Is Your Company Viable?

You may just recently have noticed some new words appearing in the strategic report of companies you invest in. This new requirement requires companies to look forward and comment on how they see the future for their business. It is becoming known as a 'viability statement'.

In 2011 Vince Cable, then in charge of the Department for Business, Innovation and Skills, asked a well known academic, John Kay, to report on UK Equity Markets and Long Term Decision Making. He came to the conclusion that there needed to be a rebuilding of trust between investors and those who manage money on their behalf. He made several recommendations which he said would require action by not only government but most parties involved.

One strong theme of his was the need to reduce "short termism" and as a part of this he suggested that companies should state how they saw their future. For many years the accounts of companies have been drawn up on what is called the "going concern" assumption. This meant that the values in accounts reflected their worth to an ongoing business and not the values of a fire sale. Kay was asking for more.

This recommendation was picked up by the Financial Reporting Council, the UK regulator of accounting and reporting matters. After much debate in which UKSA amongst many others was involved a new requirement was introduced into the Corporate Governance Code which says: *"Taking account of the company's position and principal risks the directors should explain in the annual report how they have assessed the prospects of the company, over what period they have done so and why they consider that period to be appropriate. The directors should state whether they have reasonable expectations that the company will be able to continue in operation and meet its liabilities as they fall due over the period of the assessment, drawing attention to any qualifications or assumptions as necessary."*

One aim of this was to distinguish this requirement from the 'going concern' requirement which is why the term 'viability statement' is now being used. The debate around this requirement recognised that businesses differ and thus it would not be sense to prescribe the period which had to be covered in the statement. Instead it was agreed to ask the directors to decide that period, taking into account their company's business cycle. However, importantly, the directors are asked to justify the period over which they have considered the viability of their company.

It is hoped that this emphasis on a longer period will encourage both boards and investors to also take a longer term view. So if you attend an AGM in the near future look out for this new statement and ask the chairman about it and, in particular, ask how they came to decide on the period the statement covers. UKSA will be interested to have any comments you may have on this.

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