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Dear Sir

Going Concern and Liquidity Risk: Guidance for directors of UK companies

We are responding to your invitation to comment on the above exposure draft issued in May 2009. We are supportive of the FRC's initiative to update the existing guidance for directors, and the move to make it applicable to directors of all companies, including those that adopt the FRSSE. We also welcome the new guidance introduced for directors of listed companies in relation to half-yearly financial statements.

We make some general comments below, and then address the questions contained in the exposure draft.

General Comments

1. Additional clarity in respect of disclosures in the financial statements

We believe that in order to avoid confusion and conflict, the guidance for directors should align as closely as possible to accounting and auditing standards. There remains room for improvement in the guidance, in making it clear to directors that the expectation of them is to state clearly in the financial statements where there are "material uncertainties that may cast significant doubt" on the ability of the entity to continue as a going concern. The guidance stops short of recommending to directors that this exact phraseology should be used, but at the same time explains the obligation on the auditor to report if this level of clarity is not achieved. It would be better, rather than shifting the focus onto what the auditor needs to report, to remain focussed on what the directors should be reporting, and to give the strong message that using the exact phraseology is the way to ensure that a true and fair view is presented. It is difficult to conclude that the financial statements "state clearly" that there is a material uncertainty which may cast significant doubt if those words are not used. We acknowledge that the words are used in Example 3 in Appendix I, but it is also worth noting that paragraph 32 of the auditing standard, ISA 570, also includes reference to disclosure that the entity may be unable to realise its assets and discharge its liabilities in the normal course of business, and this wording is not currently incorporated into the Example.

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2. Summary of effect of the different conclusions

The table of possible conclusions in paragraph 20 is helpful and our understanding is that directors have been referring to this table already in making their assessments, even though the guidance is still in draft form. This means that it is particularly important to ensure that there is no risk of misunderstanding arising in this area of the guidance. We have some concerns around the wording in the final row of the table, where the conclusion is “The going concern basis is not appropriate”. It suggests that an unmodified audit report will be given, provided that the financial statements contain the necessary disclosures and the auditor agrees with the conclusion reached by the directors. In practice, auditors will wish to draw attention to the basis of preparation of the accounts (consistent with paragraph 36 of ISA 570, which states that the auditor may require an emphasis of matter). Also, there may be circumstances where it is not possible to audit the adjustments necessary to apply a non-going concern basis, necessitating a qualified opinion, or a disclaimer. Therefore, it is misleading to suggest that the report will be unmodified. We also suggest that the wording in the table to describe the conclusions reached, aligns with wording elsewhere in the guidance which discusses the three conclusions, for example in paragraph 57, to ensure that there is no potential for confusion.

3. Group scenarios

The guidance might helpfully include some more material on group scenarios. In practice, this is an area around which there is much difficulty for directors in arriving at their conclusions. For example, for directors of wholly owned subsidiaries, where there are substantial inter-company balances that have built up over a number of years, with accompanying comfort letters to support the debts, the directors need to form an objective view of the likelihood of settlement. It is unclear as to what would constitute sufficient rigorous procedures for the directors to satisfy themselves about not only the financial wherewithal to provide the support, but also the genuine intention to do so. There is also some difficulty around the timing of signing statutory accounts, to allow for a full and proper assessment to be made.

4. Documentation

The guidance would benefit from more emphasis on the need for directors to document their assessments, including a clear representation of the rationale for reaching their conclusions and evidence of approval at board level.

5. Events outside the look-forward period

It should be clear in the guidance that whilst directors should look forward 12 months from date of approval, this does not mean that a major event falling just outside of that period can be ignored. Such events, which may include renewal of financing arrangements for example, should be factored into the directors’ assessment.

6. Financial services sector specific concerns

In some areas, the guidance could usefully provide additional considerations appropriate to the financial sector. For example, the guidance in paragraphs 29 & 30 addresses the generic techniques of forecasts and budgets and the need to subject them to sensitivity analysis. For the financial services sector, especially those entities that are deposit-takers, the equivalent is scenarios and stress-testing them. In order to make it relevant to such entities, the guidance should pick up liquidity and capital as separate issues, in addition to forecasts and budgets. Another example is the section on sensitivity analysis and stress testing: paragraph 43 of the guidance discusses using sensitivity analysis to ensure that there will be no expected breaches of covenants. For entities in the financial services sector, this isn’t usually directly applicable, so it

would be better to reword as follows: “breaches of covenants or other triggers within funding arrangements or other arrangements.”

As a final point, it might be appropriate to include an example in Appendix I that relates directly to the financial services sector.

Responses to individual questions in the exposure draft

Question 1: Do you agree that the FRC should provide guidance on going concern relevant for directors of all companies? If so, do you believe that the Exposure Draft achieves this in a reasonably balanced way?

Yes, we agree that it is appropriate for the FRC to provide guidance in this area. We are supportive of the objectives set out in the exposure draft, and believe that the objectives are largely met, other than in the specific instances we refer to in this response letter.

Question 2: Do you agree with the principles as drafted? If not how would you amend them?

Yes we agree with them, and we don’t have suggestions to alter them.

Question 3: Do you agree with the three conclusions? If not, please explain what alternative you would suggest?

Yes we agree with the three conclusions. However, please see our comments above in relation to item 2: Summary of the effect of the different conclusions. Also, we believe that there may be scope to allow some flexibility around how much needs to be disclosed, depending on where on the spectrum a company might fall within each category.

Question 4: Do you agree that the directors should disclose when the period they have considered is less than twelve months from the date of approval of half-yearly and interim financial statements that give a true and fair view?

Yes we do agree with this. In practical terms, our perception is that directors tend to look at what the position will be for their going concern assessment for the annual financial statements at their next year end, so in a sense they look ahead 18 months. Banks often push clients to prepare forecasts for even longer periods than 12 months from the date of approval. Therefore we believe that directors are unlikely to see this requirement as overly onerous. It should only be in exceptional circumstances that directors do not consider the 12 month period.

Having said that, there may be issues in multi-national group scenarios with the confusion that arises because some auditors apply the international audit standard (ISA 570), which only looks for consideration of 12 months from the balance sheet date, and some overseas companies, both parents and subsidiaries, may therefore work to this standard. Nevertheless, the guidance should retain its clear message of 12 months from approval.

Question 5: Do you believe that it would be appropriate to replace the existing Guidance for directors with this document for periods ending on or after 31 December 2009? If not, what alternative application date would you suggest?

We do believe that it would be appropriate to make the revised document applicable for December 2009 year ends, on condition that appropriate involvement of the FSA has been secured, such that they are able to follow due process to make the necessary adjustments to the Listing Rules to align with the implementation of the FRC’s guidance.

If you have any questions or comments about this response, please contact Margaret Cassidy (020 7213 1285) or Geoff Swales (020 7213 3350).

Yours faithfully

PricewaterhouseCoopers LLP