

11 December 2008

[s.leonard@frc-apb.org.uk](mailto:s.leonard@frc-apb.org.uk)

Steven Leonard  
Financial Reporting Council  
5<sup>th</sup> Floor Aldwych House  
71 – 91 Aldwych  
London WC2B 4HN

Dear Steve

**Discussion Paper on Going Concern and Financial Reporting: The Objective of Revising the Guidance for Directors of Listed Companies**

IMA is the trade body representing the UK asset management industry. IMA members include independent fund managers, the asset management arms of retail banks, life insurers, investment banks and occupational pension scheme managers. They are responsible for the management of approximately £3 trillion of funds (based in the UK, Europe and elsewhere), including institutional funds (for example, pensions and life funds), private client accounts and a wide range of pooled investment vehicles. In particular, our members manage 99% of UK-authorized investment funds.

In managing assets for both retail and institutional investors, IMA members are major investors in companies whose securities are traded on regulated markets. Therefore, we have an interest in the requirements governing how such companies prepare their accounts and the information disclosed to our members as the ultimate owners of companies and users of that information.

The original Guidance for Directors was written by one of the Cadbury Committee working groups and has remained unchanged since its inception in 1994. Since then there have been changes to requirements in standards and Company Law. Furthermore, the current economic climate has led to significant business failures both within and outside the financial services sector and shown how quickly financial institutions, in particular, can unwind. Deteriorating economic conditions and the drying up of liquidity have raised the importance of the going concern assumption and it is important that going concern disclosures in the forthcoming year end are robust. A Deloitte report has revealed that warnings that a company may not be able to continue as a going concern appeared in the audit reports of 5% of listed companies for the 2007/08 year and it is likely that this will increase at the year end.

In this context, we consider it confusing for both preparers and users that requirements to comment on going concern and liquidity risk are so dispersed and are set out in International Financial Reporting Standards, UK Generally Accepted Accounting Principles, the FSA's Listing Rules, the 1994 Guidance, the Business Review requirements in the Companies Act 2006, and in auditing standards. Thus

65 Kingsway London WC2B 6TD  
Tel:+44(0)20 7831 0898 Fax:+44(0)20 7831 9975

[www.investmentuk.org](http://www.investmentuk.org)

we welcomed the FRC recently issuing additional guidance bringing the requirements for directors together in one document. In this context, the paper seeks to introduce some consistency and proposes a fourth conclusion on the going concern status that accords with the requirements in IAS 1. Whilst this consistency is helpful it means that the Guidance now has two separate conclusions that directors have identified:

- factors that cast doubt but where the going concern is still appropriate; and
- 'material uncertainties that may cast significant doubt about the ability of the company to continue as a going concern and so additional disclosures are required by IFRSs '.

We consider it unhelpful to have four conclusions and both "doubt" and "significant doubt" in the Guidance in that the latter is more likely to become a self-fulfilling prophecy than if there were simply three conclusions.

Furthermore, an additional category whereby the "significance" of the doubt merits additional disclosure could mean that the reporting and disclosures of situations where there is simply a doubt could be reduced. We consider that any circumstances which give rise to doubts as to an entity's going concern should be disclosed. Investors value the quality of the disclosures and any statements need to be clear and unambiguous and cross referenced to other parts of the annual report and accounts, as appropriate.

Lastly, although IFRS only require management to take into account all information from 12 months from the end of the reporting period, we support the retention of FRC's requirements of a foreseeable future of at least 12 months from the date of approval of the accounts by the directors as this is more helpful to investors.

In conclusion, whilst we would welcome more harmonization of disclosure requirements in this area, we are not convinced that adding a fourth category in the Guidance in the current economic climate would be helpful. IMA believes that such changes should only be made when economic conditions are more benign in that changes now may raise more questions than they would answer.

We set out in the attached our answers to the specific questions raised and trust that the above and the attached are self-explanatory. However, please do contact me if you require any clarification of the points in this letter or if you would like to discuss any issues further.

Yours sincerely



Liz Murrall  
Director, Corporate Governance and Reporting

**ANNEX****IMA RESPONSE TO DISCUSSION PAPER (DP) ON GOING CONCERN AND FINANCIAL REPORTING*****Need for Guidance for Directors***

The FRC has observed that very significant changes have been made to the accounting standards that must be applied by directors of listed companies when preparing their consolidated accounts in compliance with IFRSs as adopted for use in the EU. However, these changes principally address financial statement disclosures rather than guidance on process.

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?

IMA considers that there is a continuing need for such guidance.

***Adequacy of proposed amendments to the existing guidance.***

The FRC has set out some proposed amendments to the existing Guidance for Directors with the objective of a minimal update to respond to changes in the supporting standards and rules. The FRC has not sought to identify substantial additional material that might be included.

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?

The paper proposes a fourth conclusion on the going concern status that directors: "have identified material uncertainties that may cast significant doubt about the ability of the company to continue as a going concern and so additional disclosures are required by IFRSs<sup>1</sup>".

Although this seeks to introduce some consistency in that it accords with the disclosure requirements in IAS 1, we consider it unhelpful to have both "doubt" and "significant doubt" as to whether a company will continue as a going concern in the Guidance.

First, to have two separate conclusions that there are:

- factors that cast doubt but where the going concern is still appropriate; and
  - 'material uncertainties that may cast significant doubt',
- is more likely to make the latter a self-fulfilling prophecy than if there were simply three conclusions.

---

<sup>1</sup> Paragraph 47 of page 18.

Secondly, an additional category whereby the “significance” of the doubt merits additional disclosure could mean that the reporting and disclosures of situations where there is simply a doubt could be reduced. We consider that any circumstances which give rise to doubts as to an entity’s going concern should be disclosed. Investors value the quality of the disclosures and any statements given need to be clear and unambiguous and cross referenced to other parts of the annual report and accounts, as appropriate.

In conclusion, whilst we would welcome more harmonization of disclosure requirements in this area we are not convinced that adding a fourth category in the current economic climate would be helpful. IMA believes that such changes should only be made when economic conditions are more benign in that changes now may raise more questions than they would answer.

### ***Redundant content in the proposed guidance***

The FRC has not set out to adopt a more radical approach to the proposed Guidance for Directors, such as a bottom up wholesale re-write. As a result, the FRC has not considered whether substantial parts of the text could be dropped.

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

Subject to our comments under question 2, IMA is content with the FRC’s approach and does not believe that parts of the text should be dropped.

### ***Approach to the inclusion of example text for directors to include in financial statements***

The FRC notes that since 1994 there has been a trend away from giving detailed guidance that prescribes standardised text towards encouraging directors to draft the text of disclosures in a way that is specific to their own facts and circumstances. However, the proposed guidance continues to contain example disclosures (see Section 2 paragraphs 49 and 51).

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

IMA believes that for financial reporting of this kind to be meaningful it needs to be tailored to the specific circumstances of the company concerned. However, the uncertainties in the current economic climate will undoubtedly mean that companies and auditors will have difficult judgements to make and there will be an increase in the liquidity and going concern disclosures. In this context, IMA believes it is helpful to include example disclosures in the guidance.

### ***Approach to the disclosure of a minimum period of review***

The FRC notes that the proposed text continues to be consistent with International

Standards on Auditing (UK and Ireland) which, among other things, require disclosure to be made by the auditor if the period considered by the directors in making their going concern assessment is less than one year from the date of approval of the financial statements. However, whilst IFRSs require management to take into account all available information about the future, this period need only be twelve months from the end of the reporting period.

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?

IMA supports the retention of a foreseeable future of at least 12 months from the date of approval of the accounts by the directors and the consistency with the International Standards on Auditing. IFRS require management to take into account all available information about the future, but specify that this period need only be twelve months from the end of the reporting period. IMA agrees that the FRC should maintain a difference from IFRS on the grounds that its disclosures are more beneficial to the interests of shareholders.