

# Identifying, Assessing and Reporting on Going Concern Issues

Presentation by:

CPA Ibrahim Mohamed  
Managing Partner Ibrahim & Company  
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# Presentation agenda



- ☐ Going Concern Basis of Accounting
- ☐ Responsibilities of Management and Auditor
- ☐ Relevant International Standards on Auditing (ISAs)
- ☐ Conditions Affecting Going Concern
- ☐ Audit Procedures
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# Going Concern Basis of Accounting



- ❑ Going concern is an important concept in the preparation of financial statements.
- ❑ Financial statements are prepared on the assumption that the entity will its operations for the foreseeable future.
- ❑ General purpose financial statements are prepared using the going concern basis of accounting unless management intend to liquidate the entity or cease operation.
- ❑ Also relevant to public sector entities.

# Responsibilities of Management and Auditor



- ❑ Management is required to assess the entity's ability to continue as a going concern and related financial statement disclosures which involves making judgment about the future.
- ❑ Auditor is required to obtain sufficient and appropriate audit evidence and conclude the appropriateness of management use of going basis in the preparation of the financial statements and to determine whether a material uncertainty exists.

# Relevant ISAs



- ❑ ISA 570 (revised) Going Concern – Deals with the auditor's responsibilities in the audit of financial statements relating to going concern and the implications for auditor's report.
- ❑ ISA 1 Presentation of Financial statements – Requires management to make assessment of the entity's ability to continue as a going concern.

# Relevant ISAs (Cont.)



- ❑ ISA 315 (revised) Identifying and Assessing the Risks of Material Misstatements through Understanding the Entity and its Environment- Requires auditor to consider during planning stage conditions that may cast doubt on the entity's ability to continue as a going concern.

# Conditions Affecting Going Concern



- ☐ Net current liability position
- ☐ Withdrawal of financial support by creditors
- ☐ Adverse key financial ratios
- ☐ Substantial operating losses
- ☐ Arrears or discontinuance of dividends
- ☐ Inability to pay creditors
- ☐ Inability to comply with the terms of loan agreement
- ☐ Management intention to liquidate the entity

# Conditions Affecting Going Concern (Cont.)



- ☐ Loss of key management without replacement
- ☐ Loss of major market, customer or supplier
- ☐ Emergence of highly successful competitor
- ☐ Non-compliance with capital, statutory and regulatory requirement
- ☐ Legal proceedings with adverse financial implications
- ☐ Change in law or government policy expected to adversely affect the entity



# Audit Procedures



- ☐ Perform going concern consideration during planning and audit completion stage.
- ☐ Determine whether management has identified events that may affect going concern basis of accounting.
- ☐ Evaluate management assessment of the entity's ability to continue as going concern.
- ☐ Analyze cash flow, profit and other relevant forecast with management.

# Audit Procedures (Cont.)



- ☐ Analyze the latest available interim financial statements.
- ☐ Read terms of loan agreement and determine whether any have been breached.
- ☐ Read minutes of shareholders, management and relevant committee for reference for financing difficulties.
- ☐ Obtain confirmation from company lawyer of pending claims and litigation.

# Audit Procedures (Cont.)



- ☐ Confirm existence, terms and adequacy of borrowing facilities.
- ☐ Obtain written representation from management about future plans.
- ☐ Written representation from third parties about support of the entity.
- ☐ Details of identified material uncertainty about going concern.
- ☐ Evaluation and conclusion about going concern.

# Reporting of Material Uncertainty



- ☐ Adequately disclose the principal condition.
- ☐ Highlight management's plan to deal with the condition.
- ☐ Evaluate management plan.
- ☐ Disclose clearly the material uncertainty.

# Auditor's Report



## 1. Unmodified Opinion

- Based on the audit evidence the auditor concludes that a material uncertainty exists and disclosure in the financial statement is adequate.
- Key Audit matters communicated in accordance with ISA 701.
- The auditor includes a separate section under the heading “Material Uncertainty Related to Going Concern”.

# Auditor's Report (Cont.)



## 2. Qualified Opinion

- Based on the audit evidence the auditor concludes that a material uncertainty exists related to conditions that may cast significant doubt on the entity's ability to continue as a going concern.
- Disclosure in the financial statement is not adequate.
- Key Audit matters communicated in accordance with ISA 701.

# Auditor's Report (Cont.)



## 3. Adverse Opinion

- Based on the audit evidence the auditor concludes that a material uncertainty exists related to conditions that may cast significant doubt on the entity's ability to continue as a going concern.
- The material uncertainty is not disclosed in the financial statement.

# Case Study



Mumias Sugar Company Limited was incorporated in 1971. The principal activities of the company are the production and sale of sugar and ethanol and the generation and sale of electricity. In recent past, the company continued to experience a number of challenges including; sugar cane shortage, unfair competition, lack of critical spares, below capacity operation, high cost of production and cash flow constraints.



# Case Study (Cont.)



The company incurred a loss of Shs 6,773,934,000 for the year ended 30<sup>th</sup> June 2017 and current liabilities exceeded its current assets by Shs 15.2 billion.

1. Identify conditions affecting going concern?
2. What are the appropriate audit procedures?
3. How do you report in the financial statements?

# References



1. ISA 570 (revised) Going Concern
2. ISA 1 Presentation of Financial statements
3. ISA 315 (revised) Identifying and Assessing the Risks of Material Misstatements through Understanding the Entity and its Environment-