



राष्ट्रीय वित्तीय रिपोर्टिंग प्राधिकरण

National Financial Reporting Authority

Auditor – Audit Committee* - Interactions Series 6 dealing with Going Concern Assessment : SA 570 (Revised)

**NFRA does not set standards and codes for Corporate Governance, Board of Directors and Audit Committees.*

Introduction

Going concern basis of accounting is the assumption on which most sets of financial statements in India are prepared, unless the management either intends to liquidate the entity or to cease operations and has no alternative but to do so. Using the going concern basis of accounting denotes that the financial statements are prepared on the assumption that the entity will continue its operations for the foreseeable future, and assets and liabilities are recognised on the basis that the entity will be able to realise its assets and discharge its liabilities in the normal course of business. Where that assumption is not appropriate, the effect is not confined to a note in the financial statements or a paragraph in the auditor's report, rather it reaches the measurement of every asset the entity owns and the classification of every liability it owes.

The assumption is therefore, critical and is the only judgement in the preparation of financial statements that needs to be made in every reporting period. It is

among the few judgements whose consequences extend well beyond the shareholders. The consequences extend to suppliers extending credit, to lenders sanctioning facilities, and to employees and small vendors whose exposure to the entity is concentrated and involuntary. It is also forward looking, which means that the nature of evidence gathered by management or by the auditor, cannot be entirely conclusive and is likely to be anchored in assumptions about the future.

What do the regulations require?

The obligations in relation to going concern are relevant for four groups, and each obligation arises from a different regulatory framework.

Management is required to assess the entity's ability to continue as a going concern. Under Ind AS 1¹, that assessment takes into account all available information about the future, covering at least, but not limited to, twelve months from the end of the reporting period, and material uncertainties² which

¹ Ind AS 1 - Presentation of Financial Statements

² When events or conditions are identified which cast significant doubt on the entity's ability to continue as a going concern, assessment is needed with regard to whether or not

material uncertainties exist related to those events or conditions after having considered mitigating factors. This phenomenon is referred to as material uncertainty in SA 570 (Revised). Paragraph 16 of SA 70 (Revised)

are required to be disclosed. For entities not applying Ind AS, the going concern assumption is a fundamental accounting assumption under AS 1³. This is the primary obligation, and everything that follows depends upon the quality with which this is discharged.

The Board of Directors is required to state, in the Directors' Responsibility Statement forming part of the Board's Report under Section 134(5) of the Companies Act 2013, (the 'Act') that the annual accounts have been prepared on a going concern basis. The Act requires the confirmation of the basis.

The audit committee is required to, under Section 177 of the Act and Regulation 18 of the SEBI Listing Obligations and Disclosure Requirements ('LODR') Regulations 2015 read with Part C of Schedule II, review with management the annual financial statements before submission to the board, with particular reference to the matters required to be included in the Directors' Responsibility Statement. Consequently, the Audit Committee is also required to look into and assess the appropriateness of going concern assumption.

The statutory auditor is required to, under SA 570 (Revised)⁴, obtain sufficient appropriate audit evidence regarding, and conclude on, the appropriateness of management's use of the going concern basis, and is required to conclude on whether a material uncertainty exists. These responsibilities exist even where the applicable financial reporting framework contains no explicit requirement for management to make an assessment. Critically, the standard states that it is not the auditor's responsibility to rectify a lack of analysis by management⁵. It is essential to note that the auditor is required to evaluate and not prepare the analysis.

What does SA 570 (Revised) require and its outcomes

SA 570 (Revised) recognises the complexity of situations that could exist in an entity and consequently provides guidance for various situations. It lays out a sequence of situations to be assessed, and the answer to each determines which question arises next and what the auditor needs to ultimately report.

The auditor first considers, at the risk assessment stage, whether events or conditions exist that may cast significant doubt on the entity's ability to continue as a going concern. Where none are identified, the auditor still concludes on the appropriateness of the basis.

Where events or conditions are identified, the standard mandates a set of further procedures⁶, following which the auditor is required to conclude whether a material uncertainty exists⁷. The disclosure requirements and the reporting outcomes, follow from that conclusion.

The result is a set of distinct situations, each with its own requirements and its own consequences in terms of how it gets reported in the auditor's report.

	Situation	What the standard requires	Reporting outcome
1	No events or conditions casting significant doubt are identified (either by management or the auditor)	The auditor concludes on the appropriateness of the going concern basis	Unmodified opinion. No going concern reporting arises
2	Events or conditions are identified	The auditor is still required to evaluate whether	Unmodified opinion, with no Material

³ AS 1 - Disclosure of Accounting Policies

⁴ Paragraph 9 of SA 570 (Revised)

⁵ Paragraph 12, A9 of SA 570 (Revised)

⁶ Paragraph 16 of SA 570 (Revised)

⁷ Paragraph A3 of SA 570 (Revised) provides examples of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern

Situation		What the standard requires	Reporting outcome
	in the management assessment, but the auditor concludes no material uncertainty exists	the financial statements provide adequate disclosure about those events or conditions	Uncertainty Related to Going Concern (MURGC) section, since none exists
3	Going concern basis is appropriate, but material uncertainty exists and the disclosure is adequate	The principal events or conditions and management's plans, are required to be disclosed in the financial statements and they are also required to state clearly that a material uncertainty exists that the entity may be unable to realise its assets and discharge its liabilities in the normal course of business	Unmodified opinion, with a separate MURGC section
4	Going concern basis is appropriate, but a material uncertainty exists; and the disclosure is not adequate	The auditor states in the Basis for Opinion section that a material uncertainty exists and that the financial statements do not adequately disclose it	Qualified opinion where the effects are material but not pervasive; adverse opinion where they are material and pervasive. In rare cases, where multiple

Situation		What the standard requires	Reporting outcome
			uncertainties exist, the auditor may consider an disclaimer of opinion
5	Going concern basis has been used but its use is inappropriate	The reporting requirement applies whether or not the financial statements disclose the inappropriateness.	Adverse opinion
6	Use of going concern basis is inappropriate and another acceptable basis has been used	Where another acceptable basis is used instead, an unmodified opinion may be possible with adequate disclosure of that basis	An unmodified opinion with an Emphasis of Matter where an acceptable alternative basis is adopted

Each of these situations calls for a different conversation between the audit committee and the statutory auditor, and in each circumstance the questions that a statutory auditor can expect are different.

The questions that can be expected by the auditor, have been grouped below as per the respective situations since the questions to be expected where nothing has been identified are not the same where a material uncertainty has been concluded.

Consequently, this document is structured around these situations, so that the auditor may prepare to respond to the audit committee's questions in accordance with the situation being dealt with.

Certain matters, such as reliance on support from a parent or a promoter, group structures, regulated entities and companies undergoing an insolvency resolution process, may entail further modifications

to the expected questions. Further the size and complexity of the entity or the group will also play a significant role in the way going concern assessment is carried out and may lead to modifications to the expected questions.

A related but separate requirement under CARO 2020

Clause 3(xix) of the Companies (Auditor's Report) Order 2020 ('CARO 2020') requires the auditor to state whether, on the basis of the financial ratios, the ageing and expected dates of realisation of financial assets and payment of financial liabilities, other information accompanying the financial statements, and the auditor's knowledge of the plans of the Board of Directors and management, the auditor is of the opinion that no material uncertainty exists as on the date of the audit report, and that the company is capable of meeting its liabilities existing at the date of the balance sheet as and when they fall due within a period of one year from the balance sheet date.

Although the subject matter overlaps with SA 570, this is a distinct requirement. It requires a different lens to be applied, directed at the capability of meeting existing liabilities rather than at the appropriateness of the going concern basis; it is assessed as at the date of the audit report rather than a specific duration from the date of the financial statements; and it is factual reporting on a specified evidence base rather than an opinion on the financial statements.

Therefore, it may be possible that the auditor's response to the two assessments (CARO and SA 570) may lead to different answers

A company may hold sufficient current assets, including receivable whose realization is reasonably assured, or may have arranged short-term financing adequate to discharge its existing liabilities as they fall due within the stipulated period. Reporting on Clause 3(xix) statement would accordingly be unqualified. The wider matters to which SA 570 is directed may nonetheless give rise to significant

doubt, whether by reason of recurring operating losses, erosion of net worth, the loss of a key customer or of a license necessary to the business, the discontinuance of a principal product line, or the absence of committed funding for the business beyond the immediate schedule of existing liabilities.

Conversely, the analysis of financial ratios and of the ageing and expected dates of realization and payment may disclose a short-term mismatch between the maturity dates of liabilities and the availability of resources to meet them. Subject to the timing mismatch, the auditor may nonetheless have obtained sufficient appropriate audit evidence of a concrete and credible mitigating plan, such as a committed facility, a binding infusion of capital or a support arrangement whose terms and the supporting party's ability to perform have both been evidenced, which resolves the matter for the purposes of SA 570 and which is adequately disclosed in the financial statements.

The auditor may expect the audit committee to question these differing responses when the audit committee reads the reporting on clause 3(xix) statement together with the main auditor's report when it evaluates the report at the year end, and the auditor may be expected to be able to provide a rationale for any apparent difference between them.

Sequence

The obligations described above are not discharged in parallel. The board's statement and the audit committee's review of going concern basis are their respective responsibilities and are expected to be discharged independent of the work undertaken by the auditors. Neither is satisfied by either adopting or depending on the auditor's conclusion. Therefore, the audit committee's first engagement on this subject is likely to be with the management because the management is required to prepare the assessment under Ind AS 1 or AS 1, as the case may be, and the auditor's role under SA 570 (Revised) is to evaluate such an assessment.

The questions that follow, are based on the assumption that the audit committee has met its obligations mentioned in page 2 above.

Potential questions the Auditor may expect from the Audit Committee:

No events or conditions have been identified:

1. Has the auditor identified any events or conditions that exist that may cast significant doubt on the company's ability to continue as a going concern?
2. Has the auditor determined that there were certain indicators⁸ present but assessed as mitigated by other factors, and what were those factors?
3. Did the auditor observe anything during the audit that caused the auditor to revisit the going concern position after the initial risk assessment⁹? If yes, what was auditor's response?
4. Did the auditor inquire of management about its knowledge of events or conditions beyond the assessment period, and what was the response?
5. Has the auditor evaluated the internal controls established by management pertaining to going concern and what is the auditor's assessment regarding their design and operating effectiveness?

Events or conditions have been identified:

6. Does the management's assessment as provided to the auditor cover the period of assessment as required by the standard or is it shorter¹⁰?
7. Where the assessment period considered by management is shorter than 12 months, has the management revised its period of assessment and does the auditor

find such revised assessment period reasonable?

8. Has the auditor been made aware of by the management, of any events or conditions beyond the period of management's assessment that may cast a significant doubt on the company's ability to continue as a going concern?¹¹
9. Has management's assessment changed in method or approach from last year and if yes, is it reasonable in the auditor's view?
10. Did the auditor evaluate the process management followed to reach its assessment, the assumptions on which it is based, and whether the plans are feasible in the circumstances?
11. With respect to the cash flow projections, was the auditor able to evaluate the reliability of the underlying data and determine whether there is adequate support for the assumptions¹²? For instance, where going concern assessment depends on the proposed sale of assets, has the auditor performed adequate procedures to assess whether there is an identified buyer or existence of a market for that asset, its valuation and net realizable value and the timing thereof?
12. Did the auditor compare the actual results against the forecasts made by the management in the past and were they in line with the forecasts¹³?
13. Did the auditor perform sensitivity analysis and what are the auditor's observations with regard to the reasonableness of the critical assumptions?

⁸ Paragraph 10 and A3 (*Events or Conditions That May Cast Significant Doubt on the Entity's Ability to Continue as a Going Concern*) of SA 570 (Revised)

⁹ Paragraph 11 of SA 570 (Revised)

¹⁰ Paragraph 13 of SA 570 (Revised)

¹¹ Paragraph 15 of SA 570 (Revised)

¹² Paragraph 16 of SA 570 (Revised)

¹³ Paragraph 16 and A18 of SA 570 (Revised)

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14. Having considered the management's plans for future action, has the auditor been able to conclude that the outcome of plans is likely to improve the situation?
 15. For any future plans that are dependent on a third party's concurrence, has the auditor been able to obtain sufficient information to support management's assumptions and conclusions? (For example, in case of planned disposal of assets, is there sufficient appropriate evidence to support the amount and timing of cash flows; in case of borrowing facilities, has the auditor been able to obtain confirmation regarding its existence, terms and adequacy; in case of litigation and claims, has the auditor inquired of the legal counsel/been able to obtain sufficient evidence ,on the reasonableness of management's expectations)
 16. What aspects of the going concern assessment are based on management representation and has the auditor found them to be reasonable, particularly with respect to feasibility of future plans?¹⁴
 17. Are there any existing or potential breaches of covenants that the auditor has considered and how has the impact been considered by management and assessed by the auditor?
 18. Did the work related to going concern assessment cause the auditor to revise the assessed risks of material misstatement or the planned procedures elsewhere in the audit?
 19. Where a parent entity, promoter or any other party has provided support that is critical to the going concern assessment:
 - a. Was the auditor able to obtain written confirmation of the terms

- and conditions of that support directly from the supporting party?
- b. What is the auditor's view on enforceability of the support arrangement?
- c. Has the auditor been able to assess the financial ability of the supporting party¹⁵ to extend support, if needed and what is the auditor's conclusion?

20. In case of a group situation, are both the standalone and consolidated financial statements prepared on going concern basis, and if not, why?
21. In respect of material subsidiaries, joint venture or associates, has the auditor obtained sufficient and appropriate evidence that cash flow assumptions are consistent with going concern assessment? In case of any concerns flagged in such entities, what has been the auditor's response?

Going concern basis is appropriate, but no material uncertainty exists and the disclosure is adequate

22. Did the auditor assess that it was a close call¹⁶ and how was that assessment arrived at?
23. In case of a close call, does the auditor find the management's conclusion regarding the disclosures made under the circumstances, reasonable?

Going concern basis is appropriate, but material uncertainty exists; however, the disclosure is adequate

24. What were the events or conditions considered by the auditor in the going

¹⁴ Paragraph 16 and A20 of SA 570 (Revised)

¹⁵ Paragraph 12, 13 and A13 of SA 570 (Revised)

¹⁶ Whilst not specifically mentioned in SA 570 (Revised) or the corresponding ISA 570 (Revised), this phrase has been used to

describe the situations contemplated in Paragraph 20 of SA 570 (Revised) by IAASB and is frequently used by auditors. Refer <https://www.iaasb.org/publications/reporting-going-concern-matters-auditor-s-report>

concern assessment and how was the conclusion that material uncertainty exists, arrived at?

25. Has the auditor concluded on whether the matter will be considered as a Key Audit Matter and what led to the conclusion?

Going concern basis is appropriate, but a material uncertainty exists and the disclosure is not adequate

26. In the auditor's view, what is the missing or inadequate information in the disclosure, and whether- the management provided any reasons for non-inclusion of such information?
27. What is the effect of the inadequate disclosure (material and/or pervasive) and what is the basis of that conclusion?

Going concern basis has been used but its use is inappropriate

28. What is the basis and evidence considered by the auditor to conclude that the use of going concern basis is inappropriate and what is the management's response to those observations?
29. What is the impact of having used going concern basis for preparation of the financial statements (as against another basis., e.g. alternate basis)?

Use of going concern basis is inappropriate and another acceptable basis has been used

30. In the auditor's view whether the alternate basis used by the management is acceptable under the circumstances?
31. Has the auditor evaluated the adequacy of disclosures¹⁷ about the basis of accounting on which the financial statements are prepared?

32. Has the auditor concluded on whether an Emphasis of Matter will be included on use of another acceptable method and what led to the conclusion?

Additional considerations in case of regulated entities

33. Has the auditor assessed whether the company is meeting the capital, solvency, liquidity or other prudential requirements applicable to it¹⁸?
34. Does the auditor find the extent of disclosures regarding breach or potential breach of prudential norm, adequate under the circumstances?
35. Has the auditor assessed whether a change in law, regulation or government policy expected to adversely affect the company¹⁹?

¹⁷ Paragraphs 21 and A27 of SA 570 (Revised)

¹⁸ Paragraphs 10 and A3 of SA 570 (Revised)

¹⁹ Paragraphs 10 and A3 of SA 570 (Revised)

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