

## Press Release

15 October 2021

### FRC Investigates Going Concern Reporting of China Evergrande

The FRC has today initiated:

- (1) An enquiry into the financial statements of China Evergrande Group (**China Evergrande**) for both the year ended 31 December 2020 (**2020 Annual Accounts**) and the six months ended 30 June 2021 (**2021 Interim Accounts**); and
- (2) An investigation of the audit carried out by PricewaterhouseCoopers (**PwC**) on the 2020 Annual Accounts (**2020 Audit**).

The FRC identified questions about the adequacy of reporting on going concern in China Evergrande's 2020 Annual Accounts and 2021 Interim Accounts and PwC's auditor's report for the 2020 Audit through our market surveillance activities. We also received a complaint from a member of the public on these matters in relation to the 2020 Annual Accounts and 2020 Audit.

#### 2020 Annual Accounts

In the 2020 Annual Accounts, China Evergrande referred to:

- (i). Financing activities conducted to properly manage the Group's liquidity risk and capital structure; and
- (ii). Alternative plans to mitigate potential cash flow impacts if there are significant adverse changes in the economic environment.

However, as at 31 December 2020, China Evergrande:

- (i). Reported cash and cash equivalents of RMB159 billion that did not cover its current liabilities of RMB1,507 billion;
- (ii). Had further borrowings of RMB167 billion maturing in 2022; and
- (iii). Made no explicit statement in the 2020 Annual Accounts as to whether material going concern uncertainties existed before or after the effects of implementing the mitigating plans.

#### 2020 Audit

PwC expressed an unmodified audit opinion in its auditor's report on the 2020 Annual Accounts but made no reference to going concern material uncertainties.

#### 2021 Interim Accounts

In the 2021 Interim Accounts, China Evergrande:

- (i). Disclosed that the company was negotiating with suppliers and construction workers on some contracts for which work was suspended due to overdue property development accounts payable;
- (ii). Identified other mitigating measures it would adopt to address liquidity issues being faced; and
- (iii). Made an equivocal statement to the effect that if the mitigating measures are effectively implemented the going concern basis is appropriate in the 2021 Interim Accounts but if they cannot be implemented effectively it would be inappropriate to prepare the 2021 Interim Accounts on the going concern basis.

However, China Evergrande made no explicit statements in the 2021 Interim Accounts as to whether:

- (i). Material going concern uncertainties existed; or
- (ii). The directors judged it appropriate to adopt the going concern basis and, if so, whether that judgment was significant.

Based on China Evergrande's financial position as at 31 December 2020 and 30 June 2021 and the disclosures about its liquidity risks and mitigating actions in the 2020 Annual Accounts and the 2021 Interim Accounts, the FRC considers that there are reasons to:

- (1) Enquire into whether China Evergrande's going concern assessments for the 2020 Annual Accounts and the 2021 Interim Accounts, and the disclosures in those financial statements relating to going concern uncertainties and the adoption of the going concern basis of accounting, complied with the applicable financial reporting standards; and
- (2) Investigate whether PwC's audit work on China Evergrande's going concern assessment in the 2020 Audit and its auditor's report complied with applicable auditing standards.

### ***Why assessment and reporting relating to going concern matters to investors***

Applicable financial reporting standards (**AFR Standards**) have been developed on the basis that financial statements that comply with them will provide information that is useful to investors when a company is a 'going concern', i.e. is able to continue trading and meet its liabilities in full as they fall due. The resulting basis of accounting reflected in the AFR Standards is referred to as the 'going concern basis of accounting'. When a company is not a going concern, financial statements prepared on the going concern basis of accounting may not provide useful information to investors and the company is not allowed to prepare them on that basis. In preparing financial statements, management has to judge whether the company intends, or has no alternative, to cease trading or enter into liquidation.

### ***Our purpose in reporting publicly***

The FRC initiated the enquiry into the 2020 Annual Accounts and the 2021 Interim Accounts and the investigation into the 2020 Audit, taking into account that it is in the interests of the investing public for us to address questions about whether and to what extent:

- (i) The 2020 Annual Accounts and the 2021 Interim Accounts failed to comply with the AFR Standards with respect to going concern considerations; and
- (ii) The auditor's report on the 2020 Annual Accounts failed to comply with applicable auditing standards with respect to going concern considerations.

The FRC publicly announces the initiation of enquiries and investigations when considered necessary in the circumstances in order to protect the interests of shareholders and the investing public so as to maintain public confidence in our financial markets and independent auditor regulation.

End

### **About the Financial Reporting Council**

The FRC is the full-fledged independent listed entity auditor regulator for Hong Kong. We are committed to upholding the quality of financial reporting of listed entities of Hong Kong so as to enhance investor protection and strengthen investor confidence in corporate reporting.

For more information about the statutory functions of the FRC, please visit [www.frc.org.hk](http://www.frc.org.hk).

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