3: Do you believe that any significant parts of the proposed unnecessary? If so, which paragraphs can be removed and why?

See previous answer.

Question 4: Do you believe that it continues to be appropriate to include standardised text within the proposed Guidance for Directors indicating how directors might explain their use of the going concern basis of accounting?

Whilst recognising the need to encourage directors to draft text that is specific to their own circumstances, we believe that directors appreciate concrete examples of how they can apply guidance principles in various contexts. In our view, this ultimately contributes to the improvement of reporting standards. Consequently, we would encourage the FRC to retain guidance of this nature.

Question 5: Do you believe that it continues to be appropriate for the Guidance for Directors to require directors to consider whether an additional disclosure should be given where they have not considered a period that extends to at least twelve months from the date of approval of the financial statements?

Yes.

Do not hesitate to contact us if you have any further queries.

Yours faithfully,

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