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Are You a Going Concern?

The FASB's update *Presentation of Financial Statements—Going Concern (Subtopic 205-40)* requires management to assess an entity's ability to continue as a going concern by incorporating and expanding upon certain principles that are currently in the US auditing standards. Ben Leung and Joseph Domingo of EisnerAmper Cayman provide some guidance.

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The rules of US Generally Accepted Accounting Principles (GAAP) are no longer silent on management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and what management should disclose in their financial statements.

In August 2014 the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-15, titled Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern, which provides guidance about management's responsibilities in this regard.

Guidance has been issued to reduce diversity in timing and content of footnote disclosures. Management need to consider this guidance to produce US GAAP-compliant financial statements.

Specifically, the amendments (1) provide a definition of the term 'substantial doubt'; (2) require an evaluation every reporting period including interim periods; (3) provide principles for considering the mitigating effect of management's plans; (4) require certain disclosures when substantial doubt is alleviated as a result of consideration of management's plans; (5) require an express statement and other disclosures when substantial doubt is not alleviated; and (6) require an assessment for a period of one year after the date the financial statements are issued (or available to be issued).

The meaning of 'substantial doubt'

Substantial doubt about an entity's ability to continue as a going concern exists when conditions and events, considered in the aggregate, indicate that it is probable that the entity will be unable to meet its obligations as they become due within one year after the date the financial statements are issued (or within one year after the date the financial statements are available to be issued when applicable).

Management assessments—considered in the aggregate

When evaluating an entity's ability to meet its obligations, management shall consider quantitative and qualitative information about the following conditions and events, among other relevant conditions and events known and reasonably knowable at the date the financial statements are issued:

a) The entity's current financial condition, including its liquidity sources at the date the financial statements are issued (for example, available liquid funds and available access to credit);

b) The entity's conditional and unconditional obligations due or anticipated within one year after the date the financial statements are issued (regardless of whether those obligations are recognised in the entity's financial statements);

c) The funds necessary to maintain the entity's operations considering its current financial condition, obligations, and other expected cash flows within one year after the date the financial statements are issued; and

d) The other conditions and events, when considered in conjunction with (a), (b), and (c) above that may adversely affect the entity's ability to meet its obligations within one year after the date the financial statements are issued.

When relevant conditions or events, considered in the aggregate, initially indicate that it is probable that an entity will be unable to meet its obligations as they become due within one year after the date the financial statements are issued (and therefore they raise substantial doubt about the entity's ability to continue as a going concern), management shall evaluate whether its plans that are intended to mitigate those conditions and events, when implemented, will alleviate substantial doubt about the entity's ability to continue as a going concern.

Management plans to mitigate going concern issues

The mitigating effect of management's plans shall be considered in evaluating whether the substantial doubt is alleviated only to the extent that information available as of the date the financial statements are issued indicates both of the following:

a) It is probable that management's plans will be effectively implemented within one year after the date the financial statements are issued; and

b) It is probable that management's plans, when implemented, will mitigate the relevant conditions or events that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date the financial statements are issued.

Disclosures—when substantial doubts exist which are alleviated by management plans

If, after considering management's plans, substantial doubt about an entity's ability to continue as a going concern is alleviated as a result of consideration of management's plans, an entity shall disclose in the footnotes information that enables users of the financial statements to understand all of the following (or refer to similar information disclosed elsewhere in the footnotes):

a) Principal conditions or events that raised substantial doubt about the entity's ability to continue as a going concern (before consideration of management's plans);

b) Management's evaluation of the significance of those conditions or events in relation to the entity's ability to meet its obligations; and

c) Management's plans that alleviated substantial doubt about the entity's ability to continue as a going concern.

Disclosures—when substantial doubts exist which are not alleviated by management plans

If, after considering management's plans, substantial doubt about an entity's ability to continue as a going concern is not alleviated, the entity shall include a statement in the footnotes indicating that there is substantial doubt about the entity's ability to continue as a going concern within one year after the date the financial statements are issued.

Additionally, the entity shall disclose information that enables users of the financial statements to understand all of the following:

a) Principal conditions or events that raise substantial doubt about the entity's ability to continue as a going concern;

b) Management's evaluation of the significance of those conditions or events in relation to the entity's ability to meet its obligations; and

c) Management's plans that are intended to mitigate the conditions or events that raise substantial doubt about the entity's ability to continue as a going concern.

If conditions or events continue to raise substantial doubt about an entity's ability to continue as a going concern in subsequent annual or interim reporting periods, the entity shall continue to provide the required disclosures in those subsequent periods.

Disclosures should become more extensive as additional information becomes available about the relevant conditions or events and about management's plans. An entity shall provide appropriate context and continuity in explaining how conditions or events have changed between reporting periods.

For the period in which substantial doubt no longer exists (before or after consideration of management's plans), an entity shall disclose how the relevant conditions or events that raised substantial doubt were resolved.

These amendments are effective for annual periods ending after December 15, 2016 and for annual periods and interim periods thereafter. Early application is permitted.■

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