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By email to: narrative@frc.org.uk

12 January 2016

Dear Madam

Exposure Draft: Guidance on the going concern basis of accounting and reporting on solvency and liquidity risks

PwC welcomes the opportunity to respond to the FRC's consultation on providing guidance in the above areas for companies that do not apply the UK Corporate Governance Code ('the Code'). We set out responses to each of the consultation questions below, as well as comments on a number of other aspects of the draft Guidance.

Naturally, many of the concepts in the draft Guidance are closely related to those embedded in the 2014 version of the Code and the FRC Guidance for companies that apply the Code (i.e. the Guidance on risk management, internal control and related financial and business reporting – 'GRM'). Because of this we think it would be helpful to provide a brief summary of the similarities and differences between the Code and GRM and the draft Guidance. We have included a suggested format for this analysis in the Appendix to this letter.

Also because of the close relationship between the draft Guidance and the framework for those reporting against the Code, we urge the FRC to review the outcomes of the first full reporting season under the Code before finalising the draft Guidance, so that the lessons learned can be reflected in it.

Consultation questions

Question 1 Do you agree with the scope of the guidance as set out in section 1?

We agree with the companies brought into scope for the Guidance – they need to be those that make disclosures on the going concern basis of accounting (where necessary) and on the principal risks and uncertainties facing the business.

Question 2 Is the guidance sufficient for the different types of company that fall within its scope?

We believe that the draft Guidance could provide more help for companies at both ends of the range that it would apply to, rather than focusing on the concept of being proportionate to the specific circumstances.

For instance, in our view, more established AIM companies with multiple stakeholders should consider applying the relevant assessment and disclosure provisions of the 2014 UK Corporate Governance Code and the GRM in full, whereas privately-owned companies with stakeholders who are directly involved in management of the business might find value in the risk assessment process but regard extended external disclosure as less significant.

Question 3 Do you agree with the draft guidance on the assessment of solvency and liquidity risk as set out in paragraphs 4.1 to 4.6?

We do not have any objection to these paragraphs but feel that they need to be read in the context of the rest of sections 4 & 5 in particular.

Within section 4 we would amend the order of the content of the paragraphs so that 4.2 and 4.3 come after the current 4.6. This would start the discussion of risk broad and narrow down to solvency and liquidity risks.

Question 4 Does the draft guidance sufficiently distinguish between the assessment of and reporting on the 'narrow' going concern basis of accounting (section 3) and the broader concept of solvency risk and liquidity risk (section 4)?

Yes – we think it does for the most part but would raise two specific points:

- The discussion of Other disclosures in paragraph 3.15 would be better positioned in section 4 as it is relatively indirectly related to the narrow going concern basis of accounting and more connected with risk.
- Similarly, the discussion on Financial instruments from paragraph 3.16 onwards would also be better positioned in section 4 and could also provide clearer guidance on how to deal with the directors' report and financial statement disclosure requirements.

Question 5 Does the draft guidance adequately highlight the relationships between the concepts (section 2)?

Yes, it does. We find Figure 1 on page 11 helpful in framing the overall model and how the various disclosures for companies relate.

Question 6 Do you consider that the guidance is sufficiently practical?

We recognise that the draft Guidance contains more specific information such as lists of factors to consider than the GRM, partly because a significant amount of content is carried across from the 2009 Guidance for directors of UK companies on going concern and liquidity risk. However, we believe that users of the Guidance would also find it helpful to have an indication of where the FRC sees the most significant changes in practice (accepting that the extent of change will vary depending on the type of organisation and its existing arrangements).

We have also indicated how this could be achieved in the Appendix to this letter.

Other points

Structure of the draft Guidance

We would recommend the following amendments to the order of content:

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- The Assessment process content in section 5 to become part of section 4, following on from paragraphs 4.1 to 4.6.
- The Reporting requirements (paragraph 4.11 onwards) to be placed after the Assessment process has been dealt with (in section 4 per the last suggestion).

Status of Guidance

In paragraph 1.2 it is explained that the draft Guidance is designed to be "non-mandatory, best practice guidance". Notwithstanding this, it is often stated that "the directors *should*" do something or consider something. This is not new practice – the 2009 FRC Guidance for directors on going concern and liquidity risk was drafted on the same basis – and where "should" is followed by a verb such as "consider" this usually softens the instruction to an appropriate extent. Nevertheless, we believe it would be helpful for the FRC to check whether it regards "should" as being correctly used each time it appears in the draft Guidance.

In section 3, for instance, it is appropriate as this section deals with the accounting framework requirement to consider the going concern basis of accounting. In a number of other instances, however, we think "should" potentially overstates the force of the draft Guidance. Particular examples include the following – the first relates to disclosure and the second to process:

4.13 This paragraph states that the strategic report *should* include a description of the principal risks and uncertainties facing the company, together with an explanation of how they are managed or mitigated. There is no legal requirement for the strategic report to set out management or mitigation of the principal risks, so we would either state this or amend the use of "should".

5.14 This paragraph states that if there is uncertainty over contractual arrangements with lenders or other providers of finance, the directors *should* seek confirmation from them of the principal terms and conditions. While the importance of the point at issue is clear, it does not appear appropriate to mandate a particular course of action in 'Guidance'.

Other paragraphs where we believe the usage of "should" could be questioned are: 5.5, 5.6, 5.8, 5.9, 5.12 and 5.15 (all relating to potential aspects of the risk assessment process).

Other terminology points

We do not believe that the frequent references to 'viability' in the draft Guidance are helpful and we would replace them with 'prospects' (consistent with the 2014 Code and GRM).

In paragraph 5.7 it is stated that sensitivity analysis involves measuring the impact of changing assumptions "within reasonably possible ranges". The GRM (Appendix B paragraph 4) refers to carrying out stress and sensitivity analysis for "severe but plausible scenarios". It is important for companies to be clear that the same thresholds are - presumably - to be applied.

In paragraph 4.15 it is stated that material solvency or liquidity risks could arise from, amongst other things, "uncertainties posed by the potential impact of the economic outlook on business activities". We think the Guidance should clarify that only economic factors directly related to the specific business should be disclosed, or more general 'risk factor' disclosures could result from this.

One significant difference between the GRM and the draft Guidance is that the former provides guidance across all aspects of risk whereas the draft Guidance is intended to focus on risks to solvency and liquidity. We think this focus could be made clearer in the language used in paragraphs 5.1 to 5.4 of the draft Guidance. (This could be addressed in part by taking up our suggested move of section 5 to come after paragraphs 4.1 to 4.6.)

Responsibilities for auditors

Section 7 of the draft Guidance sets out for directors the responsibilities of auditors in respect of the areas that it addresses. We think this is useful but that it would be helpful to confirm early in Section 7 that there is no change to the auditors' responsibilities.

If you have any questions or would like to discuss any of the points raised in this letter in more detail, please contact Peter Hogarth (0207 213 1654) or John Patterson (01223 552413).

Yours faithfully,

PricewaterhouseCoopers LLP

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Appendix

Solvency and liquidity risk

2014 UK Corporate Governance Code and GRM	Draft Guidance	Practical impact
Explanation of *how* the directors have assessed the prospects of the company…	No disclosure of the process used is required, but relatively detailed guidance on the suggested process is included in section 5	The directors will need to go through a process similar to that which supports the formal viability statement under the Code and GRM but the output of this process will simply be the disclosures of the principal risks to solvency and liquidity. The principal risks will need to be assessed with respect to a particular period – this will be a significant change for many companies, as principal risk disclosures tend not to be based on a specific time period (and are often relatively short term). Despite the nature of the process, the period and why it was chosen will not need to be disclosed. Presumably some companies may think it appropriate to do so on a voluntary basis.
…over what period they have done so…	No disclosure of the period of assessment is required, but paragraphs 4.7 onwards provide guidance consistent with the GRM that the period should, except in rare circumstances, be significantly longer than 12 months	
…and why that period was considered to be appropriate.	No disclosure of the reason why the period was regarded as appropriate is required, but paragraph 4.9 suggests a number of factors that should be considered	
Formal statement – reasonable expectation continuing in operation and meeting liabilities over the chosen period…	No requirement for a formal statement.	n/a

2014 UK Corporate Governance Code and GRM	Draft Guidance	Practical impact
...drawing attention to any qualifications or assumptions as necessary. [All above from Code C.2.2]	Not required as no formal statement is required.	n/a
Directors robustly assess the principal risks, including those that would threaten solvency or liquidity and the directors should describe those risks and how they are being managed or mitigated. [Code C.2.1]	Paragraph 4.13 requires a description of the principal risks and uncertainties facing the company, together with an explanation of how they are managed and mitigated.	Most of the companies to which the draft Guidance applies will have to provide details of how risks are managed or mitigated for the first time. (See also our comment on paragraph 4.13 in the body of this letter.)
n/a	Paragraph 5.17 states that directors of subsidiary companies need to make their own assessment to support disclosure of the principal risks and uncertainties facing the company	Presumably the existing proportionate approach to subsidiary disclosures of risk will be continued, but with management and mitigation of those risks disclosed for the first time.

Going concern

2014 UK Corporate Governance Code and GRM	Draft Guidance	Practical impact
Formal statement by the directors that they considered it appropriate to prepare the financial statements on a going concern basis [2014 Code C.1.3]	No requirement for a formal statement.	Some companies may continue to choose to disclose that the going concern basis of accounting has been used in the Basis of preparation note; otherwise, there is no need to provide any disclosure on going concern unless there is a material uncertainty.