

Going Concern—Issues and Drafting Team Recommendations**Summary of the IAASB's Discussions at Its June 2014 Meeting****Auditor Reporting – Going Concern/Revisions to ISA 570¹***Description of Management's and Auditor's Responsibilities with Respect to Going Concern*

The Board generally supported requiring statements in the auditor's report describing both management's and the auditor's responsibilities with respect to both the use of the going concern basis of accounting in the preparation of the financial statements and the identification of material uncertainties and the proposed illustrative wording that had been developed by the Drafting Team in this regard. The Board encouraged the Drafting Team to further consider how the requirements had been articulated in proposed ISA 700 (Revised), in order to ensure adequate alignment between the requirements and the proposed illustrative wording. The Drafting Team was encouraged to give further consideration to:

- Revisit the sentence in the auditor's responsibilities section stating that the auditor cannot predict future events or conditions that may cause an entity to cease to continue as a going concern. In this regard, Ms. de Beer suggested it would be preferable for the language to be as balanced and factual as possible to respond to the CAG's concerns about the inclusion of such a statement in the auditor's report.
- Potentially reduce the length of the standardized wording to be included in the auditor's report in relation to going concern or present it more clearly.
- Further consider how the illustrative wording and underlying requirements align with the work effort in proposed ISA 570 (Revised) and management's responsibilities in accordance with International Financial Reporting Standards (IFRSs), while allowing for tailoring if other financial reporting frameworks apply.

Adequacy of Disclosures When Events or Conditions Have Been Identified but No Material Uncertainty Exists

The majority of the Board generally supported the goals of DT-570's recommendation set out in Agenda Item 3-A to include a new requirement to address the auditor's work effort in relation to disclosures when events or conditions that may cast significant doubt on the entity's ability to continue as a going concern had been identified, but the auditor had concluded that no material uncertainty exists after considering the mitigating effects of management's plans. It was noted that promoting a behavioral change by auditors is in the public interest and would be particularly useful when in a "close call" situation – that is, when significant judgment was required for the auditor to conclude that no material uncertainty exists relating to going concern. In addition, such a requirement could enhance communications by auditors and management about what disclosures relevant to going concern were necessary, and could provide greater communication to users.

¹ Proposed ISA 570 (Revised), *Going Concern*

Some concern was expressed that this new requirement unduly shifted the focus away from disclosures relating to material uncertainties and could be seen as setting additional disclosure requirements beyond those in the accounting standards (in particular, in IFRSs), notwithstanding that the proposed requirement sought to explain that the auditor's work effort was in view of what was required by the applicable financial reporting framework and the existing "stand back" requirement in proposed ISA 700 (Revised).

Ms. de Beer was of the view that, given the CAG's disappointment that the IAASB was reverting to exception-based reporting on going concern, including a new requirement for auditors to review the overall disclosures relevant to going concern would be partially responsive to calls for greater auditor attention on going concern. In her view, this new requirement did not set an extra threshold for the auditor to provide disclosure beyond the accounting standards. Accounting frameworks such as IFRSs already have an overarching or stand-back "fair presentation" requirement and this is merely requiring the auditor to ensure that this was appropriately considered by the entity.

The Board asked the Drafting Team to:

- Further refine the proposed requirement and application material, in particular to consider whether additional guidance is needed in proposed ISA 570 (Revised) to first explain disclosures relevant to material uncertainties and then allow for the possibility that, in accordance with the evaluation of the financial statements required by proposed ISA 700 (Revised), the auditor may consider additional disclosures necessary even when no material uncertainty had been identified.
- Consider the interaction between the proposed new requirement and the possibility, as acknowledged in proposed ISA 701,² that such "close call" circumstances may be determined to be a key audit matter (KAM).

Other Revisions to Proposed ISA 570 (Revised)

The Board also agreed further refinements to proposed ISA 570 (Revised), as included in Agenda Item 3-B. The Board asked the Drafting Team to further consider the proposed requirement for the auditor to make reference to material uncertainties in both the Basis for Qualified (or Adverse) Opinion section of the auditor's report and a separate section describing the material uncertainty when disclosures about a material uncertainty were inadequate or omitted, as some members viewed this duplication as unnecessary. The IAASB will consider a revised draft of proposed ISA 570 (Revised) for approval at its September 2014 meeting.

Flowchart

The Board considered a decision flowchart relating to the auditor's work effort under proposed ISA 570 (Revised) included in Agenda Item 3-A, and whether it could be usefully included in the final standard. The Board expressed mixed views on the inclusion of a flowchart in proposed ISA 570 (Revised) and asked the Drafting Team to consider a number of suggestions for refinements and examples developed by NSS in informing its final decision of whether to retain the flowchart or similar material in the final standard or to include it elsewhere.

² Proposed ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

Objectives of the IAASB Discussion

The following are the objectives of the IAASB discussion at its September 2014 meeting:

- Discuss and finalize the requirements in proposed ISA 700 (Revised) in respect of management's responsibilities and the auditor's responsibilities relating to going concern and the associated illustrative wording in the those sections of the auditor's report.
- Discuss and finalize an updated requirement and guidance in respect of the auditor's work effort in relation to management's disclosures of events and conditions that may give rise to a material uncertainty.
- Approve the revised draft of ISA 570 as a final standard.

I. Management and Auditor Responsibilities with Respect to Going Concern

1. Subsequent to the June 2014 IAASB meeting, DT-570 considered the Board's recommendations both to revisit the length and content of the required description of management's and the auditor's responsibilities and also to reconsider the wording of the sentence that the auditor cannot predict future events or conditions that may cause an entity to cease to continue as a going concern (i.e., the "guarantee statement").
2. With respect to management's responsibilities, DT-570 acknowledged that the illustrative wording was somewhat repetitive; however, DT-570 considered that the responsibilities included within the illustration continued to be relevant. As such, DT-570 has proposed an alternative presentation that alleviates the identified repetition.
3. DT-570 agreed with the Board that there was an imbalance with respect to the discussion of the auditor's responsibilities relating to going concern when compared with descriptions of the auditor's other responsibilities. DT-570 has therefore proposed edits to both the statement in the auditor's report and to the underlying requirement to address the balance of responsibilities while retaining the salient points of those responsibilities.
4. DT-570 also considered the wording with respect to those responsibilities. Specifically, DT-570 considered whether users might misinterpret the wording proposed to the Board at the June 2014 meeting,³ and as a result would assume that the auditor would always be able to determine if a material uncertainty exists.
5. DT-570 considered replacing "a material uncertainty exists" with "a material uncertainty has been identified" but determined that this might imply a greater work effort on the part of the auditor than that which is required by proposed ISA 570 (Revised).

³ Agenda Item 2-D from the June 2014 Board Meeting included the following illustrative wording with respect to the auditor's responsibilities relating to going concern: "Evaluate the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements, and evaluate, based on the audit evidence obtained, whether a material uncertainty exists about the entity's ability to continue as a going concern.... If a material uncertainty exists, we are required to draw attention in our auditor's report to the relevant disclosures in the financial statements..."

6. Based on the above considerations, DT-570 considered that the auditor responsibilities section should align with the responsibilities as described in proposed ISA 570 (Revised) and thus proposes that the illustrative wording in respect of the auditor's responsibilities relating to going concern uses the term "concludes that a material uncertainty exists."
7. In respect of the guarantee statement, DT-570 acknowledged the difficulty in obtaining the right balance for the statement. However, DT-570 continues to believe that it is useful to continue to include this statement and has drafted alternative wording to address the request to make the language as balanced and as factual as possible.
8. The proposed statements for inclusion in the Management's Responsibilities and Auditor's Responsibilities sections of the auditor's report are included in the illustrative auditor's report in **Agenda Item 4-B**. The requirements relating to these proposed statements are included in paragraphs 34(b)–(c) and 39(b)(iv) of **Agenda Item 4-B**, respectively. Further the related application material in paragraph A48 of **Agenda Item 4-B** explains that these statements may need to be adapted if a reporting framework other than IFRS is used.

Matter for IAASB Consideration

1. The IAASB is asked for its feedback on the revised requirements and related illustrative wording in respect of management's and the auditor's responsibilities relating to going concern.

II. Adequacy of Disclosure when Events or Conditions Have Been Identified but No Material Uncertainty Exists

9. In light of the Board's majority support, expressed at the June 2014 meeting, DT-570 has continued to refine the proposed requirement and related application material to address the auditor's work effort in relation to going concern disclosures. In particular, DT-570 has considered feedback that the new requirement unduly shifted the focus away from disclosures relating to material uncertainties and could be seen as setting additional disclosure requirements beyond those in the accounting standards (in particular, in IFRSs).
10. DT-570 is of the view that this new requirement and related guidance does not create new accounting requirements, but rather focuses the auditor, specifically with respect to going concern, on requirements that already exist within both the accounting and the auditing standards, which require the financial statements to present fairly the activities and position of an entity.
11. DT-570 also considered the feedback received indicating that too much emphasis was being placed on close call situations when compared with the limited guidance relating to the auditor's work effort in relation to disclosure of material uncertainties. A few IAASB members were of the view that the revised application material discussed at the June 2014 meeting⁴ could apply equally to material uncertainties as to close call situations.

⁴ The revised application material was presented at the June 2014 Board Meeting in Agenda Item 3 – ISA 570

International Financial Reporting Interpretation Committee (IFRIC) Agenda Decision

12. Subsequent to the June 2014 meeting, IFRIC has finalized and published its Agenda Decision in respect of disclosure requirements relating to the assessment of going concern⁵. The finalized Agenda Decision clarifies that IAS 1⁶ applies to “judgments made in concluding that no material uncertainties remain related to events or conditions that may cast doubt on an entity’s ability to continue as a going concern.” DT-570 believes that this is a positive step forward and notes that the new requirement and related guidance proposed in proposed ISA 570 (Revised) leverages the finalized Agenda Decision.

Drafting Team Recommendations

13. On balance, DT-570 believes the revised requirement presented at the June 2014 IAASB meeting is a positive step to enhance the auditor’s work effort in relation to going concern disclosures, particularly when the consideration of whether a material uncertainty exists involves significant judgment on the part of management and the auditor. However, DT-570 reconsidered the placement of the proposed application material. Such material has been restructured to first place more emphasis on the auditor’s consideration of disclosures of material uncertainties.
14. DT-570 first reviewed the extant requirement that the auditor consider the adequacy of disclosures in the financial statements when a material uncertainty exists and based on this consideration developed application material designed to make the guidance around the auditor’s consideration of disclosures robust and to place adequate emphasis on the requirement when a material uncertainty exists. These updates are presented in paragraphs A21–A22 of **Agenda Item 3-B**.
15. In light of the IFRIC Agenda Decision, DT-570 then reviewed the proposed new requirement for the auditor’s consideration of disclosures when events or conditions have been identified but it is ultimately concluded that no material uncertainty exists. DT-570 developed additional application material explaining the auditor’s responsibilities in respect of disclosures in such situations. Further, DT-570 is of the view that it continues to be appropriate to remind the auditor of the underlying fair presentation framework in accordance with proposed ISA 700. These updates are presented in paragraphs A23–A24 of **Agenda Item 3-B**.
16. DT-570 considered whether additional guidance should be included within proposed ISA 570 (Revised) to explain that the circumstance contemplated by the proposed new requirement could also be determined to be a KAM in accordance with proposed ISA 701. On reflection, DT-570 determined that all matters pertaining to the consideration of going concern as a KAM were more appropriately considered in proposed ISA 701 and further discussion in proposed ISA 570 (Revised) was unnecessary duplication. DT-570 acknowledged that paragraph A55 of proposed ISA 701 (**Agenda Item 2-B**) provides a useful signal to the fact that one or more matters relating to the conclusion arising from the auditor’s work effort in relation to going concern under proposed ISA 570 (Revised) may be determined to be KAM.

⁵ The finalized Agenda Decision can be found on the IFRS website - <http://media.ifrs.org/2014/IFRIC/July/IFRIC-Update-July-2014.pdf>

⁶ International Accounting Standard (IAS) 1, *Presentation of Financial Statements*, paragraph 122

Matter for IAASB Consideration

2. The IAASB is asked for its feedback on whether it believes that:
- It is appropriate to retain the requirement as presented at the June Board Meeting; and
 - The new application material developed, and its placement, is appropriate.

III. Other Revisions to Proposed ISA 570 (Revised)

Going Concern Reporting when the Auditor Expresses a Qualified or Adverse Opinion

17. In light of the Board's feedback that such a requirement was unnecessarily duplicative, DT-570 agreed to delete the proposed requirement for the auditor to make reference to a material uncertainty in both the Basis for Qualified (or Adverse) Opinion section of the auditor's report and a separate section describing the material uncertainty when disclosures about a material uncertainty were inadequate or omitted.
18. However, given the fundamental importance of going concern to the preparation of the financial statements, DT-570 continues to be of the view that the auditor's report should clearly state that the qualification is due to a material uncertainty relating to going concern. As such, DT-570 amended proposed ISA 570 (Revised) to include the requirement that the Basis for Opinion paragraph explicitly use the term "material uncertainty"; that reference is made to the fact that a material uncertainty exists that may cast doubt on the entity's ability to continue as a going concern and that the auditor's opinion is qualified in this respect (see paragraph 23 of **Agenda Item 3-B**).

Matter for IAASB Consideration

3. The IAASB is asked for its feedback on the proposal to require that the Basis for Opinion section always include a statement that the financial statements are qualified due to a material uncertainty relating to going concern.

Auditor Reporting When the Form and Content of the Auditor's Report is Prescribed by Law or Regulation

19. DT-570 considered the feedback received from the Board in respect of the paragraph in proposed ISA 570 (Revised), which provided flexibility when the form and content of the auditor's report is prescribed by law and regulation. DT-570 also considered the interaction of this paragraph with the comparable requirement in paragraph 50 of proposed ISA 700 (Revised). DT-570 noted that having requirements in both proposed ISA 570 (Revised) and proposed ISA 700 (Revised) introduced a level of inconsistency, because the requirement in paragraph 51 of proposed ISA 700 (Revised) extended flexibility to circumstances when the auditor referred to both ISAs and national auditing standards in the auditor's report, whereas proposed ISA 570 (Revised) only addressed reporting when law or regulation prescribed the form and content of the auditor's report.

Drafting Team Recommendations

20. Based on the proposal to make proposed ISA 570 (Revised) consistent with proposed ISA 700 (Revised) when the form and content of the auditor's report is prescribed by law and regulation, DT-570 proposes that the specific paragraph discussing this in proposed ISA 570 (Revised) be deleted.

21. DT-570 believes that this allows for flexibility both when law or regulation prescribes the form and content of the auditor's report and where a dual reference is made to ISAs and national auditing standards. As such, where a dual reference is made, the specific heading "Material Uncertainty Relating to Going Concern" would not be required, but the information included in that paragraph would need to address the matters in paragraph 22 of proposed ISA 570 (Revised), such that users would still be able to note that a material uncertainty exists.
22. DT-570 is also of the view that the requirement as drafted also envisages that auditors may have additional reporting responsibilities in relation to going concern, and is aimed at arriving at a section in the auditor's report that is not inconsistent with that required by proposed ISA 570 (Revised). The Board has supported a similar approach to reporting on KAM, to recognize that other jurisdictions (e.g., the UK, France and the EC) may take a different approach to KAM but nevertheless are trying to achieve a similar objective).
23. DT-570 proposed that paragraph 50(f) in proposed ISA 700 (Revised) be amended to create 2 separate sub-requirements within paragraph 50. This enables a separate discussion of the requirements in proposed ISA 570 (Revised) when a separate section for a material uncertainty is required and when the opinion is either qualified or adverse. The revised paragraphs 50(f) and 50(g) are presented in **Agenda Item 4-B**.

Matters for IAASB Consideration

4. The IAASB is asked for its feedback on how the requirement(s) in paragraph 50(f)-(g) have been articulated.
5. The IAASB is invited to provide feedback on the remaining changes to proposed ISA 570 (Revised) included in **Agenda Item 3-B**, which were largely made in light of other comments raised at the June 2014 IAASB meeting.

IV. Flowchart Considerations

24. DT-570 reflected on the Board discussion around the content of the flowchart and whether it could usefully be included in proposed ISA 570 (Revised). On balance, DT-570 determined that the flowchart should not be included within the standard but should form part of the Basis for Conclusions document.
25. DT-570 also considered if, as part of that document, any changes should be made to the flowchart based on the feedback from the June 2014 Board Meeting and determined that, while certain of the recommendations were incorporated into a revised flowchart, it should continue to be at a sufficiently high level. The updated flowchart is presented in **Agenda Item 3-D**.

Matter for IAASB Consideration

6. The IAASB is asked if it agrees with DT-570's recommendation to incorporate the flowchart into the Basis for Conclusions document, rather than proposed ISA 570 (Revised).

V. Significant Matters Identified by DT-570

26. In DT-570's view, the significant matters it has identified as a result of its deliberations since the beginning of this project, and its considerations therein, have all been reflected in the issues papers presented to the IAASB at its meetings. In DT-570's view, there are no significant matters it has discussed in this project that have not been brought to the IAASB's attention.