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FRC updates going concern definition

by Richard Crump 07 Nov 2013

THE WAY going concern is assessed for stewardship and accounting purposes is to be clarified as part of wider changes to how companies and auditors disclose risks in annual reports, in reforms proposed by the FRC.

As part of changes to reporting rules imposed on listed businesses, the accounting watchdog wants companies and auditors to be clearer in their financial reports about how solvency and liquidity risks are being managed and has set out how it will implement the recommendations of Lord Sharman's 2012 inquiry into going concern.

The FRC is combining previous guidance on risk management and internal control with the assessment of the going concern basis of accounting as part of changes to the UK corporate governance code that is hopes will "raise the bar" for risk management by boards and auditors.

The draft guidance sets out boards' responsibilities for setting risk appetite, creating an appropriate risk culture throughout the organisation, and assessing and managing the principal risks facing the company, including risks to its solvency and liquidity.

Notably, however, the FRC wants to remove the current requirement for listed companies to make a going concern statement because it "detracts from the broader integrated assessment...of liquidity risks" envisaged by Lord Sharman.

Melanie McLaren, executive director of codes and standards at the FRC, explained the "narrow accounting basis" of going concern would be retained but that it would incorporate the stewardship definition into the reporting of solvency and liquidity risks.

"When looking at going concern in layman's terms people want to know if the entity is going to be able to settle its bills," McLaren told *Accountancy Age*. "We wanted to move away from giving a going concern statement in the narrative report."

Earlier proposals on going concern were **subjected to a barrage of criticism** from the profession amid concerns companies would find it hard to raise finance and attract investment because they would be required to report more material going concern uncertainties.

Critics also wanted the FRC to the stewardship and accounting purposes of the going concern assessment because it had "blurred the distinction between the two" and that confusion would arise when, for stewardship purposes, directors disclosed material uncertainties as to whether the business is a going concern, but that a going concern for 'accounting purposes' is appropriate.

The decision to make clearer distinctions as to the meaning of going concern was welcomed by Hywel Ball, UK head of assurance at EY. "On first reading, the latest FRC proposals seem to address earlier concerns," Ball said. "Highlighting the issues that boards need to consider when assessing and managing risk, including risks to solvency and liquidity, has got to be a step in the right direction."