Statement to companies, auditors, investors and other stakeholders

Joint statement by the Financial Conduct Authority (FCA), Financial Reporting Council (FRC) and Prudential Regulation Authority (PRA)

The Covid-19 pandemic is an unprecedented situation but it is important to recognise that, while the reduction in activity associated with Covid-19 could be sharp and large, it is likely to rebound sharply when social distancing measures are lifted. In addition, in the intervening period, while activity is disrupted, substantial and substantive government and central bank measures have been put in place in the UK and internationally to support businesses and households. These measures, which have been evolving rapidly and could evolve further, are expected to remain in place throughout the period of disruption.

Successful and sustainable businesses underpin our economy and society by providing employment and creating prosperity. Equity and debt capital markets play a vital role providing finance to these businesses and will aid the recovery. Governments and regulators around the world remain focused on keeping capital markets open and orderly.

Capital markets rely on timely, accurate information. Investors and other stakeholders rely on financial reporting – backed by high-quality auditing. However, companies and their auditors currently face unprecedented challenges in preparing and auditing financial information.

In response to the current situation, the FCA, FRC and PRA are today announcing a series of actions to ensure information continues to flow to investors and support the continued functioning of the UK's capital markets. This includes:

1. A statement today by the FCA allowing listed companies an extra 2 months to publish their audited annual financial reports.

2. Guidance from the FRC for companies preparing financial statements in the current uncertain environment. This is complemented by guidance from the PRA regarding the approach that should be taken by banks, building societies and PRA-designated investment firms in assessing expected loss provisions under IFRS9.

3. Guidance from the FRC for audit firms seeking to overcome challenges in obtaining audit evidence.

In these extraordinary circumstances, previous market practices relating to the timing and content of financial information and the audit work that is done must change. These changes are likely to include:

- Modified audit opinions where auditors have been unable to gather the necessary audit evidence to complete the audit in full: for example, by limiting the scope of the audit opinion.
- Given the uncertainty about the immediate outlook for many companies, more audited financial statements that include disclosures that management is aware of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern.
- Changes to timetables for publication of financial information that had been set before the full implications of Covid-19 were clear.

The FCA, FRC and PRA strongly encourage investors, lenders and other users of financial statements to take into account the unique set of circumstances arising from Covid-19 which might result in uncertainty in companies' financial positions, potential delays in the provision of financial information, the need for auditors to undertake additional work to support their audit opinions and the increased use of modified audit opinions, including qualifications arising from scope limitations.

UK banking authorities[1] have acted to reduce pressure on banks to restrict the provision of financial services, including the supply of credit and support for market functioning. Noting these actions, the FCA, FRC and PRA strongly encourage lenders and other parties to take into account these circumstances in responding to potential breaches of covenants arising directly from the Covid-19 pandemic and its consequences, given the common goal that the financial system should be a source of strength for the real economy during this challenging period.

[1] The Financial Policy Committee (FPC), the Bank of England, the Monetary Policy Committee (MPC) and the Prudential Regulation Committee (PRC)

1. Reporting timetable for listed companies

Recognising the challenges facing both auditors and listed companies, the FCA has today published a statement permitting a delay in the publication of audited annual financial reports from four to six months from the end of the financial year. This policy is intended to be temporary while the UK faces the extreme disruption of the coronavirus pandemic and its aftermath. We will keep its application under review. When the disruption abates we will consider how best to end the policy in a fair, orderly and transparent way.

Investors will still receive timely information on which to base their decisions as companies will still need to observe their other disclosure obligations, in particular those concerning inside information under the Market Abuse Regulation, recognising that the global pandemic and policy responses to it may alter the nature of information that is material to business prospects.

The Covid-19 pandemic is causing companies of all types to re-think and re-plan almost all aspects of their business and operations. We recognise that some companies, given the nature of their operations, may feel it appropriate to maintain the 4 month calendar, but **we would urge all those companies that feel it appropriate to utilise the additional 2 months to do so.** We urge market participants not to draw undue adverse inferences when companies make use of the extra time our temporary relief gives them, for a great many companies it will be a sensible decision to make in unprecedented times.

We strongly recommend that listed companies review all elements of their timetables for publication of financial information in order to make appropriate use of the time available within regulatory deadlines to ensure accurate and carefully prepared disclosures. Such timetables will likely have been set before the full implications of Covid-19 and the public policy response to it were clear. Companies should take note of the time available to them and they should feel supported in using it.

Further measures to allow companies and auditors to focus on the delivery of information to investors and the capital markets include:

- ***Delaying the filing of accounts by companies*** - Companies House has issued guidance to permit a delay to the filing of accounts at Companies House by companies. While companies will still have to apply for the 3-month extension to be granted, those citing issues around COVID-19 will be automatically and immediately granted an extension via a fast-tracked process. For example, this will permit applications for delayed filing of financial statements for subsidiary companies of listed entities.
- ***Postponement of auditor tenders***. Companies are encouraged to consider delaying planned tenders for new auditors, even when mandatory rotation is due. The FRC has a power in law to extend certain mandates, where the initial appointment commenced after 17 June 1994 by up to 2 years in exceptional circumstances.[2]
- ***Postponement of audit partner rotation*** – Key audit partners are required to rotate every five years. However, where there are good reasons, for example to maintain audit quality in current circumstances, the rotation can be extended to no more than seven years. This needs to be agreed with the audit committee of any affected entity and does not need to be cleared with or approved by the FRC.
- ***Reduction of FRC demands on companies and audit firms***. The FRC will, where possible, delay or extend the deadlines for consultations; it has paused for at least one

[2] Applications should be sent to AAT@frc.org.uk

month writing new letters to companies following its review of their annual reports and accounts; it is considering how it can adjust its audit quality review work to reduce demands on audit firms; and it will pause for at least one month requests to firms on supervisory initiatives, such as operational separation of audit practices.

- ***Extension of reporting deadlines for public sector bodies.*** HM Government is revising deadlines for reporting by a range of public bodies, which will also provide some relief to their auditors[3]. For example, the deadline for publication of final report and accounts of local government authorities has been extended by two months to the end of September.

2. Guidance for companies

Many companies preparing financial statements are facing unprecedented uncertainty about their immediate prospects in an environment that may challenge or disrupt their usual management and governance processes.

To maintain effective decision making in the interests of the company, their workforce and other business partners, the FRC encourages Boards to:

- Develop and implement mitigating actions and processes to ensure that they continue to operate an effective control environment: in particular, addressing any key reporting and other controls on which they have placed reliance historically, but which may not prove effective in the current environment.

- Consider how they will secure reliable and relevant information, on a continuing basis, in order to manage their future operations and those of their workforce and suppliers, including the flow of financial information from significant subsidiary, joint venture and associate group entities.

- Pay attention to capital maintenance, ensuring that sufficient reserves are available when the dividend is made, not just proposed.

Making forward-looking assessments and estimates is particularly difficult currently. The FRC has prepared guidance for companies intended to help them make key forward-looking judgements as consistently as possible.

The FRC's Financial Reporting Lab has been seeking feedback from investors on the disclosures that they would like to see and has produced a short infographic.. This work has highlighted a desire for disclosures from companies on the financial resources available to them including cash and access to additional finance (such as committed bank lines), other financing and non-standard debt arrangements (such as supply chain financing).

Investors have also pointed out the importance of forward looking information which explains how resilient the company's business model is to the current events, and to scenarios which are now reasonably plausible: for example, how long they are likely to be able to sustain their operations based upon these scenarios, and what mitigating actions they may be able to take

[3] The UK Government has announced that the deadline for the publication of audited principal authority accounts has been extended to 30 September 2020. For principal local Government councils, changes will made to to extend the deadline for unaudited accounts to be signed and published to 30 June 2020. Audited accounts for health bodies and Trusts and Clinical Commissioning Groups are now due to be published on 25 June 2020, instead of 31 May 2020.
In addition, the time allowed for delivery of unaudited accounts has been extended to 27 April 2020, and the implementation of IFRS16 has been deferred until the year ended 31 March 2021.

to extend these timeframes. Information about such stress testing and reverse stress testing is particularly valuable in the current environment, and will help support both the going concern assessment of the company and its viability statement.

In addition, the PRA has provided guidance to UK banks, building societies and PRA-designated investment firms regarding the application of IFRS9 including the extent to which payment holidays should constitute an event of default or should otherwise attract a lifetime expected loss provision. The PRA has also provided guidance to lenders on how they should respond to covenant breaches related to Covid-19, as follows:

"[The PRA] would expect lenders to consider the need to treat [covenant breaches that arise from Covid-19 related matters that are of a general nature or are firm-specific but unrelated to the solvency or liquidity of the borrower] differently compared to uncertainties that arise because of borrower-specific issues and in doing so consider waiving the resultant covenant breach. [The PRA] would expect firms to do so in good faith and not to impose new charges or restrictions on customers following a covenant breach that are unrelated to the facts and circumstances that led to that breach."

3. Guidance for auditors

In order to be able to give an audit opinion, the auditor must obtain sufficient, appropriate audit evidence. However, the current circumstances create obstacles to carrying out audit procedures arising from restrictions over accessing information electronically in some jurisdictions, social distancing measures taken in many countries; and the challenges posed by the current uncertain economic environment. Given these concerns, the FRC has issued guidance to auditors intended to provide practical help.

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