

Going Concern Audit Changes & Effect on Entity Management

Management is responsible for an entity's financial statements and, beginning in 2017, this explicitly includes taking the initiative in assessing whether substantial doubt exists regarding its entity's ability to continue as a going concern. Accounting Standards Update (ASU) 2014-15, *Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*, is effective for annual periods ending after December 15, 2016, and for interim periods thereafter. For governmental entities, Governmental Accounting Standards Board (GASB) Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*, establishes similar requirements related to management's responsibilities for assessing going concern for state and local governmental entities.

The Financial Accounting Standards Board (FASB) and GASB standards address preparer requirements. For the auditor, the American Institute of CPAs (AICPA) Auditing Standards Board issued an updated going concern standard in February 2017. Statement on Auditing Standards (SAS) No. 132, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*, updates auditor guidance primarily by considering the ASUs for preparers. Although SAS 132 is auditor guidance, certain changes may affect the auditor's expectations of management. SAS 132's requirements are effective for annual audits ending on or after December 15, 2017, and reviews for interim periods ending on or after December 15, 2017.

Key Considerations

Separate Auditor Assessments

Unchanged in SAS 132 is the auditor's requirement to independently conclude—based on audit evidence obtained—whether substantial doubt exists about an entity's ability to continue as a going concern for a reasonable period of time. However, the definition of a reasonable period of time has changed from a period of time not to exceed one year beyond the date of the financial statements being audited to the period of time required by the applicable financial reporting framework, or if no such requirement exists, within one year after the date the financials are issued (or available to be issued, when applicable). Also unchanged is the auditor's requirement to obtain evidence to conclude on the appropriateness of management's use of the going concern basis of accounting in financial statement preparation, when relevant. SAS 132 clarifies the two requirements are separate determinations and conclusions.

- **Practice Point:** For entities reporting within special-purpose frameworks where a going concern basis of accounting is not relevant, the auditor is still required to conclude—based on audit evidence obtained—whether substantial doubt exists and evaluate the possible financial statement effects.

Third-Party or Owner-Manager Documentation

SAS 132 includes a new requirement for auditors to obtain evidence from management supporting its plans to mitigate substantial doubt when such plans include third-party financial support. The auditor will request written evidence about the third-party commitment or directly confirm with the supporting party and assess the third party's intent and ability to provide the necessary financial support. These audit procedures were generally already performed in practice.

- **Practice Point:** As with other financial statement items, management should prepare sufficient and appropriate evidence to support its going concern assessment, particularly its plans to alleviate substantial doubt. An auditor will request this documentation regardless of whether a third-party commitment or owner-manager is providing financial support. If the auditor concludes management's assessment is not adequately supported, the entity is at risk of a qualified or adverse audit opinion.

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When the owner-manager is providing the financial support, management should have a letter of intent or comparable written representation. Illustrative wording can be obtained from SAS 132's application material or the entity auditor.

Evaluation Period

Management's going concern evaluation period is 12 months from the date the financial statements are issued (or available to be issued). The new auditing standard requires auditors to ask management about conditions or events beyond management's evaluation period that may influence the entity's ability to continue as a going concern.

- **Practice Point:** The auditor's requirement to assess an entity's ability to continue as a going concern for a longer period than management is not intended to require management to extend its evaluation period. However, management should expect the auditor to ask questions about conditions or events beyond management's evaluation period.

Emphasis Paragraph in the Auditor's Report

Unchanged from current auditing standards, an auditor will generally include an emphasis-of-matter paragraph in its report when substantial doubt exists and management's plans do not alleviate the substantial doubt. In addition, an auditor may decide to include an emphasis paragraph in its report when it concludes that management's plans alleviate substantial doubt. The explanatory paragraph will generally highlight liquidity issues related to management's going concern disclosures.

- **Practice Point:** The addition of an emphasis-of-matter paragraph does not change the unmodified nature of the audit opinion; however, it may initiate questions from users. SAS 132 includes example language for such explanatory paragraphs that management may be interested in reviewing and discussing with financial statement users.

Interim Assessments

When interim evaluations are required by the applicable reporting framework, *e.g.*, FASB ASU 2014-15, GASB 56, SAS 132 amends AU-C 930, *Interim Financial Information*, and requires an auditor to perform interim review procedures related to going concern. When the auditor concludes certain conditions or events exist indicating substantial doubt about an entity's ability to continue as a going concern, the auditor also is newly required to include in its review report an emphasis-of-matter paragraph. Prior to SAS 132, an auditor was required to perform interim inquiries and consider the adequacy of management's going concern disclosures only in certain circumstances.

- **Practice Point:** The new requirements promote consistency in the auditor's work and reporting for annual and interim periods. In turn, management is expected to have policies and procedures in place to ensure adequate and timely documentation of its assessments and mitigating plans, as applicable.

Related Resource

[Management's Going Concern Reminder](#)

For further information, contact your BKD advisor.

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