Financial Reporting Council

Going Concern and Liquidity Risk: Guidance for Directors of UK Companies 2009

THE PRINCIPLES

ASSESSING GOING CONCERN

1 Directors should make and document a rigorous assessment of whether the company is a going concern when preparing annual and half-yearly financial statements. The process carried out by the directors should be proportionate in nature and depth depending upon the size, level of financial risk and complexity of the company and its operations.

THE REVIEW PERIOD

2 Directors should consider all available information about the future when concluding whether the company is a going concern at the date they approve the financial statements. Their review should usually cover a period of at least twelve months from the date of approval of annual and half-yearly financial statements.

DISCLOSURES

3 Directors should make balanced, proportionate and clear disclosures about going concern for the financial statements to give a true and fair view. Directors should disclose if the period that they have reviewed is less than twelve months from the date of approval of annual and half-yearly financial statements and explain their justification for limiting their review period.

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Introduction and overview

1. The purpose of this Guidance is to bring together the requirements of company law, accounting standards and the Listing Rules on going concern and liquidity risk for small, medium and large UK companies and to provide further assistance on their application.

2. This Guidance applies to accounting periods ending on or after 31 December 2009. It supersedes the guidance issued in 1994 for directors of listed[1] companies and extends the application of the guidance to all sizes of company[2] for annual and half-yearly financial statements.

3. Going concern is a fundamental accounting concept that underlies the preparation of financial statements of all UK companies. Under the going concern concept it is assumed that a company will continue in operation and that there is neither the intention nor the need either to liquidate it or to cease trading.

4. This Guidance provides a framework to assist directors, audit committees and finance teams in determining whether it is appropriate to adopt the going concern basis for preparing financial statements and in making balanced, proportionate and clear disclosures. Separate standards and guidance have been issued by the Auditing Practices Board to address the work of auditors in relation to going concern.

5. Directors of all companies are encouraged to focus on the principles contained in this Guidance and to apply them in a manner proportionate to the nature of their business.

6. The principles contained in this Guidance should be applied by directors of all companies when preparing annual and half-yearly[3] financial statements. For companies that are subject to the Disclosure and Transparency Rules (DTR) of the FSA, or the AIM Rules for Companies, this Guidance need not be applied in the preparation of communications which do not comprise financial statements such as interim management statements prepared in accordance with DTR 4.3.

Making an assessment

7. The Financial Reporting Standard for Smaller Entities (FRSSE), UK Generally Accepted Accounting Practice for medium and large UK companies (UK GAAP) and International Financial Reporting Standards as adopted by the EU (IFRS) require directors to satisfy themselves that it is reasonable for them to conclude whether it is appropriate to prepare financial statements on a going concern basis.

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[1] A listed company is a UK company that has any class of its securities admitted to the Official List maintained by the FSA in accordance with section 74 of the Financial Services and Markets Act 2000.

[2] The Guidance has been drafted in the context of companies but it may also be useful to the management of other entities that produce financial statements that are intended to give a true and fair view.

[3] In this Guidance the expression "half-yearly financial statements" is used to be consistent with the terminology used in the DTR. The Guidance may also be useful for directors when preparing other interim financial statements intended to give a true and fair view.

These requirements are not intended to, and do not, guarantee that a company will remain a going concern until the next annual or half-yearly financial statements are issued.

8. Where companies are facing difficult economic conditions and/or are in financial difficulty this will necessitate particularly careful consideration by directors when making their assessment. If the directors consider that the company might no longer be a going concern they may need to take legal advice.

9. Small companies may take advantage of certain concessions on the accounting standards to be applied and the content of their financial statements. However, directors of small companies are not relieved from the obligation to assess going concern when they prepare annual financial statements. The extent of the procedures necessary to make an assessment for a small company will generally be less than would be appropriate for larger more complex companies.

10. A going concern assessment involves consideration of the facts and circumstances of an individual company. If a subsidiary of a parent company has no realistic alternative but to cease trading, this does not necessarily mean that the parent company should produce its financial statements on other than a going concern basis. However, such circumstances are likely to trigger specific provisions of the FRSSE, UK GAAP and IFRS, such as a requirement to perform impairment reviews, and are likely to require additional disclosures so that the financial statements give a true and fair view.

11. There will be economic circumstances that present particular challenges for all of the parties involved in the preparation of annual and half-yearly financial statements and for the users of such financial statements. In such circumstances:
    - directors need to ensure that they prepare thoroughly for their assessment of going concern and make appropriate disclosures;
    - auditors need to ensure that they consider fully the going concern assessments and refer to going concern in the auditor’s report only when appropriate; and
    - investors and lenders need to be prepared to read and evaluate all of the relevant information in annual reports and financial statements before reacting.

12. Directors should plan their assessment of going concern as early as practicable including deciding on the processes, procedures, information, analyses and board papers that will be needed. These plans should also address the evidence to be obtained, including identifying any potential remedial actions that may need to be addressed, to support their conclusion prior to their approval of the annual or half-yearly financial statements. Addressing these challenges well before the preparation of such financial statements may mitigate problems arising at the last minute that might unsettle investors and lenders unnecessarily.

13. Early discussions with the company’s auditor about these plans may help minimise the risk of last-minute surprises. It is also likely to be helpful if a draft of the relevant disclosures about going concern and liquidity risk is prepared and discussed with the auditor well before the end of the reporting period.

14. Directors need to evaluate which one of three potential conclusions is appropriate to the specific circumstances of the company. The directors may conclude:
    - there are no material uncertainties that may cast significant doubt about the company's ability to continue as a going concern; or
    - there are material uncertainties related to events or conditions that may cast significant doubt about the company's ability to continue as a going concern but the going concern basis remains appropriate; or
    - the use of the going concern basis is not appropriate i.e. the company has no realistic alternative but to cease trading or go into liquidation or the directors intend to cease trading or place the company into liquidation.

15. Care should be taken by the directors to evaluate fully all of the facts and circumstances and to make a balanced assessment of the disclosures that are necessary. For example, lenders may be reluctant to provide positive confirmation to the directors that facilities will continue to be available. This reluctance may extend to companies with a profitable business and relatively small borrowing requirements. There may be a number of understandable reasons why a lender may be reluctant to confirm that a facility will be available in the future including:
    - as a matter of policy the lender does not provide such confirmations to its customers during difficult economic conditions;
    - the company and its lenders are engaged in negotiations about the terms of a facility (e.g. the interest rate). However, there is no evidence that the lender is reluctant to lend to the company; and
    - the lender renewed a rolling facility immediately prior to the date of the issuance of the financial statements and is reluctant to go through the administrative burden to confirm the facility will be renewed again in a year's time.

16. The absence of confirmations from lenders does not of itself necessarily cast significant doubt upon the ability of the company to continue as a going concern nor require the auditor necessarily to refer to going concern in its auditor's report.

17. Market conditions impact companies differently. It should not be assumed that difficult market conditions, affecting many companies, mean that a material uncertainty exists about a specific company's ability to continue as a going concern. Equally, material uncertainties may exist about a company's ability to continue as a going concern in times of relatively benign economic circumstances. Whatever the economic circumstances, it is important that a rigorous assessment is made and documented and that financial statements contain balanced, proportionate and clear disclosures of going concern uncertainties and liquidity risk as necessary to give a true and fair view.

The review period

18. The FRSSE, UK GAAP and IFRS do not specify a maximum period that should be considered by directors as part of the assessment of going concern. The extent of the review period is a matter of judgment based on facts and circumstances. The FRSSE and UK GAAP provide that disclosure should be made where the review period considered by the directors is less than twelve months from the date of approval of the annual financial statements. Directors of companies applying this Guidance when preparing IFRS annual and half-yearly financial statements and UK GAAP half-yearly financial statements should also make this disclosure in those financial statements.

19. The practical effect of these disclosure requirements will usually be that directors of UK companies will adopt a review period of not less than twelve months from the date of approval of annual and half-yearly financial statements but, in rare cases, when they do not they should explain why.

Disclosures

20. The FRSSE, UK GAAP and IFRS require explicit disclosure of the material uncertainties that directors are aware of arising from their assessment of going concern that may cast significant doubt on the company's ability to continue as a going concern.

21. Disclosure will also need to be made about liquidity risk, other uncertainties and key assumptions concerning going concern necessary to give a true and fair view. In addition, disclosure of principal risks and uncertainties will be needed in the directors' report[4].

22. Directors of listed companies incorporated in the UK are required by Listing Rule 9.8.6R (3) to include in their annual financial report a statement that the business is a going concern, together with supporting assumptions or qualifications as necessary, that has been prepared in accordance with this Guidance[5].

23. The auditor is required to make its own assessment of the directors' conclusion on going concern. If the auditor concludes that a material uncertainty exists related to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern, it is required to modify the auditor's report. Even if the material uncertainty is explained fully by the directors in the financial statements the auditor is required to include an emphasis of matter paragraph in its report.

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[4] This does not apply to small companies.

[5] Text that is shown in blue shading sets out relevant requirements of the Listing Rules. These requirements are applicable only to listed UK companies.

Summary of effect of the different conclusions

24. The combination of the facts and circumstances at the date of approval of the financial statements will generally result in one of the following three conclusions that lead to specific disclosures:

Conclusion	Resulting disclosures	Consequence(s) for the auditor's report
No material uncertainties related to events or conditions that may cast significant doubt about the ability of the company to continue as a going concern have been identified by the directors.	Going concern is presumed in preparing financial statements. Disclosure will need to be made about liquidity risk, other uncertainties and key assumptions concerning going concern as necessary. Disclosure of principal risks and uncertainties will be needed in the directors' reports of companies other than small companies. ***See Appendix I example 1 and Appendix II examples 1 (a), 1 (b) and 2.*** **The Listing Rules require that a statement be made that the business is a going concern together with supporting assumptions as necessary.**	Unmodified report provided the auditor concurs with the directors' assessment and supporting disclosures.
Material uncertainties related to events or conditions that may cast significant doubt about the ability of the company to continue as a going concern have been identified by the directors, but the going concern basis remains appropriate.	Disclosures explaining the specific nature of the material uncertainties that may cast significant doubt and explaining why the going concern basis has still been adopted. Other disclosures will have to be made as described above. ***See Appendix I example 2 and Appendix II example 3.*** **The Listing Rules require that a statement be made that the business is a going concern together with supporting assumptions or qualifications as necessary.**	Modified report including an emphasis of matter paragraph highlighting the existence of material uncertainties that may cast significant doubt provided the auditor concurs with the directors' assessment and supporting disclosures.
The going concern basis is not appropriate as the company has no realistic alternative but to cease trading or go into liquidation, or the directors intend to cease trading or place the company into liquidation.	Disclosures explaining the basis of the conclusion and the accounting policies applied in preparing the financial statements on other than a going concern basis and any uncertainties about the carrying amounts of assets and liabilities.	Unqualified opinion provided that the financial statements contain the necessary disclosures and the auditor considers the basis to be appropriate to the specific facts and circumstances. The auditor may include an emphasis of matter paragraph. If the decision and its implications are not adequately explained the auditor may determine it necessary to modify its opinion.

One – Assessing going concern

Principle 1: Directors should make and document a rigorous assessment of whether the company is a going concern when preparing annual and half-yearly financial statements. The process carried out by the directors should be proportionate in nature and depth depending upon the size, level of financial risk and complexity of the company and its operations.

Guidance relevant to all companies

25. The FRSSE, UK GAAP and IFRS require directors to make a going concern assessment. If the directors intend to cease trading, or go into liquidation or they have no realistic alternative but to do so, the use of the going concern basis of accounting ceases to be appropriate and this is likely to lead to significant differences in the carrying amounts of assets and liabilities recognised in the financial statements.

26. The assessment of going concern is made at the date that the directors approve the annual or half-yearly financial statements, and takes into account the relevant facts and circumstances at that date. Any judgment made, whilst reasonable at the time, can be valid only at that time and can be overturned by subsequent events. The assessment should be documented in sufficient detail to explain the basis of the directors' conclusion with respect to going concern. The assessment should be adopted by the Board.

Small companies

27. The extent of the directors' review process will depend upon the size and nature of the company and the complexity of its business. Small companies tend to be dependent upon a single provider of finance, have only one business activity and a limited number of creditors including the tax authorities. As a result the extent of the process and procedures for a small company are likely to be much simpler than that for medium and large companies. However, it is still important that the assessment is carried out and documented and addresses, to the extent necessary, the directors' plans to manage the company's borrowing requirements, the timing of cash flows and the company's exposure to contingent liabilities.

Subsidiary companies

28. Directors of subsidiary companies of a group need to make their own going concern assessment taking into account the specific facts and circumstances of the subsidiary company and in particular:
    - the need for support[6] from the parent company or fellow subsidiaries;
    - the ability and willingness of the parent company or fellow subsidiaries to provide such support; and
    - the risks to the company's going concern status arising from support that it has undertaken to provide to other members of the group.

29. The directors should consider the degree of autonomy that the subsidiary company has and how the subsidiary's business fits into the group's activities and future plans, and the particular business risks that might arise that could threaten the appropriateness of adopting the going concern basis of

[6] "Support" for this purpose encompasses both financial and non-financial support.

accounting for the subsidiary. The adequacy of the evidence of any parent company support is a matter for the judgment of the directors of the subsidiary company. Their judgment usually incorporates their experience of dealing with the parent company over time, taking into account recent events and current circumstances.

30. One way of mitigating the potential difficulty that a subsidiary's directors may have when considering the group's ability to offer any necessary support, is for the financial statements of subsidiary companies to be completed and approved close to the date of approval of the parent company and group financial statements. Where this is practical it avoids the need for the group to undertake an exercise to reconsider budgets and forecasts if the subsidiary's financial statements are completed and approved at a later date. Example 1(b) of Appendix II provides illustrative disclosures for a subsidiary company.

Procedures relevant to all companies

31. Directors are best placed to assess which factors are likely to be of greater significance to their company. These factors will vary by industry and from company to company within a particular industry. For example, one company may have significant economic dependence on a particular customer, whilst another company may have a large number of customers.

Forecasts and budgets

32. Forecasting and budgeting are long-established techniques in business management. When the critical assumptions underlying the forecasts and budgets are challenged and subjected to sensitivity analysis, the refined forecasts and budgets have an increased likelihood of predicting the outcome.

33. Directors should prepare a budget, trading estimate, cash flow forecast or other equivalent analysis covering such period as they consider appropriate.

Borrowing facilities

34. The availability of borrowing facilities may be dependent upon the company's compliance with specific terms and conditions (covenants). An analysis of borrowing documentation should be undertaken to ensure that all critical terms and conditions are identified so that the risks to continued compliance can be assessed.

35. If there is uncertainty over the contractual arrangements with lenders and other providers of finance, directors should seek confirmation from the lenders of the principal terms and conditions. However, the absence of confirmations does not necessarily cast significant doubt upon the ability of a company to continue as a going concern.

36. The onus is on the directors to be satisfied that there are likely to be appropriate and committed financing arrangements in place. The facilities available to the company should be compared to the company's expected cash requirements from such facilities, as indicated by the cash flow forecasts, budgets or trading estimates. Where necessary, early discussion of any potential deficits, arrears or contractual breaches with the company's bankers may prevent potential problems crystallising.

Procedures more relevant to medium and large companies

Medium and long-term plans

37. Directors of medium and large companies generally assess further periods beyond formal budgets and forecasts by way of medium or long-term plans that give an indication in general terms of how the directors expect the business of the company to fare.

Products, services and markets

38. Directors should obtain information about the major aspects of the economic environment within which the company operates. They should consider the size of the market, its strength, their market share and assess whether there are any economic, political or other factors which may cause the market to change. This should be done for each of the main product or service markets.

39. Directors should assess whether their products or services are compatible with their market projections in terms of market position, quality and expected life.

Timing of cash flows

40. Directors should assess whether their financial plans indicate an adequate matching of projected cash inflows with projected cash outflows. The projected outflows should include liabilities, such as loan repayments, payment of tax liabilities and other commitments.

Contingent liabilities

41. Directors should consider the company's exposure to contingent liabilities. These should include sources of potential cash outflows during the review period relating to legal proceedings, guarantees, margin or other credit support provisions under derivative contracts, environmental costs and product liability.

Financial and operational risk management

42. There are many types of financial and operational risks facing a company and directors should identify which risks are most significant to their company. For example, exposure to fixed-price contracts and to movements in foreign currency exchange rates may be the most significant risks for a construction company engaged in overseas markets. Consideration should also be given to counterparty risks that arise from concentration on key suppliers or customers who may themselves be facing financial difficulty. The directors should consider how such risks could affect the company and how they are managed in practice.

Sensitivity analysis and stress testing

43. Sensitivity analysis should be prepared to enable an understanding to be gained of the critical assumptions that underlie the budgets and forecasts. Sensitivity analysis involves assessing the extent to which the headroom against facilities varies with changes in assumptions. It may, depending upon the facts and circumstances, be appropriate to test the impact of changes of the following:
    - interest rates;
    - exchange rates;

- market share;
- raw material costs;
- expected selling costs;
- a customer or supplier failing;
- availability of borrowings;
- margin requirements consequent on varying underlying prices relevant for derivative contracts during their life;
- likely extent of damages arising from unfavourable legal judgments; and
- taxation rates.

44. Sensitivity analysis should be used to seek to ensure that there are no unexpected:
    - shortfalls in facilities against requirements; or
    - breaches of covenants or other triggers within funding arrangements.

45. Where sensitivity analysis indicates that there is a significant risk that the headroom between cash requirements and facilities available will be insufficient, the company should stress test its assumptions. Stress testing enables the directors to assess the effect of a combination of pessimistic but plausible estimates or assumptions.

Auditor's report

46. International Standard on Auditing (UK and Ireland) 570 "Going Concern" requires the auditor to evaluate the directors' assessment of the company's ability to continue as a going concern. If the auditor concludes that a material uncertainty exists which may cast significant doubt about the ability of the entity to continue as a going concern it is required to modify its report by including an emphasis of matter paragraph provided that the circumstances are fully explained in the financial statements.

Half-yearly financial statements

47. Companies with securities subject to the DTR, admitted to trading on AIM or traded on the PLUS-quoted market are required to prepare an interim report which will include half-yearly financial statements.

48. Directors will need to exercise judgment about the nature and extent of the procedures that they apply to assess the use of the going concern assumption at the half-yearly date and the need for disclosures about new activities, events and circumstances. Issues which might trigger a need to re-examine the going concern assumption and going concern and liquidity risk disclosures include:
    - a significant adverse variation in operating cash flows between prior budgets and forecasts and the outturn in the first half of the year;
    - a significant reduction in revenues or margins forecast for the second half of the year;
    - a failure to obtain renewal or extension of bank facilities that had been anticipated; and
    - a failure to sell capital assets for their expected amounts or within previously forecast time-frames.

49. If going concern has become a significant issue since the last annual financial statements, directors should undertake procedures similar to those that they would have carried out for annual financial statements to ensure that all relevant issues have been identified and considered.

50. Where no new issues have been identified that raise questions about the assessment made at the last annual financial statements, the directors will need to undertake procedures to roll forward the previous budgets and forecasts by the length of the half-yearly period.

Auditor's half-yearly review report

51. The auditor may be engaged to review half-yearly financial statements. The APB's International Standard on Review Engagements (UK and Ireland) 2410 "Review of interim financial information performed by the independent auditor of the entity" requires the auditor, among other things, to inquire whether the directors have changed their assessment of the entity's ability to continue as a going concern.

52. When the auditor becomes aware of events or conditions that may cast significant doubt on the company's ability to continue as a going concern, the auditor is required to inquire of the directors as to their plans for future actions, the feasibility of those plans and whether the directors believe that the outcome of those plans will improve the situation.

Questions for boards to consider

53. Appendix III identifies key questions which boards may need to consider when carrying out their role in relation to annual and half-yearly financial statements.

Two – The review period

Principle 2: Directors should consider all available information about the future when concluding whether the company is a going concern at the date they approve the financial statements. Their review should usually cover a period of at least twelve months from the date of approval of annual and half-yearly financial statements.

Annual financial statements

54. Under this Guidance, directors of all companies should consider all available information about the future at the date of approval of the financial statements including the information obtained from budgets and forecasts. The FRSSE, UK GAAP and IFRS each provide for a minimum period that should be reviewed by directors as part of their assessment of going concern. However, the extent of the review period is a matter of judgment based on facts and circumstances and it may be appropriate to obtain information for longer periods.

55. Paragraph 26 of IAS 1 "Presentation of financial statements" provides that "management takes into account all available information about the future, which is at least, but not limited to, twelve months from the end of the reporting period". The FRSSE and UK GAAP give rise to a similar outcome by requiring specific disclosure where the period reviewed by the directors is less than twelve months from the date of approval of the financial statements.

Auditor's report

56. If the period of the directors' review is less than twelve months from the date of approval of the financial statements and the directors have not disclosed that fact, the auditor is required to do so in the auditor's report.

Half-yearly financial statements

57. Under this Guidance, directors of all companies should consider all available information about the future at the date of approval of half-yearly financial statements including the information obtained from budgets and forecasts. The Accounting Standards Board (ASB) has issued a non-mandatory statement "Half-Yearly Financial Reports" for companies complying with UK GAAP. The statement provides that the accounting policies and presentation should be consistent with those applied in the latest published annual financial statements unless (a) the policies and presentation are to be changed in the subsequent annual financial statements or (b) the FSA otherwise agrees.

58. Companies subject to the DTR are required to produce a half-yearly financial report containing financial statements. Where such companies use IFRS they are required to apply IAS 34 "Interim Financial Reporting". It provides that the same recognition and measurement principles be applied to half-yearly financial statements as are applied to annual financial statements. Consequently, the minimum review period requirement in paragraph 26 of IAS 1 applies to financial statements for a half-yearly period as described in IAS 34. Where such companies continue to use UK GAAP, the DTR refers to the ASB's statement described in paragraph 57.

Three – Disclosures

Principle 3: Directors should make balanced, proportionate and clear disclosures about going concern for the financial statements to give a true and fair view. Directors should disclose if the period that they have reviewed is less than twelve months from the date of approval of annual and half-yearly financial statements and explain their justification for limiting their review period.

All companies

59. Directors of all companies need to reach a conclusion about the ability of the company to continue as a going concern. The disclosures which follow from the directors' conclusion will be:
    - **the use of the going concern basis of accounting is appropriate because there are no material uncertainties related to events or conditions that may cast significant doubt about the ability of the company to continue as a going concern.** The directors should use the going concern basis of accounting in preparing the financial statements and make the necessary disclosures, including those about liquidity risk, necessary to give a true and fair view; or
    - **the use of the going concern basis is appropriate but there are material uncertainties related to events or conditions that may cast significant doubt about the ability of the company to continue as a going concern.** The directors should use the going concern basis of accounting in preparing the financial statements, disclose the material uncertainties that may give rise to significant doubt and make the disclosures, including those about liquidity risk, necessary to give a true and fair view; or
    - **the going concern basis is not appropriate.** Such a conclusion will result in abandoning the going concern basis of accounting in preparing the financial statements and making detailed disclosures about the basis of accounting that has been used.

60. Disclosure requirements relevant to the directors' going concern assessment are set out in the FRSSE, UK GAAP, IFRS, the Companies Act 2006 (CA 2006) and (for certain listed companies) the Listing Rules. The following paragraphs provide an overview of these requirements. Paragraphs 79 to 83 provide recommendations as to how these diverse requirements might be drawn together into a single place in the company's financial statements.

UK GAAP (including FRSSE)

61. The FRSSE and UK GAAP require disclosure where directors identify a material uncertainty that may lead to significant doubt about going concern. The disclosure should set out the facts and circumstances in a manner that is proportionate to the nature of the company.

Business Review required by CA 2006 to be included in directors' reports of medium and large companies

62. The Business Review is required to be a balanced and comprehensive analysis of the development and performance of the company's business during the financial year and the position of the company at the end of that year, consistent with the size and complexity of the business. In particular, it must include a description of the principal risks and uncertainties facing the company.

63. In the case of a quoted company, the Business Review is also required to provide, to the extent necessary for an understanding of the business, information on a number of other matters including:
    - the main trends and factors likely to affect the future development, performance or position of the company's business; and
    - information about persons with whom the company has contractual or other arrangements that are essential to the business of the company[7].

64. Directors need to explain in the Business Review the principal risks and uncertainties facing the company which should include any particular economic conditions and financial difficulties that the company is experiencing. One of the purposes of the Business Review is to help the shareholders assess how the directors have performed their duty to promote the success of the company, so it is reasonable to expect that it will also contain an account of how the directors intend to respond to these risks and uncertainties. Issues which may require disclosure depend upon individual facts and circumstances include:
    - uncertainties about current financing arrangements (whether committed or uncommitted);
    - potential changes in financing arrangements such as critical covenants and any need to increase borrowing levels;
    - counterparty risks arising from current credit arrangements (including the availability of insurance where relevant) with either customers or suppliers;
    - a dependency on key suppliers and/or customers; and
    - uncertainties posed by the potential impact of the economic outlook on business activities.

Disclosure of the existence of material uncertainties that may cast significant doubt upon the company's ability to continue as a going concern

65. The FRSSE, FRS 18 "Accounting policies" and IAS 1 all require directors to disclose the existence and nature of the uncertainties where they have concluded that there are "material uncertainties that may cast significant doubt upon the entity's ability to continue as a going concern".

66. The FRSSE, FRS 18 and IAS 1 do not specify that this precise phrase must be used. However, when preparing their financial statements directors will wish to bear in mind the need for the disclosures to be clear about them having identified a material uncertainty that has led to significant doubt about going concern. They will also wish to bear in mind the obligation on the auditor to report if that level of clarity has not been achieved in the words that have been used, and made clear that the company may be unable to realise its assets and discharge its liabilities in the normal course of business.

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7 However, CA 2006 does not require the disclosure of information about a person if the disclosure would, in the opinion of the directors, be seriously prejudicial to that person and contrary to the public interest.

UK GAAP (including the FRSSE)

67. The FRSSE and UK GAAP provide that an explicit disclosure should be made if the period of the review for going concern has not extended to twelve months from the date of approval of the financial statements. Such disclosures should explain the directors' justification for their decision.

IFRS

68. A failure to consider a period of at least twelve months from the balance sheet date would be contrary to the requirements within accounting standards for companies applying IFRS. This would require directors to justify this departure.

Other risk disclosures required by accounting standards

69. In addition, for medium and large companies (and small companies that do not apply the FRSSE) a number of UK GAAP and IFRS standards require specific disclosures to be made about liquidity risk and other risks that may have a bearing on a going concern assessment including:

Disclosure	IFRS (2009)	UK GAAP (2009/10)
Disclosures relating to risks arising from financial instruments, including liquidity risk where it is material.	IFRS 7 paragraphs 31 to 42	FRS 29 paragraphs 31 to 42 (where adopted)
Disclosure is encouraged of undrawn borrowing facilities and any restrictions on the use of those facilities such as covenant requirements, where relevant.	IAS 7 paragraph 50 (a)	For certain companies that have not adopted FRS 26, FRS 13 paragraph 40 requires disclosure of the maturities of material undrawn committed borrowing facilities
Disclosure of defaults and covenant breaches.	IFRS 7 paragraphs 18 and 19	FRS 29 paragraphs 18 and 19 (where adopted)
Disclosure of sources of estimation uncertainty about the carrying amounts of assets and liabilities.	IAS 1 paragraphs 125 to 133	FRS 18 paragraphs 50 to 55 and 57

Liquidity risk

70. Liquidity risk is the risk that an entity will encounter difficulty in meeting its obligations associated with financial liabilities. FRS 29 "Financial Instruments: Disclosures" and IFRS 7 "Financial Instruments: Disclosures" require a company to make both qualitative and quantitative disclosures concerning liquidity risk, where it is a material financial risk.

71. Where liquidity risk is material, FRS 29 and IFRS 7 require:
    - disclosure of information that enables users to evaluate the nature and extent of the entity's exposure to liquidity risk;

- narrative disclosures explaining how liquidity risk arises in the business and how it is managed in practice;
- summary numerical data about liquidity risk based on the information that is provided to key management personnel, often the Board of Directors; and
- certain mandatory disclosures such as a maturity analysis of financial liabilities.

72. For companies using IFRS, the disclosures required by IFRS 7 are supplemented by disclosures required by other IFRS standards. For example, IAS 7 "Statement of Cash Flows" requires disclosure of undrawn borrowing facilities where relevant to users' understanding of the financial position and liquidity of the entity and IFRS 7 requires disclosure of defaults and breaches of loan terms and conditions.

Statement on going concern required to be made by certain listed companies

73. **Listing Rule 9.8.6R (3) of the FSA requires that the following must be included in the annual financial reports of listed companies incorporated in the United Kingdom:**
"…a statement made by the directors that the business is a going concern, together with supporting assumptions or qualifications as necessary, that has been prepared in accordance with Going Concern and Liquidity Risk: Guidance for Directors of UK Companies 2009, published by the Financial Reporting Council". Listing Rule 9.8.10R (1) requires the auditor to review the directors' statement before the annual report is published.

Preliminary announcements

74. Preliminary announcements of annual results form one of the focal points for investor interest, primarily because they confirm or update market expectations.

75. **Under the Listing Rules such announcements are voluntary, although if made their contents are subject to minimum requirements. One such requirement (Listing Rule 9.7A.1 (2)) is "If a listed company prepares a preliminary statement of annual results the statement must be agreed with the company's auditor prior to publication".**

76. **Directors may need to consider whether, in light of the requirement "to include any significant additional information necessary for the purpose of assessing the results being announced" (Listing Rule 9.7A.1 (5)) they need to make appropriate disclosures about going concern in their preliminary announcements.**

77. **The Listing Rules also require specific disclosure in the preliminary announcement of the nature of any likely modification contained in the auditor's report that is to be included with the annual financial report.**

78. The FSA has commented in Issue 20 of List! published in January 2009 that "Directors may need to consider whether, in light of the requirement to include any significant additional information necessary for the purpose of assessing the results being announced, there is a need to make appropriate disclosures about going concern in their preliminary announcements. In addition, the Listing Rules require specific disclosure in the preliminary announcement of any likely modification contained in the

auditor's report that is to be included with the annual financial report. This would, for example, include an emphasis of matter paragraph in relation to going concern."

Balanced, proportionate and clear disclosures

79. Addressing the requirements of the FRSSE, UK GAAP, IFRS, CA 2006 and the Listing Rules that apply to a company may lead it to address going concern and liquidity risk in different sections of its annual report and financial statements. This may create difficulties for investors and other stakeholders in seeking to obtain a clear, comprehensive and cohesive understanding of the issues facing the company.

80. It is helpful to investors and other stakeholders if all of these disclosures are brought together in a single place in the company's financial statements. It may be necessary to provide a cross reference to that single place from other parts of the annual report. If it is not practicable to provide all of the information in a single place, it is still helpful if the key disclosures are brought together by way of a note that includes appropriate cross references to information in the financial statements and from the financial statements to information included elsewhere in the annual report.

81. Balanced, proportionate and clear disclosures would include the following components:
    - the key disclosures or references thereto;
    - the particular factors which the directors have considered in reaching a conclusion on going concern; and
    - a concluding statement as to whether the use of the going concern basis of accounting is appropriate, explaining the basis of that conclusion.

82. Clutter caused by excessive disclosure of irrelevant or immaterial data has the capacity to detract from the ability of users of financial statements to identify the relative significance of issues facing a company and could undermine the ability of financial statements to provide a true and fair view.

83. Examples illustrating such disclosures and how they can be brought together are included in Appendix I for small companies and in Appendix II for other companies.

Auditor's report

84. The auditor is required to consider the disclosures about going concern and liquidity risk made in the financial statements. If the auditor concludes that the disclosures are not adequate to meet the requirements of accounting standards and CA 2006, including the need for financial statements to give a true and fair view, the auditor is required to qualify its opinion and to provide its reasons for doing so.

85. CA 2006 requires the auditor to review the Directors' Report and to state in its report whether the information given in the Directors' Report is consistent with the financial statements.

Half-yearly financial statements

86. IAS 34 provides that entities may elect to provide less information at half-yearly dates, as compared with their annual financial statements, in the interests of timeliness and cost considerations and to avoid

repetition of information previously reported. Instead the focus of half-yearly financial statements is on new activities, events and circumstances which have not previously been reported.

87. Directors will need to exercise judgment in determining the disclosures about going concern and liquidity risk that they should include in a set of half-yearly financial statements. Practical experience suggests that new events and circumstances are likely to arise quite often in businesses facing financial difficulties, for example as borrowings are renegotiated and assets and businesses are sold or closed. In these circumstances, it is likely that half-yearly financial statements will include additional explanation about going concern and liquidity risk. In other cases, a short statement confirming the use of the going concern basis should suffice.

88. Where the period considered by the directors in assessing going concern for a half-yearly period has been limited to a period of less than twelve months from the date of the approval of the half-yearly financial statements, directors complying with this Guidance should disclose that fact and provide their justification.

Auditor's half-yearly review report

89. The auditor is required to consider the adequacy of the disclosures about going concern in the half-yearly financial statements and, where there is a material uncertainty that may cast significant doubt on the entity's ability to continue as a going concern (and the disclosures made are adequate), to add an emphasis of matter to its review report. If there is a material uncertainty that may cast significant doubt about the ability of the company to continue as a going concern which is not adequately disclosed the auditor is required to express a qualified or adverse conclusion.

Appendix I – Examples of going concern disclosures for small companies

The purpose of this Appendix is to illustrate the guidance in paragraph 61. In practice, such disclosures should be specific to the individual circumstances of each company.

No material uncertainties that may cast significant doubt about the ability of the company to continue as a going concern have been identified by the directors

Example 1 – A small company that has adopted the FRSSE and anticipates reduced sales next year

There has been a significant reduction in requests for estimates for new decorating work and the directors expect sales to reduce significantly next year. However, costs are expected to reduce accordingly and the company should be able to operate within its overdraft. The directors are not aware of any reason why the overdraft facility might be withdrawn. As a result they have adopted the going concern basis of accounting.

Material uncertainty that casts significant doubt about the ability of the company to continue as a going concern has been identified by the directors

Example 2 – A small company that has adopted the FRSSE and has experienced difficulties in securing future work

The company has orders for work for the next two months. However, despite significant efforts, it has so far proved impossible to obtain additional sales orders. If new orders are not forthcoming, the directors will need to close the factory and make the employees redundant.

The directors have concluded that a material uncertainty exists that casts significant doubt upon the company's ability to continue as a going concern and that, therefore, the company may be unable to realise its assets and discharge its liabilities in the normal course of business. However, given the continuing efforts to secure new orders, the directors continue to adopt the going concern basis of accounting.

Appendix II – Examples of going concern disclosures for companies other than small companies (including for subsidiary companies of large private or listed groups)

The purpose of this Appendix is to illustrate the guidance in paragraphs 79 to 83 in bringing together going concern and liquidity risk disclosures. In practice, such disclosures should be specific to the individual circumstances of each company.

No material uncertainties that cast significant doubt about the ability of the company to continue as a going concern have been identified by the directors

Example 1(a) – A company with a significant positive bank balance, uncomplicated circumstances and little or no exposure to economic difficulties that may impact the going concern assumption

The company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Business Review on pages X to Y. The financial position of the company, its cash flows, liquidity position and borrowing facilities are described in the Finance Director's Review on pages P to Q. In addition, notes A-D to the financial statements include the company's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk.

The company has considerable financial resources together with long-term contracts with a number of customers and suppliers across different geographic areas and industries. As a consequence, the directors believe that the company is well placed to manage its business risks successfully despite the current uncertain economic outlook.

The directors have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

Example 1(b) – A significant subsidiary where the subsidiary is financed by its parent company and participates in group banking arrangements

The company's business activities, together with the factors likely to affect its future development and position, are set out in the Business Review section of the Directors' Report on pages X to Y.

The company is expected to continue to generate positive cash flows on its own account for the foreseeable future. The company participates in the group's centralised treasury arrangements and so shares banking arrangements with its parent and fellow subsidiaries.

The directors, having assessed the responses of the directors of the company's parent ABC Limited to their enquiries have no reason to believe that a material uncertainty exists that may cast significant doubt about the ability of the ABC group to continue as a going concern or its ability to continue with the current banking arrangements.

On the basis of their assessment of the company's financial position and of the enquiries made of the directors of ABC Limited, the company's directors have a reasonable expectation that the company will be able to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

Example 2 – A company with uncomplicated circumstances, some exposure to economic difficulties and either a current material bank overdraft or loan and a need to renew this facility in the foreseeable future albeit not imminently

The company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Business Review on pages X to Y. The financial position of the company, its cash flows, liquidity position and borrowing facilities are described in the Finance Director's Review on pages P to Q. In addition, notes A-D to the financial statements include the company's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk.

As highlighted in note B to the financial statements, the company meets its day-to-day working capital requirements through an overdraft facility that is due for renewal on [date]. The current economic conditions create uncertainty particularly over (a) the level of demand for the company's products; (b) the exchange rate between sterling and CY and thus the consequence for the cost of the company's raw materials; and (c) the availability of bank finance in the foreseeable future.

The company's forecasts and projections, taking account of reasonably possible changes in trading performance, show that the company should be able to operate within the level of its current facility. The company will open renewal negotiations with the bank in due course and has, at this stage, not sought any written commitment that the facility will be renewed. However, the company has held discussion with its bankers about its future borrowing needs and no matters have been drawn to its attention to suggest that renewal may not be forthcoming on acceptable terms.

The directors have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

Material uncertainties that cast significant doubt about the ability of the company to continue as a going concern have been identified by the directors

Example 3 – A company with complicated circumstances, considerable exposure to economic difficulties and either a current material bank overdraft or loan that requires renewal and perhaps an increase in the year ahead

The company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Business Review on pages X to Y. The financial position of the company, its cash flows, liquidity position and borrowing facilities are described in the Finance Director's Review on pages P to Q. In addition, notes A-D to the financial statements include the company's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk.

As described in the directors' report on page X, the current economic environment is difficult and the company has reported an operating loss for the year. The directors' consider that the outlook presents significant challenges in terms of sales volume and pricing as well as input costs. Whilst the directors have instituted measures to preserve cash and secure additional finance, these circumstances create material uncertainties over future trading results and cash flows.

As explained on page X, the directors are seeking to sell a property to provide additional working capital. The company is in negotiations with a potential purchaser but there can be no certainty that a sale will proceed. Based on negotiations conducted to date, the directors have a reasonable expectation that the sale will proceed successfully, but if not the company will need to secure additional finance facilities.

As explained in the Business Review on page Y, the company has commenced discussions with its bankers about an additional facility that may prove to be necessary should the sale of the property not proceed or should material adverse changes in sales volumes or margins occur. It is likely that these discussions will not be completed for some time. The directors are also pursuing alternative sources of funding in case an additional facility is not forthcoming but have not yet secured a commitment.

The directors have concluded that the combination of these circumstances represents a material uncertainty that casts significant doubt upon the company's ability to continue as a going concern and that, therefore, the company may be unable to realise its assets and discharge its liabilities in the normal course of business. Nevertheless, after making enquiries and considering the uncertainties described above, the directors have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future. For these reasons, they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

Appendix III – Key questions for boards

For large and medium-sized companies, this Appendix provides questions that the board may wish to consider and discuss with management when determining the appropriateness of adopting the going concern basis of accounting.

The questions are not intended to be exhaustive and neither will all questions be appropriate for every company. This Appendix should be read in conjunction with the procedures described in Section One[8].

1. FORECASTS AND BUDGETS

1.1 Has management prepared monthly cash flow forecasts and/or monthly budgets covering, as a minimum, a period of twelve months from the expected date of approval of the financial statements?

1.2 Has management developed a list of assumptions (including macro-economic assumptions) that underlie the forecasts? Such assumptions might include:

- gross profit margins that are realistic and consistent with past performance, the existing and anticipated pricing structure and order book;
- expected sales mix and yield;
- the patterns of expected debtor collections (including explanation of their relationship to current debtor collections);
- levels of stock holding and work-in-progress;
- working capital requirements;
- payment terms with creditors;
- capital asset replacement programmes;
- cost escalation as a result of inflation, contractual terms or seasonal fluctuations; and
- overhead levels?

1.3 In determining the appropriateness of the going concern basis has management adequately taken into account:

- the stability of the cost base;
- potential labour difficulties;
- the risk of losing key staff;
- risks of losing key suppliers and significant customers;
- the risk of losing a key patent or franchise;
- potential losses on long-term contracts; and
- adequacy of the company's insurance policies?

1.4 Have the forecasts been tested by performing sensitivity analyses on the critical assumptions, particularly in relation to differing levels of activity?

8 Section One of "Going Concern and Liquidity Risk: Guidance for Directors of UK Companies 2009", published by the Financial Reporting Council.

1.5 Have lessons learnt from comparing past forecasts with subsequent actual results been appropriately reflected in the forecasts?

2. BORROWING REQUIREMENTS

2.1 Are the covenants on current borrowings satisfied as at the balance sheet date?

2.2 Are there any arrears of interest on current borrowings as at the balance sheet date?

2.3 Have the monthly forecast cash flow positions been compared to facilities available to establish whether or not there are any projected deficits? If so, are there plans in place to cover them, for example to renegotiate facilities with the company's bankers?

2.4 Have the forecasts been tested against existing covenants to assess whether any breaches are expected? If so, are there plans in place to prevent the breaches occurring?

3 TIMING OF CASH FLOWS

3.1. Has management analysed all known liabilities, commitments and repayment dates in the future, including the period beyond twelve months from the expected date of approval of the financial statements?

3.2 Where there are projected outflows that are unmatched by inflows, has management considered how the funds will be raised and whether appropriate arrangements can be put in place to meet payments as they fall due?

4. CONTINGENT LIABILITIES

4.1 Has management considered the exposure of the company to contingent liabilities, for example, those arising through:

- legal proceedings;
- guarantees and/or warranties;
- product liability not covered by insurance;
- grants received that are subject to conditions;
- environmental clean-up costs;
- decommissioning costs;
- intra-group guarantees; and
- retentions?

5. PRODUCTS, SERVICES AND MARKETS

5.1 For each of the main products or services, has management considered the relative strength of the company's products within the market and considered whether there are any economic, political or other factors that may cause the market, or the strength of the company's products within the market, to change?

5.2 Has management considered whether their marketing strategy is likely to secure future market share as projected in forecasts?

5.3 Has management considered the mix of customers and whether the company's turnover is economically dependent on too small a number? Has management evaluated counterparty risks such as the risk of losing these customers, for example by reviewing the customers themselves, their activities and whether these are changing? If there is a high risk of losing existing customers has management considered the likelihood of finding alternative sales markets?

5.4 Has management considered the robustness of the company's supply chain and whether there are weak links which could adversely affect the company's ability to deliver its products/services and/or increase costs through the need to seek and use alternative supply sources?

6. FINANCIAL AND OPERATIONAL RISK MANAGEMENT

6.1 Has management's sensitivity analysis evaluated the risk to the company of:

- adverse movements in interest rates;
- adverse movements in currency exchange rates; and
- exposure to risk through major fixed-price or fixed-rate contracts?

7. FINANCIAL ADAPTABILITY

7.1 Has management developed an adequate plan to enable it to take effective action to alter the amounts and timing of its cash flows so that it can respond to unexpected needs or opportunities?

7.2 In determining the financial adaptability of the company has management considered the ability of the company to:

- dispose of assets or to postpone the replacement of assets without significantly affecting other cash flows;
- lease assets rather than to purchase outright;
- obtain new sources of finance;
- renew or extend loans;
- restructure debts;
- raise additional share capital;
- obtain financial support from other group companies; and
- continue business by making limited reductions in the level of operations or by making use of alternative resources?

8. GROUP COMPANIES

8.1 Has the management of a subsidiary company performed a going concern assessment that takes account of its specific facts and circumstances? Does their assessment consider:

- how the subsidiary's business fits into the group's activities and future plans;
- the business risks that might arise that could threaten the going concern status of the subsidiary; and

- the extent to which the subsidiary is dependent on either financial or other support from the parent company and/or other group companies.

8.2 Has management made a determination concerning the ability and willingness of the parent company and/or other group companies to provide such support?

9. DOCUMENTATION

9.1 Has the going concern assessment been documented in sufficient detail to explain the basis of management's conclusion with respect to going concern?

9.2 Will the Board be invited to review and approve the documented assessment at the Board meeting at which it is expected to approve the financial statements?

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