

IFRS Developments

Going concern – disclosure reminders issued by the IASB

What you need to know

- ▶ On 13 January 2021, the IFRS Foundation released a document, for educational purposes, highlighting what entities should consider when assessing their ability to continue as a going concern together with the respective disclosures.
- ▶ The document does not change, remove, or add to, the requirements in IFRS standards.

Introduction

On 13 January 2021, the IFRS Foundation released a document, prepared for educational purposes, highlighting the requirements in IFRS that are relevant to an entity's assessment of its ability to continue as a going concern and the respective disclosures. The document does not change, remove, or add to, the requirements in IFRS standards. Rather the intention is to remind preparers of the IFRS requirements for going concern assessments and the disclosure of material uncertainties and significant judgements.

Stakeholders are increasingly concerned about the impact of the COVID-19 pandemic on entities' ability to continue as a going concern given the significant economic downturn and, particularly, the reduction in entities' revenue, profitability and liquidity. This has increased the importance of going concern assessments and the related disclosures.

In September 2020, the International Auditing and Assurance Standards Board (IAASB) published a Discussion Paper (DP) *Fraud and Going Concern in an Audit of Financial Statements: Exploring the Differences Between Public Perceptions About the Role of the Auditor and the Auditor's Responsibilities in a Financial Statement Audit* (available on the [IAASB's](#) website), which considers audit-related going concern matters and also highlights the going concern requirements of IAS 1 *Presentation of Financial Statements*. The DP specifically asks for perspectives as to whether the concept of, and requirements related to, a material uncertainty are sufficiently aligned across the requirements of audit standards and IFRS standards. The DP is open for consultation until 1 February 2021.

The International Accounting Standards Board (the IASB) has identified going concern as a potential agenda item to be covered in its upcoming agenda consultation, for which it plans to publish a request for information in March 2021. The key messages in the educational document are summarised in the following sections.

Considering time periods longer than 12 months for the going concern assessment is not inconsistent with the requirements in IAS 1, which establishes a minimum period rather than a cap.

The applicable requirements

IAS 1 explains going concern by stating that financial statements are prepared on a going concern basis “unless management either intends to liquidate the entity or

to cease trading, or has no realistic alternative but to do so”. In making the assessment about whether the going concern basis of preparation is appropriate, management may need to consider factors that relate to:

- ▶ The entity's current and expected profitability
- ▶ The timing of repayment of existing financing facilities
- ▶ The potential sources of replacement financing

However, considering the current stressed economic environment, there may be a wider range of factors that can affect an entity's going concern assessment than those considered in the past. The educational document refers to the requirement of IAS 1 that management needs to take into account all available information about the future and provides the following examples:

- ▶ The effects of any temporary shut-down or curtailment of the entity's activities
- ▶ Possible restrictions on activities that might be imposed by governments in the future
- ▶ The continuing availability of any government support
- ▶ The effects of longer-term structural changes in the market (such as changes in customer behaviour)

According to IAS 1, an entity needs to look at a period of at least 12 months from the end of the reporting period when assessing whether to prepare financial statements on a going concern basis. Note, however, that emphasis is given to the fact that the outlook is not limited to 12 months. That is, considering time periods longer than 12 months (as may be required by national requirements) is not inconsistent with the requirements in IAS 1, which establishes a minimum period rather than a cap.

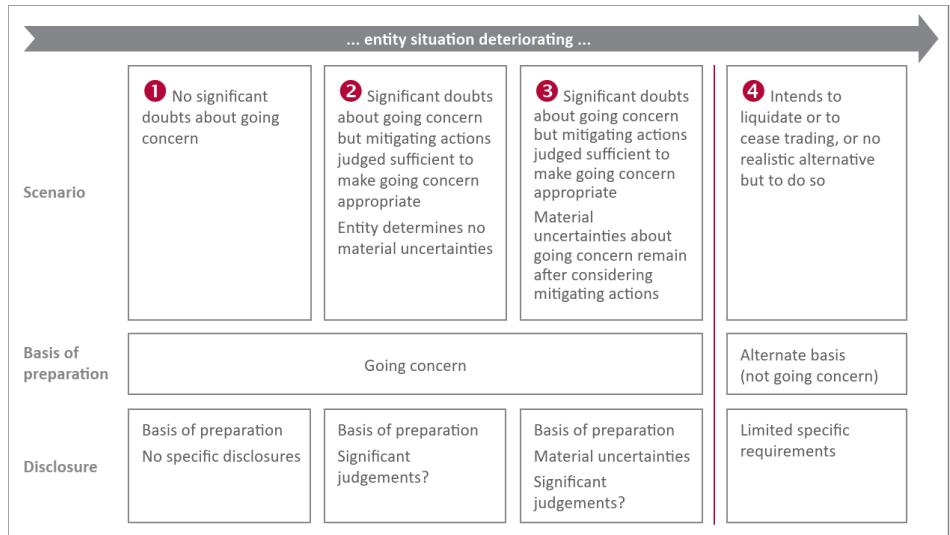
The educational document highlights the fact that, in the current environment, there might be rapid changes in the circumstances affecting management's assessment of the entity's ability to continue as a going concern. For this reason, it makes reference to IAS 10 *Events after the Reporting Period*, which explains that management's assessment of the use of a going concern basis of preparation needs to reflect the effect of events occurring after the end of the reporting period up to the date that the financial statements are authorised for issue. That is, the financial statements must not be prepared on a going concern basis if, before they are authorised for issue, circumstances were to deteriorate so that management no longer has any realistic alternative but to cease trading, even if the assessment at the end of the reporting period supported the application of the going concern basis.

There is a wide variety of circumstances under which entities prepare financial statements on a going concern basis. Assumptions and judgements are used by management to support its decision about going concern and, in the current environment, greater uncertainty may be involved than in the past. Consequently, users of financial statements are more likely to focus on disclosures relating to going concern and may question how the assumptions management used in reaching its conclusion about going concern relate to assumptions underpinning other aspects of the financial statements.

Therefore, the educational document emphasises the importance for an entity to not only consider the specific disclosure requirements relating to going concern in IAS 1, but also its overarching disclosure requirements. This includes judgements that have the most significant effect on the amounts recognised in the financial statements.

Applying the requirements

The educational document includes the following diagram relating to the application of the requirements in IAS 1 and includes four scenarios:



The four scenarios represent different situations that may be applicable in practice. The educational document explains in more detail how to apply the requirements of IAS 1 on each of these scenarios.

Scenarios 1 and 4 are at each end of a spectrum. It is less likely that additional disclosures are required if an entity has profitable operations and has no liquidity concerns (Scenario 1). Disclosure of the fact that a basis other than going concern has been applied and the reasons why, as well as disclosure of the alternative basis applied, are required if an entity intends to liquidate or cease trading, or no has not realistic alternative but to do so (Scenario 4).

Scenarios 2 and 3 are similar, but a key difference applies with respect to an entity's final conclusion on whether material going concern uncertainties exist. If an entity concludes that there are no material uncertainties regarding its ability to continue as a going concern and that conclusion involves significant judgement, then the overarching disclosure requirements in IAS 1 would apply to the judgments made in concluding that no material uncertainties remain (Scenario 2). The same overarching disclosure requirements in IAS 1 would apply in a similar situation where the conclusion is that material going concern uncertainties exist and that conclusion involves significant judgement (Scenario 3). In that case, IAS 1 also requires disclosure of the material uncertainties relating to the entity's ability to continue as a going concern.

Another example of overarching disclosure requirements in IAS 1 that could be relevant, especially in cases of close calls, are the requirements relating to sources of estimation uncertainty. These require disclosing information about the assumptions made about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

The overarching disclosure requirements in IAS 1 would apply to the judgements made in order to reach the going concern conclusion, if that conclusion involved significant judgement.

How we see it

Although the educational document does not introduce any new requirements, it may help preparers to apply the existing requirements in IFRS. More specifically, in light of the economic downturn caused by the COVID-19 pandemic, the educational document represents a helpful reminder about challenging assessments that management may need to make and key disclosures that may apply to many entities under the current circumstances.

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