STAFF PAPER

March 2013

IASB Meeting

Project	**Time frame for an assessment of going concern**
Paper topic	Proposed narrow-focus amendment to IAS 1

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Purpose of this paper

1. In June 2012, the IFRS Interpretations Committee (the Interpretations Committee) received a request for clarification about IAS 1 *Presentation of Financial Statements*. The Standard requires that when management are aware of material uncertainties about the entity's ability to continue as a going concern, those uncertainties shall be disclosed. The submitter, the International Audit and Assurance Standards Board (IAASB), thinks that the guidance about the disclosure of these uncertainties is not clear. The Interpretations Committee has held two meetings to discuss when these uncertainties should be disclosed and what format those disclosures should take. The resulting proposed narrow-focus amendment to IAS 1 is contained in Agenda Paper 3 A *Disclosure Requirements about an Assessment of Going Concern.*
2. In considering disclosures about material uncertainties about an entity's ability to continue as a going concern, the Interpretations Committee also discussed the time period that should be covered by the going concern assessment required by IAS 1. At present the Standard requires that management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the end of the reporting period.
3. Some members of the Interpretations Committee suggested that we should extend the proposed amendment in order to align the assessment time frame in IAS 1 with those of local auditing requirements, but the discussions on this topic were

not conclusive. As a result, the Interpretations Committee proposed that as part of the proposed narrow-scope amendment relating to disclosure requirements about the assessment of going concern, the IASB should consult publicly on the question of the assessment time frame. Specifically the Interpretations Committee proposed that the IASB ask whether the assessment time period in IAS 1 should be amended to align with the time frame set out in local auditing requirements and, if so, what form that amended wording should take.

4. The purpose of this paper is to provide you with information about the assessment time frame in IAS 1 and also about the time frames set out in local auditing requirements in order that you can decide:

   (a) whether the Exposure Draft of the proposed narrow-focus amendment to IAS 1-about disclosures relating to material uncertainties about an entity’s ability to continue as a going concern - should include a question about aligning the time frame in IAS 1 with those of local auditing requirements; and

   (b) what form that question should take.

Paper structure

5. This paper is organised as follows:

   (a) background;

   (b) outreach conducted;

   (c) potential alignment with local audit requirements; and

   (d) public consultation about the time frame of the assessment period.

Background

Requirements of the Standard

6. IAS 1 requires management to assess an entity’s ability to continue as a going concern:

> 25 When preparing financial statements, management shall make an assessment of an entity's ability to continue as a going concern.

7. The time frame for this assessment is also given in IAS 1:

> 26 … In assessing whether the going concern assumption is appropriate, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the end of the reporting period.

8. This assessment time frame is referred to in the *Conceptual Framework* in terms of "the foreseeable future":

> 4.1 The financial statements are normally prepared on the assumption that an entity is a going concern and will continue in operation for the foreseeable future. …

9. In the narrow-focus amendment to IAS 1 discussed in Agenda Paper 3 A, it is proposed that paragraph 26 of the Standard should be amended to refer to 'foreseeable future', rather than merely 'future', to align with the *Conceptual Framework*. Consequently, the assessment made by management in accordance with IAS 1 will take into account all available information about the foreseeable future, which is at least, but is not limited to, twelve months from the end of the reporting period.

Requirements of International Standards on Auditing

10. The requirements relating to an auditor's duty with respect to an entity's ability to continue as a going concern are contained in paragraphs 12 and 13 of International Standard on Auditing 570 *Going Concern* (ISA 570):

> 12 The auditor shall evaluate management's assessment of the entity's ability to continue as a going concern.
>
> 13 In evaluating management's assessment of the entity's ability to continue as a going conecrn, the auditor shall cover the same period as that used by management to make its assessment as required by the applicable financial reporting framework, or by law or regulation if it

> specifies a longer period. If management's assessment of the entity's ability to continue as a going concern covers less than twelve months from the date of the financial statements as defined in ISA 560, the auditor shall request management to extend its assessment period to at least twelve months from that date.

11. The date of the financial statements is defined in paragraph 5 (a) of ISA 560 *Subsequent Events* as the date of the end of the latest period covered by the financial statements. The effect of the requirements of International Standards on Auditing is to cover the same period used by management, which is the longer of:

    (a) that required by the applicable financial reporting framework or by law or regulation, and

    (b) twelve months from the end of the reporting period.

12. Consequently, both IAS 1 and ISA 570 require a minimum assessment period of 12 months from the end of the reporting period. It should be noted that in its submission on going concern the IAASB did not include the assessment time period as an issue.

Outreach conducted

13. Both IAS 1 and ISA 570 set twelve months from the end of the reporting period as the minimum period on which to base management's going concern assessment. In some jurisdictions, however, ISA 570 is modified by local audit or regulatory requirements to impose a different minimum time frame locally for the going concern assessment.

Outreach conducted by the staff

14. The outreach that we conducted on going concern is summarised in Agenda Paper 3A *Disclosure Requirements About an Assessment of Going Concern*. Many respondents noted as part of this outreach that in many jurisdictions aspects of the going concern assessment will be modified or defined by local insolvency rules. Outreach that we conducted suggested that audit firms in general wanted a clearer

link between local audit guidance and the IASB's requirements. Standard-setters and securities regulators, on the other hand, warned about the difficulties in trying to achieve an international solution on a topic that affects auditing, corporate governance, financial reporting and compliance. Many respondents think that a local level of guidance is currently adequate to reflect local regulatory and auditing concerns.

Outreach conducted by the submitter

15. In February 2013 the IAASB conducted outreach on our behalf to assess how widespread the variation from the minimum requirements of ISA 570 is in practice. They contacted their reference jurisdictions and asked them a series of questions about the time frame used by management and by auditors in their reviews of going concern. Thirteen jurisdictions responded to this request for information. The time frames reported for the audit requirements varied:

    (a) The majority of respondents had adopted ISA 570 without variation and the assessment period was no shorter than 12 months from the end of the reporting period.

    (b) One jurisdiction noted that they applied ISA 570 without supplementary guidance at present, but intended to amend their local assessment period to 12 months from date of audit signature.

    (c) In one jurisdiction the assessment period was 12 months from the date of approval of the financial statements.

    (d) In another jurisdiction the assessment period was approximately 12 months from the date of the auditors' current report. The reason for setting this period was so that it would be roughly equal to 12 months until the date of the auditors' report for the next annual period.

16. In just under a quarter of jurisdictions surveyed by the IAASB, the minimum time period set by local auditing requirements is longer than the minimum required by both IAS 1 and ISA 570.

FASB project on going concern

17. At its November 2012 meeting the FASB agreed to pursue a project that requires management to formally perform going concern assessments and to provide related footnote disclosures. This represents a significant change in practice in the US, where the onus to perform a going concern assessment currently rests with auditors.

Proposed financial reporting assessment time frame

18. The FASB has proposed that at each period end, management will assess an entity's potential inability to continue as a going concern for "a reasonable period of time". A reasonable period of time would represent 12 months from the financial statement (period end) date, but would not exceed a period of 24 months from the period end date. This minimum assessment period proposed is consistent with that in IAS 1 and ISA 570 as currently worded. Neither IAS 1 nor ISA 570 imposes a maximum time limit, such as 24 months, on an assessment of the future.

19. The FASB expect to publish an Exposure Draft of their proposals by late March or early April 2013.

Potential alignment with local audit requirements

20. The difference in the time frame used to assess an entity's ability to continue as a going concern can be a source of tension between auditors and their clients. Any difference between financial reporting requirements and local audit requirements would be expected to be more difficult to resolve for IFRSs than for national GAAPs, because we operate in a wide range of jurisdictions.

21. The IAASB themselves, in the wording that they used in ISA 570, acknowledge the varying requirements in different jurisdictions with respect to the assessment period. Their principle is to cover the same period on which management's review is based and the definition of the assessment period in ISA 570 allows for local variations:

> 13 … the same period as that used by management to make its assessment as required by the applicable

> financial reporting framework, or by law or regulation if it specifies a longer period. ..

22. If the detailed guidance in IAS 1 were to be amended to be compatible with a range of local auditing requirements, we might consider amending the wording of the current paragraph 26 of IAS 1 to mirror the flexibility used in ISA 570 (added wording in *italics*):

> 26 In assessing whether the going concern assumption is appropriate, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the end of the reporting period *or the period required by law, auditing requirements or regulation if it specifies a longer period.*

23. If we are to reconsider the assesment time frame in IAS 1, we have a number of choices:

    (a) We could do nothing which would ensure that IAS 1 remains consistent with ISA 570.

    (b) We could extend the minimum time frame to:

        (i) 12 months from date of approval of the financial statements;

        (ii) 12 months from date of audit of the financial statements; or

        (iii) approximately 12 months before the date of the next audit report.

    (c) We could extend the wording in IAS 1 to include a reference to both 12 months from the end of the reporting period and to local requirements, whichever is longer.

Extension of the assessment period

24. Some think that we should take this opportunity to extend the minimum assessment time frame in IAS 1.

25. Supporters of extending the assessment period refer to IAS 10 *Events After the Reporting Period*, which states, in paragraph 14, that:

> An entity shall not prepare its financial statements on a going concern basis if management determines *after the*

reporting period either that it intends to liquidate the entity or cease trading or has no realistic alternative but to do so. *[Emphasis added]*

26. In their view, this shows that the going concern assessment is a continuous one and one that happens up to the date on which the financial statements are finalised. They are concerned that the current time frame in IAS 1 does not adequately cover entities that may take several months to prepare and finalise their financial statements. They also note that the submitter (the IAASB) and the Sharman Inquiry have both suggested that the IASB should align IFRSs with auditing and regulatory requirements where possible.

27. Some think that the assessment period should be 12 months from the date of approval of the financial statements:

    (a) because this tracks management's stewardship cycle from one date of reporting to shareholders to the next annual date of reporting to shareholders; and

    (b) the date is under the control of management, which underlines their responsibility for the assessment.

28. Others support using the date of audit completion, because this is likely to be the longest possible extension and because it is audit firms that are currently most affected by any difference in time frame.

29. Alternatively, we could include wording in IAS 1 that would make the financial reporting requirements compatible with the longer of 12 months from the end of the reporting period or local requirements.

Retain the existing guidance

30. Others do not recommend amending IAS 1 to attempt to align the going concern assessment time frame with that of local auditing requirements.

    (a) The requirements of IAS 1 and ISA 570 are not inconsistent at present and consequently questions about the assessment period were not included in the submission from the IAASB on going concern. Any proposed amendment to IAS 1, if it was not reflected in ISA 570, would make financial reporting and international auditing standards inconsistent.

(b) Most jurisdictions surveyed did not modify ISA 570 and so most local audit requirements are not inconsistent at present with those of IAS 1.

(c) The proposed amendment was requested to deal with diversity in practice in relation to the timely disclosure of material uncertainties. In particular, there was concern at a perceived failure to forewarn investors of the high-profile collapse of some entities as a result of the financial crisis. We are not aware that the distinction between financial reporting and audit time frames was a factor in these collapses. In other words, the higher-priority issue that needs to be addressed is the non-disclosure of material uncertainties about an entity's ability to continue as a going concern rather than any inadequacy in the definition of the look-forward period.

(d) Many think that the lack of alignment between IAS 1 and local requirements causes few practical problems in jurisdictions in which different asssessment periods exist at present. Although IAS 1 requires a minimum period of 12 months from the end of the reporting period, in practice management comply with their auditor's request for an assessment of at least 12 months from the finalisation of the financial statements.

(e) Some think that the Standard defines the time frame in terms of the end of the reporting period in order to give certainty to the assessment time period in IFRSs and to underline management's responsibility for the assessment.

(f) For distressed entities, finalisation of the financial statements may be considerably delayed after their preparation. In our view the current limit, 12 months from the end of the reporting period, reinforces the requirement on management to make that going concern assessment on intial preparation rather than at finalisation.

(g) Amending IAS 1 so that it includes a reference to local auditing and rregulatory time frames will introduce diversity into financial reporting and prevent the requirements in IFRSs from beiong definitive.

Summary

31. There are advantages and disadvantages in deciding whether the assessment time frame should be extended and, if so, how that assessment period should be defined:

	Advantages	**Disadvantages**
12 months from		
end of the reporting period	Known in advance Agrees with ISA 570 and FASB proposals	Shorter than local alternatives where they exist
date of approval of financial statements	Basis used in IAS 10 Milestone that marks the end of formal involvement by management	Date may be unknown between end of the reporting period and auditors' report. May pre-date auditors' report
date of auditors' report	Ensures audit requirement and financial reporting requirements are identical	Date may be unknown between end of the reporting period and auditors' report. How will use of audit date link with the assessment being management's responsibility?
Greater of 12 months from end of the reporting period or local requirements	Maintains compatibility with ISA 570 as well as with local requirements	Introduces diversity in financial reporting Requirements of IAS 1 will not be definitive; will require knowledge of local requirements

32. At their January 2013 meeting, the Interpretations Committee recommended that we should further investigate whether the assessment period can be aligned with local auditing requirements.

Question 1 for the IASB
Do you agree that we should try to further investigate how we can align the time frame used in IAS 1 for the assessment of an entity's ability to continue as a going concern with the time frame required by local auditing requirements?

Public consultation about the time frame of the assessment period

33. The Interpretations Committee recommend that we should include a question in the Exposure Draft *Proposed Amendment to IAS 1 Financial Statement Presentation* about whether the assessment period should be aligned with local auditing requirements and how that alignment should be achieved. A proposed question about whether the assesment period should be aligned with local auditing requirements and how that alignment should be achieved is included as Appendix A.

Question 2 for the IASB
(a) Do you agree with the recommendation of the Interpretations Committee that we should include a question about the assessment time frame in the Exposure Draft? (b) Do you have any comments or suggestions on the form that question should take?

Appendix A

Question on the time frame of the assessment period about an entity's ability to continue as going concern for inclusion in the Exposure Draft *Proposed Amendment to IAS1 Financial Statement Presentation*

Introduction

A1. IAS 1 *Financial Statement Presentation* currently requires that management assesses an entity's ability to continue as a going concern:

> 25 When preparing financial statements, management shall make an assessment of an entity's ability to continue as a going concern.
>
> 26 … In assessing whether the going concern assumption is appropriate, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the end of the reporting period.

A2. This time frame is echoed by International Standard of Auditing 570 *Going Concern* (ISA 570). ISA 570 states that auditors should review management's assessment and

> If management's assessment of the entity's ability to continue as a going concern covers less than twelve months from the date of the financial statements as defined in ISA 560, the auditor shall request management to extend its assessment period to at least twelve months from that date.

A3. In many jurisdictions, local liquidity and insolvency or auditing requirements, however, mean that auditors need to cover a longer period than the minimum 12 months after the end of the reporting period that is required by both IAS 1 and IAS 570.

A4. The time frame for this assessment can vary by jurisdiction:

(a) not shorter than 12 months from the end of the reporting period (as at present in accordance with IAS 1 and ISA 570);

(b) not shorter than 12 months from the date of approval of the financial statements;

(c) not shorter than 12 months from the date of audit; or

(d) approximately 12 months from the date of the auditor's current report to approximate to 12 months to the date of the auditors' report for the next annual period.

A5. Many have suggested that the requirements of IAS 1 and local audit requirments should be aligned.

Question

A6. Do you think that theminimum period for the assessment of going concern in IAS 1 should be amended ?

A7. Which assessment period do you think should be specified as a minimum:

(a) 12 months from the end of the reporting period, as at present;

(b) 12 months from the date of approval of the financial statements;

(c) 12 months from the date of audit; or

(d) approximately 12 months from the date of the auditor's current report to approximate to 12 months to the date of the auditors' report for the next annual period.

(e) 12 months from the end of the reporting period or the period set by local auditing and regulatory requirements, whichever is longer.