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ISA (UK) 570 Going Concern

The Financial Reporting Council (FRC) has issued a revised International Standard on Auditing (ISA (UK)) 570, Going Concern, to strengthen the role of auditors in assessing whether a material uncertainty related to going concern exists; and the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements.

Background

Recent high-profile corporate failures (BHS, Carillion, Thomas Cook etc) have prompted the FRC to revise International Standard on Auditing (ISA (UK) 570 Going Concern), in response to widespread criticism that the auditors did not do enough to highlight concerns about the future prospects of these entities prior to their collapse.

The revised standard significantly strengthens the requirements for UK auditors in comparison with the equivalent international auditing standard.

Some of the key changes to the revised standard include the following:

1. Definitions

- Revised ISA (UK) 570 now includes a definition of the term 'management bias' as well as an extensive definition of the expression 'material uncertainty related to going concern'.

2. Increase in the work effort of the auditor

- The work effort of the auditor has been strengthened in the updated standard. In many cases, it demonstrates what currently happens in practice in terms of performing a robust evaluation of management's assessment of the going concern status of the entity.
- However, it places a greater need for the auditor to demonstrate how they have challenged management's going concern assessment and the rigour with which they have tested this assessment and the evidence and supporting documentation obtained.

3. Increased documentation requirements

- The increase in the auditor's work effort based on the revised standard will inevitably increase the amount of documentation needed to support the auditor's evaluation of management's going concern assessment.
- The audit documentation will be expected to detail the enquiries made of management over their assessment of the entity's ability to continue as a going concern. The auditor's evaluation of management's assessment, details of any tests that were performed and the auditor's conclusions thereon will also need to be documented.
- There is also a new stand back requirement in the revised ISA (UK) which requires the auditor to consider all the evidence obtained before concluding on the appropriateness of management's use of the going concern basis or whether a material uncertainty related to going concern exists. This stand back step of the audit process will also need to be documented.

Enhanced auditor reporting requirements

For all entities:

- A statement that the auditor has not identified a material uncertainty that may cast doubt on the entity's ability to continue as a going concern for a period not less than 12 months from the date of approval of the financial statements.
- A conclusion that management's use of the going concern basis of accounting in the preparation of the entity's financial statements is appropriate.
- If management's assessment of the entity's ability to continue as a going concern covers a period less than 12 months from the date of approval of the financial statements, the auditor is required to ask management to extend its assessment period to at least 12 months from that date.
- If the auditor considers that a 'material uncertainty related to going concern' should be included in the auditor's report, or that it is necessary to issue a qualified, adverse or disclaimer of opinion in respect of matters related to going concern, he/she is required to determine whether law, regulation or relevant ethical requirements:
  - **a.** require he/she to report to an appropriate authority outside the entity;
  - **b.** establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.

Conclusion

The overall objective of the revised ISA is to encourage more transparency and clarity around the auditor's work in the evaluation of management's going concern assessment.

If you would like to know more about any of the points raised in this article or have another issue you would like to discuss, please contact Bertie Newman or John Durham.

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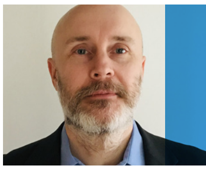

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