Implementation Guide to Standard on Auditing (SA) 570(Revised)
Going Concern

The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
New Delhi

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Foreword

Implementation Guides to Standards on Auditing (SA) are an important resource for the members to appropriately understand the requirements of these Standards and help them to implement these Standards in an appropriate manner in their audit engagements.

The first edition of the "Implementation Guide to SA 570, *Going Concern*" was brought out by Auditing and Assurance Standards Board of ICAI in the year 2013. Pursuant to revision of SA 570, there emerged the need to revise the Implementation Guide issued earlier.

I congratulate the Auditing and Assurance Standards Board in taking this initiative of revising the Implementation Guide as per SA 570(Revised), *Going Concern*. The Implementation Guide has been written in easy to understand lucid language. I am sure the Implementation Guide would be able to address the practical difficulties, if any, being faced by the members in implementing this Standard.

I extend my sincere appreciation to the entire Board and specially appreciate the efforts put in by CA. G. Sekar, Chairman and CA. Debashis Mitra, Vice-Chairman for bringing out this Implementation Guide for benefit of the members.

August 14, 2019 **CA Prafulla P. Chhajed**
New Delhi President, ICAI

Preface

In 2013, the Auditing and Assurance Standards Board of ICAI issued the “Implementation Guide to SA 570, Going Concern” to provide practical implementation guidance to the members on this Standard. ICAI issued SA 570(Revised), Going Concern in 2016 which is applicable for the audits of financial statements on or after April 1, 2017. The revised Standard has strengthened the audit requirements and has made certain changes in auditor’s reporting requirements of going concern aspect. These changes necessitated revision of the Implementation Guide earlier issued.

I am happy to place in hands of the members, this revised Implementation Guide to SA 570(Revised), Going Concern brought out by the Auditing and Assurance Standards Board. The Implementation Guide provides a very practical and easy to follow approach to going concern assessment in the forms of questionnaire, checklists, templates and case studies, etc.

I wish to place on record high appreciation of CA. Debashis Mitra, Vice-Chairman of the Board for his whole-hearted effective co-ordination and contribution in publishing this material and in various activities of the Board.

I wish to express my sincere thanks to CA. Prafulla Premsukh Chhajed, Honourable President, ICAI and CA. Atul Kumar Gupta, Honourable Vice-President, ICAI for their guidance and support to the activities of the Board.

I am extremely grateful to CA. Pramod Jain, Delhi and his team comprising CA. Pranav Jain, CA. Sandeep Jain, CA. Sarika Gosain, CA. Asha Taneja for taking time out of their professional and personal preoccupations to revise this Implementation Guide. I also acknowledge the contribution of CA. Shriniwas Joshi in finalising this Implementation Guide.

I also wish to place on record my sincere thanks to all the Board Members and all the Council Members for their suggestions, support and guidance in finalising this Implementation Guide as well as other pronouncements of the Board. I also wish to thank CA. Megha Saxena, Secretary, AASB and staff of AASB for their dedicated efforts.

I am confident that the Implementation Guide would be well received by the members and other interested readers.

August 14, 2019
Chennai

CA. G. Sekar
Chairman,
Auditing and Assurance Standards Board

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Chapter 1
Introduction and Overview

1.1 The purpose of this Implementation Guide is to provide practical guidance on implementation of the principles enunciated in the Standard on Auditing (SA) 570 (Revised), Going Concern, issued by the Institute of Chartered Accountants of India. SA 570 (Revised) is effective for audits of financial statements for periods beginning on or after April 1, 2017.

1.2 Certain fundamental accounting assumptions underlie the preparation of financial statements and going concern is one of those fundamental accounting assumptions. They are usually not specifically stated because their use is accepted and assumed. A disclosure is necessary if they are not followed. However, when the use of the going concern basis of accounting is not appropriate in the circumstances, management may be required, or may elect, to prepare the financial statements on another basis (e.g., liquidation basis). The auditor may be able to perform an audit of those financial statements provided that the auditor determines that the other basis of accounting is acceptable in the circumstances. The auditor may be able to express an unmodified opinion on those financial statements, provided there is adequate disclosure therein about the basis of accounting on which the financial statements are prepared but may consider it appropriate or necessary to include an Emphasis of Matter paragraph in accordance with SA 706(Revised) in the auditor’s report to draw the user’s attention to that alternative basis of accounting and the reasons for its use. (Refer paragraph A27of SA 570 (Revised)).

1.3 The enterprise is normally viewed as a going concern, that is, as continuing in operation for the foreseeable future. An entity’s continuance as a going concern for the foreseeable future is assumed in the preparation of financial statements in the absence of significant information to the contrary. Accordingly, assets and liabilities are recorded on the basis that the entity will be able to realise its assets and discharge its liabilities in the normal course of business. If this assumption is unjustified, the amounts and classification of assets and liabilities in the financial statements may need to be adjusted. A few examples of situations of going concern are as under:

(i) An oil and gas firm is stopped by a court from carrying out operations. The firm is not a going concern, because it has to shut down operations because of the said directions from the court.

(ii) A nationalized refinery is in cash flows problems but the government of the country provided a guarantee to the refinery to help it out with all payments, the refinery is a going concern despite poor financial position, since it has a support of the country's government.

(iii) A bank is in serious financial troubles and the government is not willing to bail it out. The Board of Directors has passed a resolution to liquidate the business. The bank is not a going concern.

(iv) A merchandising company has a current ratio below 0.5. A creditor of Rs. 5 crores demanded payment which the company could not make. The creditor requested the court to liquidate the business and recover his debts and the court grants the order. The company is no longer a going concern.

(v) A company is having significant cash and bank balances but does not carry any business activities. The net worth is positive and there are no borrowings. The company is going concern as there are no negative indicators.

However, under each of these cases, the auditor needs to review the underlying facts so as to conclude on the use of going concern basis of accounting in the preparation of financial statements.

1.4 The importance of 'going concern' basis of accounting in the preparation of financial statements can be gauged from the fact that a number of important laws and regulations impose specific responsibilities on managements as well as auditors in relation to going concern. For example, Section 134(5) of the Companies Act, 2013 *inter alia* requires the Board of Directors to make a specific assertion in their Directors' Responsibility Statement under this Section that the directors have prepared the annual accounts on a going concern basis. Similarly, regulation 18(3) of the Securities and Exchange Board of India (SEBI) (Listing Obligations and Disclosure Requirements) Regulations, 2015 envisages the Audit Committee had to review with management that the annual financial statements and auditor's report thereon before submission to the board for approval, with particular reference to matters required to be included in the director's responsibility statement to be included in the board's report in terms of clause (c) of sub-section (3) of Section 134 of the Companies Act, 2013 which requires the directors to make a specific assertion that the annual accounts have been prepared on a going concern basis of accounting.

1.5 This Implementation Guide provides a framework to assist in determining whether the use of going concern basis of accounting in preparation of the financial statements and the related disclosures are appropriate and in making balanced, proportionate and clear disclosures.

Chapter 2
The Implementation Guidance and Suggested Questionnaire

2.1 Under the going concern basis of accounting, the financial statements are prepared on the assumption that the entity is viewed as a going concern and will continue its operations for the foreseeable future. This Implementation Guide provides guidance in relation to going concern considerations covering broadly the following areas:

- Accounting framework.
- Evaluation of management's assessment of the entity's ability to continue as a going concern.
- Events or conditions that may cast significant doubts about the entity's ability to continue as a going concern.
- Determining the implications for the auditor's report when reporting in accordance with the Standards on Auditing and possible impact on reporting under section 143(3)(h) of the Companies Act, 2013.
- Consultation within audit team and with the client/management/audit committee.
- Reviewing interim financial information in accordance with the Standard on Review Engagements.

2.2 Given below are the Responses on key issues of SA 570(Revised) in a Question-Answer format.

Q.1 **Who is responsible to assess the entity's ability to continue as a going concern?**

Ans.1: The assessment of an entity's ability to continue as a going concern is the responsibility of the entity's management. The auditor needs to evaluate management's assessment of the entity's ability to continue as a going concern.

Q.2 **Over what period is going concern assessed?**

Ans.2: In evaluating management's assessment of the entity's ability to continue as a going concern, 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 SA 560, *Subsequent Events*, the auditor shall request management to extend its assessment period to at least twelve months from that date.

Q.3 **What factors are taken into account by the management when assessing the entity's ability to continue as a going concern?**

Ans.3: Management's assessment of the entity's ability to continue as a going concern involves making a judgment, at a particular point in time, about inherently uncertain future outcomes of events or conditions. The following factors are relevant to that judgment:

- The degree of uncertainty associated with the outcome of an event or condition increases significantly the further into the future an event or condition or the outcome occurs. For that reason, most financial reporting frameworks that require an explicit management assessment specify the period for which management is required to take into account all available information.
- The size and complexity of the entity, the nature and condition of its business and the degree to which it is affected by external factors affect the judgment regarding the outcome of events or conditions.
- Any judgment about the future is based on information available at the time at which the judgment is made. Subsequent events may result in outcomes that are inconsistent with judgments that were reasonable at the time they were made.

Q.4 **What evidence does Management normally consider when assessing the entity's ability to continue as going concern?**

Ans.4: The evidence normally considered by management when assessing the entity's ability to continue as going concern includes:

- Cash flow projections that show an ability to pay debts as and when they fall due after factoring realistic assumptions in the current market conditions.
- If current conditions deteriorate further, detailed business plans covering the period under consideration.
- Support for the entity's ability to obtain new funding upon the maturity of existing funding arrangements.
- Evidence that debt covenants have been assessed and any risk of breaching them has been managed, such that they do not provide significant risk.
- Management may consider having support of 'Support Letter' from the parent company for financial support for the next twelve months, as required, from the date of the latest balance sheet.
- In an unlikely situation, Support Letter may be given by the government or any other financial situation as well; however, this is a rare phenomenon. However, a mere "Support Letter" or "Comfort Letter" will generally not constitute sufficient and appropriate audit evidence to conclude on appropriateness of management's use of going concern basis of accounting. Where an auditor relies on a "support letter" as an evidence, he/ she should also evaluate the financial strength and capability of the parent company (Group company) issuing support letter to be able to discharge liabilities of the company. A standard template of Support Letter is given in **Annexure II** of this Implementation Guide.

Q.5 **What are the auditor's responsibilities for assessing the entity's ability to continue as going concern?**

Ans.5: The auditor's responsibilities are:

- To obtain sufficient appropriate audit evidence regarding and conclude on the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements;
- To conclude, based on the audit evidence obtained, whether a material uncertainty exists about the entity's ability to continue as a going concern.

These responsibilities exist even if the financial reporting framework used in the preparation of the financial statements does not include an explicit requirement for management to make a specific assessment of the entity's ability to continue as a going concern.

Q.6 **What should auditor do if management has not performed a preliminary assessment of the entity's ability to continue as going concern?**

Ans.6: In such a situation, the auditor needs to:

- discuss with management the basis for the intended use of the going concern basis of accounting.
- inquire of management whether events or conditions exist that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern.

Further, the auditor should remain alert throughout the audit for audit evidence of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern.

Q.7 **How should auditor evaluate management's assessment of going concern?**

Ans.7: In evaluating management's assessment of the entity's ability to continue as going concern, the auditor would 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. The period of assessment would be of at least twelve months from the date of the financial statements. In case the period of assessment is less than that, the auditor would request the management to cover at least a 12 months period.

The auditor's procedures for evaluating management's assessment of going concern would also include:

- Ensuring management's assessment includes all relevant information of which the auditor is aware as a result of the audit.

Q.8 What are the responsibilities of auditor for the period beyond management's assessment?

Ans.8: The auditor needs to inquire of management as to its knowledge of events or conditions beyond the period of management's assessment that may cast significant doubt on the entity's ability to continue as a going concern.

Q.9 What are the Additional Audit Procedures to be performed When Events or Conditions that may cast significant doubt on the entity's ability to continue as going concern are identified?

Ans.9: In such a scenario, the auditor needs to perform additional audit procedures to obtain sufficient appropriate audit evidence to determine whether or not a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. In doing so, the auditor would also need to take into consideration, the mitigating factors, if any. These procedures include:

- Where management has not yet performed an assessment of the entity's ability to continue as a going concern, requesting management to make its assessment.
- Evaluating management's plans for future actions in relation to its going concern assessment, whether the outcome of these plans is likely to improve the situation and whether management's plans are feasible in the circumstances.

- Where the entity has prepared a cash flow forecast, and analysis of the forecast is a significant factor in considering the future outcome of events or conditions in the evaluation of management's plans for future action:
  - Evaluating the reliability of the underlying data generated to prepare the forecast; and
  - Determining whether there is adequate support for the assumptions underlying the forecast.
- Considering whether any additional facts or information have become available since the date on which management made its assessment.
- Requesting written representations from management regarding their plans for future action and the feasibility of these plans.

Q.10 What should auditor do when use of Going Concern Basis of Accounting is Appropriate but a Material Uncertainty Exists?

Ans.10: In such a situation, the disclosure made by the entity in its financial statements become very important. The auditor should, therefore, determine whether the financial statements:

- Adequately describe the principal events or conditions that may cast significant doubt on the entity's ability to continue as a going concern and management's plans to deal with these events or conditions; and
- Disclose clearly that there is a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern and, therefore, that it may be unable to realize its assets and discharge its liabilities in the normal course of business.

For the above purpose the fact whether the information explicitly draws the readers' attention to the possibility that the entity may be unable to continue realizing its assets and discharging its liabilities in the normal course of business, would be an important factor for the auditor.

The auditor is also required to determine whether disclosures about a material uncertainty, required by the applicable financial reporting framework, are adequate. Disclosures required by some financial reporting frameworks that are in addition to matters set forth above may include disclosures about:

- Management's evaluation of the significance of the events or conditions relating to the entity's ability to meet its obligations; or
- Significant judgments made by management as part of its assessment of the entity's ability to continue as a going concern.

Q.11 What should auditor do if Events or Conditions Have Been Identified but no Material Uncertainty Exists?

Ans.11: If events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern but, based on the audit evidence obtained the auditor concludes that no material uncertainty exists, the auditor shall evaluate whether, in view of the requirements of the applicable financial reporting framework, the financial statements provide adequate disclosures about these events or conditions.

Q.12 **What are the auditor's reporting responsibilities if the auditor concludes that a material uncertainty exists and adequate disclosure of material uncertainty is made in the financial statements?**

Ans.12: In such a situation the auditor would express an unmodified opinion on the financial statements. However, his report would also need to include a separate paragraph on "Material Uncertainty related to going concern". This paragraph would:

- Highlight the existence of a material uncertainty relating to the event or condition that may cast significant doubt on the entity's ability to continue as a going concern.
- Draw attention to the note in the financial statements that discloses the matters.

An example of such wording for paragraph that may be included on 'Material Uncertainty related to Going Concern' has been given in **Annexure – I, Part A** of this Implementation Guide.

Q.13 **How should auditor report if a material uncertainty exists and adequate disclosure in respect of material uncertainty is not made in the financial statements?**

Ans.13: In the absence of adequate disclosures in the financial statements in respect of existence of material uncertainty relating to going concern basis of accounting, the auditor would need to express a qualified or an adverse opinion, as may be appropriate, in terms of principles enunciated in SA 705 (Revised), "Modifications to the Opinion in the Independent Auditor's Report". The auditor's report should clearly state that there is a material uncertainty that may cast significant doubt about the entity's ability to continue as a going concern.

Examples for paragraph to be included in audit report for; Qualified opinion and Adverse opinion, have been given in **Annexure – I, Part B** of this Implementation Guide**.**

Q.14 **What should auditor do if Use of Going Concern Basis of Accounting is Inappropriate?**

Ans.14: If in the auditor's judgment, management's use of the going concern basis of accounting in the preparation of the financial statements is inappropriate, due to existing facts and circumstances then the auditor shall express an adverse opinion.

For example

1. Company has passed a resolution to wind up its operations, and still used going concern basis of accounting for preparation of the financial statements, without disclosing the facts in the financial statements. In such circumstances, auditor would need to issue an adverse opinion.

2. The company's financing arrangements expire and amounts outstanding are payable on 30 August 20XX. The company has been unable to re-negotiate or obtain replacement financing. This situation indicates the existence of a material

uncertainty which may cast significant doubt on the company's ability to continue as a going concern and therefore it may be unable to realise its assets and discharge its liabilities in the normal course of business. The financial statements (and notes thereto) do not disclose this fact. In such circumstances, auditor would need to issue an adverse opinion

Q.15 **What should auditor do if management is Unwilling to Make or Extend Its Assessment?**

Ans.15: If management is unwilling to make or extend its assessment when requested to do so by the auditor, the auditor should consider the implications for the auditor's report. The auditor might have to issue a qualified opinion or a disclaimer of opinion, as considered appropriate, because it may not be possible for the auditor to obtain sufficient appropriate audit evidence regarding the management's use of going concern basis of accounting in the preparation of the financial statements.

Q.16 **What should be communicated to Those Charged with Governance (TCWG) and when?**

Ans.16: Unless all those charged with governance are involved in managing the entity, the auditor needs to communicate with those charged with governance events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern. Such communication with those charged with governance includes the following:

- Whether the events or conditions constitute a material uncertainty;
- Whether the management's use of the going concern basis of accounting is appropriate in the preparation of the financial statements;
- The adequacy of related disclosures in the financial statements; and
- Where applicable, the implications for the auditor's report.

Generally, a meeting of the audit committee is not held in the interim except when it meets to approve the quarterly results and/

or annual financial statements. At that meeting, auditors' report (with the going concern matter) should be placed before Those Charged with Governance. However, if considered, appropriate, the auditor may communicate with Those Charged with Governance before such a meeting of the Audit Committee.

Q.17 **What should the auditor do if there is Significant Delay in the Approval of Financial Statements?**

Ans.17: In such cases, the auditor should inquire as to the reasons for the delay. If delay relates to events or conditions relating to the going concern assessment, the auditor should perform additional audit procedures as necessary as well as consider the effect on the auditor's conclusion regarding the existence of a material uncertainty, as listed in paragraphs 16 and 18 of SA 570 (Revised).

Q.18 **An Interim Resolution Professional (IRP) has been appointed under the provisions of Insolvency and Bankruptcy Code, 2016 as the Corporate Insolvency Resolution Process (CIRP) has been initiated by an order of NCLT. Accordingly, the affairs of the Company are being managed by an IRP. The auditor has asked the IRP to provide with management's assessment of the entity's ability to continue as a going concern. The IRP provides with the assessment for a period of 180 days from beginning of CIRP period stating that he has been appointed for such period. What are the auditor's responsibilities under such circumstances?**

Ans.18: The timing of 12 months period for assessment of a going concern under SA 570(Revised) cannot be compared with 180/270 days of CIRP period as it will depend from which date the CIRP period will commence, e.g. if CIRP period starts from 1st January, auditor may have to assess the assumption of going concern for 31st March accounts. In other words, the period of CIRP and assessment period for going concern has no relevance.

So, the auditor may seek sufficient information from the IRP for his assessment of going concern. The IRP based on availability of information and his own assessment can furnish the relevant details to the auditor. The auditor would have to examine independently based on the information available as to whether he is satisfied or not and then decide the nature of report like qualified or adverse or disclaimer.

In nutshell, the IRP has to furnish information to the extent possible for him and the auditor has to make an independent assessment for going concern. The period has no relevance.

Q.19 **The IRP of a company under CIRP contends that as per Section 20(1) of IBC 2016, an Interim Resolution Professional shall manage the operations of the Corporate Debtor as a going concern. Further as per Section 25(1) of the IBC 2016, it shall be the duty of the IRP to ensure continued business operations of the corporate debtor and accordingly, the auditor should not challenge the use of going concern basis of accounting.**

Ans.19: The provisions of IBC 2016 do not affect the auditor's responsibility as per SA 570(Revised). Accordingly, the auditor should perform procedures as described in Question 9 above. Auditor should evaluate impact on auditor's report in accordance with paragraphs 21, 22, 23 and 24 of SA 570(Revised).

Q.20 **The auditor argues that since there are no apparent indicators that going concern basis of accounting is not justified, there is no need for any documentation regarding Going Concern.**

Ans.20: As per SA 700(Revised), the auditor's responsibility in the Auditor's Report include an explicit statement by the auditor to "Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern."

Accordingly, the auditor should document in his/ her working papers the basis for such conclusion and evidence obtained. This may be done by completing Section A of the Suggested Checklist included in this Implementation Guide.

Q.21 **Is Emphasis of Matter Paragraph (EOM) also required to be given for the situation where the auditor is required to give Separate Paragraph on "Material Uncertainty Related to Going Concern" to highlight material uncertainty" as per SA 570 (Revised).**

Ans.21: In situations which warrant separate Paragraph on "Material Uncertainty Related to Going Concern" (See Q12 above) as per SA 570(Revised), auditor is not required to give EOM paragraph.

Q.22 **Is including Material Uncertainty Related to Going Concern as a Key Audit Matter as per SA 701 sufficient compliance with the requirements of SA 570(Revised)?**

Ans.22: As per Paragraph 4 of SA 701, "Communicating Key Audit Matters in the Independent Auditor's Report", communicating key audit matters is not a substitute for reporting in accordance with SA 570(Revised) when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern. Accordingly, separate paragraph as per SA 570(Revised) should be given.

Chapter 3
Template for Checklists for Evaluating Management's Use of Going Concern Basis of Accounting

An entity's continuance as a going concern for the foreseeable future is assumed in the preparation of financial statements in the absence of significant information to the contrary. Accordingly, assets and liabilities are recorded on the basis that the entity will be able to realize its assets and discharge its liabilities in the normal course of business. If this assumption is unjustified, the amounts and classification of assets and liabilities in the financial statements may need to be adjusted. A detailed analysis for testing of related indicators regarding uncertainty of going concern consideration is briefly enumerated in the below checklist:

Going-Concern Consideration Program

	Particulars	Going concern indicator present (Yes/No/Not Applicable and References, if any)
A:	Going Concern Considerations	
1.	Consider whether there is a risk that the entity will not continue as a going concern for the foreseeable future: **Consider Financial Indications** • Recurring operating losses. • Negative Net Worth.	

• Working capital deficiencies. • Continuing negative cash flows from business activities. • Excessive reliance on short-term borrowings to finance long-term assets. • Adverse key financial ratios. • Inability to pay creditors on due dates. • Default on loans or similar agreements. • Restrictions on usual trade terms. • Restructuring of debt. • Entered into any arrangement with creditors for reduction of payment. • Arrears or discontinuance of dividends. • Excessive or obsolete stock. • Unable to obtain finance for new product development or essential investment. • Need to seek new sources or methods of financing, or fixed-term borrowings approaching maturity without realistic prospects of renewal or repayment. • Need to dispose of substantial assets. • Application filed against Corporate Debtor in NCLT under IBC 2016. • Sick entity under any statutory definition.	
Consider Operating Indications • Loss of key management or staff. • Work stoppages or other labor difficulties. • Substantial dependence on the success of a particular project or on a particular asset. • Management intentions to liquidate the entity or cease operations. • Emergence of a highly successful competitor.	

	• Excessive reliance on the success of a new product. • Uneconomic long-term commitments. • Loss of a major market or principal supplier. • Loss of a key franchise, license, or patent.	
	Consider Other Indications • Noncompliance with capital or other statutory requirements. • Pending legal proceedings or similar matters that might jeopardize an entity's ability to operate. • Changes in or establishment of new legislation or government policy. • Technical developments that render a key product obsolete.	
B:	Consideration of Management's Assessment	
1.	Evaluate management's assessment of the entity's ability to continue as a going concern. (The auditor should consider the same period as that used by management in making its assessment under the applicable financial reporting framework. If management's assessment of the entity's ability to continue as a going concern covers less than twelve months from the balance sheet date, the auditor should request management to extend its assessment period to twelve months from the balance sheet date.)	
2.	Inquire of management as to its knowledge of events or conditions and related business risks beyond the period of assessment used by management that may cast significant doubt on the entity's ability to continue as a going concern.	

3.	Evaluate the information obtained above in conjunction with other information obtained throughout the audit that may impact auditor's assessment of the appropriateness of the management's use of the going concern basis of accounting.	
C:	Consideration of Management's Plans	
1.	If, after considering the identified conditions and events in the aggregate, the auditor believes that continuance as a going concern may be questionable, he/she should consider management's plans for dealing with the adverse effects of the identified conditions and events and assess the likelihood of effective implementation thereof.	
2.	Obtain information about management's plans and consider whether it is likely that the adverse effects will be mitigated for the foreseeable future. Evaluate the likelihood of effective implementation of such plans. Plans that the auditor would consider and discuss with management may include: • Plans to dispose of assets. • Plans to borrow money or restructure debt. • Plans to reduce or delay expenditures. • Plans to increase revenues more than increases in related costs and expenses. • Plans to increase ownership equity.	
3.	Consider the bases on which the plans have been prepared, giving consideration as to whether they conform with facts already known and to available independent evidence.	

4.	Carry out additional procedures to update information obtained earlier. Such procedures may include:	
	• Analysis and discussion of cash flow, profit, and other relevant forecasts with management.	
	• Review of events after the balance-sheet date for items affecting the entity's ability to continue as a going concern.	
	• Analysis and discussion of the entity's latest available interim financial statements.	
	• Review of the terms of debentures and loan agreements and determination whether any have been breached.	
	• Reading of minutes of the meetings of shareholders, board of directors, and other important committees for reference to financing difficulties.	
	• Request for information on relevant material legal matters from the entity's legal counsel.	
	• Confirmation of the existence, legality, and enforceability of arrangements to provide or maintain financial support with related and third parties, and assessment of the financial ability of such parties to provide additional funds.	
	• Consideration of the entity's position concerning unfilled customer orders.	
	• Obtaining written representation from management concerning plans for future action whose outcome is expected to mitigate the situation.	

5.	Obtain written confirmation of the corresponding representations by the management.	
6.	When prospective financial information is particularly significant to management's plans, consider, based on the auditor's knowledge of the entity, its business and management, the adequacy of support for significant assumptions underlying that information. Compare the prospective data for recent prior periods with historical results and the prospective data for the current period with results achieved to date. Consider the reliability of the entity's system for generating such information and give particular attention to assumptions that are: • Material to the prospective financial information. • Especially sensitive or susceptible to change. • Inconsistent with historical trends.	
D	Management Representation	
1.	When additional disclosures are made in the financial statements relating to the entity's ability to continue as a going-concern, obtain a specific management representation stating that the disclosures contain all of the pertinent facts.	
2.	Consider whether particular matters need to be represented by management related to the considerations of the entity's ability to continue as a going concern.	
E	Consideration of Effects on the Financial Statements.	

1.	If, after considering management's plans, the auditor concludes that the going-concern question is not satisfactorily resolved, the auditor would consider the possible effects on the financial statements and ensure the adequacy of the related disclosure. The disclosure should:	
	• Describe the principal conditions and events that raised doubt about the entity's ability to continue as a going concern for the foreseeable future.	
	• Describe the possible effects of such conditions and events and management's evaluation of the significance of those conditions.	
	• Describe any mitigating factors and the management's plans (including relevant prospective financial information).	
	• State that there are doubts that the entity will be able to continue as a going concern and, therefore, may be unable to realize its assets and discharge its liabilities in the normal course of business.	
	• State that the financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or to amounts and classification of liabilities that may be necessary should the entity be unable to continue as a going concern.	
2.	If the auditor concludes that management's use of the going concern basis of accounting	

	is appropriate because of mitigating factors (in particular management's plans for future action), evaluate the need for disclosure of the principal conditions and events that initially caused the substantial doubt. Disclosure considerations include the possible effects of such conditions and events and any mitigating factors, including management's plans.	
F:	Consultation	
1.	If the auditor concludes that an entity's continuance as a going concern for the foreseeable future is questionable, consider consultation within the firm to consider management's plans or representations and financial statement effects.	
G:	Accounting Policies and Disclosures	
1.	Consider whether the presentation of the financial statements conforms with professional standards and the applicable legal or regulatory requirements. Consider whether:	
	• Material transactions or items may require separate disclosure.	
	• Accounting policies used in the financial statements are appropriate and are consistent with prior periods.	
	• Balances and associated footnote disclosures are presented in accordance with the accounting policies.	
H:	Conclusion: • Based on the tests performed and responses as noted above, a conclusion may be drawn whether management's	

use of the going concern basis of accounting is appropriate. • Also give reference to the type of audit report that may be issued based on the conclusion drawn under this section (Refer Annexure – I for audit report format).	

Chapter 4
Practical Case Studies and Illustrative Examples

Section A – Case Studies

Case Study 1: Going Concern Audit Report

You are the audit manager responsible for performing hot reviews on audit files where there is a potential disagreement between your firm and the client regarding a material issue. You are reviewing the going concern section of the audit file of Sunshine Ltd, a client with considerable cash flow difficulties, and other, less significant operational indicators of going concern problems. The working papers indicate that Sunshine Ltd is currently trying to raise finance to fund operating cash flows, and state that if the finance is not received, there is significant doubt over the going concern status of the company. The working papers conclude that the going concern basis of accounting is appropriate, but it is recommended that the financial statements should contain a note explaining the cash flow problems faced by the company, along with a description of the finance being sought, and an evaluation of the going concern status of the company. The directors do not wish to include the note in the financial statements.

Identify and discuss the implications for the audit report if:

(i) the directors refuse to give the disclosure note.

(ii) the directors agree to give the disclosure note.

Suggested Response

i) The Directors refuse to give the disclosure note:

The audit report should contain a qualified or an adverse opinion due to the disagreement. The auditors need to make a decision as to the significance of the non-disclosure of the uncertainty surrounding going concern basis of accounting. If it is decided that without the note the financial statements are not fairly presented, and could be considered misleading, an adverse opinion should be expressed.

ii) The Directors agree to give the disclosure note:

If the directors agree to give the disclosure note, it should be reviewed by the auditors to ensure that it is sufficiently detailed. In evaluating the adequacy of the disclosure in the note, the auditor should consider whether the disclosure explicitly draws the reader's attention to the possibility that the entity may not be able to continue as a going concern in the foreseeable future. The note should include a description of conditions giving rise to significant doubt, and the directors' plans to deal with the conditions. If the disclosure is considered adequate, then the opinion should not be qualified. The auditors should, however, consider adding a section on "Material Uncertainty Related to Going Concern" in accordance with SA 570(Revised) to highlight the existence of the material uncertainties, and to draw attention to the note to the financial statements. The section should firstly contain a brief description of the uncertainties, and also refer explicitly to the note to the financial statements where the situation has been fully described. The section should re-iterate that the audit opinion is not qualified. However, it could be the case that a note has been given in the financial statements, but that the details are inadequate and do not fully explain the significant uncertainties affecting the going concern status of the company. In this situation the auditors should express a qualified opinion. The auditor, however, may also consider expressing an adverse opinion, if it is warranted under the circumstances based on the auditor's professional judgment.

Case Study 2: Going Concern Audit Report

XYZ Inc. is a manufacturer of televisions. The domestic market for electronic goods is currently not doing well, and therefore many entities in this business are switching to exports. As per the audited financial statements for the year ended March 31, 20XX, the entity had net losses of Rs.120 million. At March 31, 20XX, its current assets aggregate to Rs.1,200 million and the current liabilities aggregate to Rs.1,500 million. Due to expected favorable change in the government policies for the electronic industry, the entity is projecting profits in the coming years. Furthermore, the shareholders of the entity have arranged alternative additional sources of finance for its expansion plans and to support its working capital needs in the next 12 months.

Required

Should XYZ Inc. prepare its financial statements under the going concern basis of accounting considering management's assessment for next twelve months?

Suggested Response

In this case, the two factors that raise doubts about the entity's ability to continue as a going concern are:

- The net loss for the year amounting to Rs.120 million.
- The working capital deficiency (current liability of Rs.1,500 million Less: current assets of Rs.1,200 million) of Rs.300 million existing at the balance sheet date.

However, there are two mitigating factors:

- The arrangements made by the shareholders to fund the entity's expansion and working capital needs; and
- Projected future profitability due to expected favourable changes in government policies for the industry the entity is operating in.

Based on these sets of factors, it may be possible for the management of the entity to argue that the going concern basis of accounting is appropriate and that any other basis of presentation of financial statements would be unreasonable at the moment.

If the auditor concludes based on available evidence including reasonability of future profitability that there is no material uncertainty related to going concern for at least next twelve months, there is no need to include section on "Material Uncertainty Related to Going Concern. It is, however, recommended to include a suitable note in the financial statements.

However, if matters deteriorate further instead of improving, then in the future another detailed assessment would be needed to ascertain whether the going concern basis of accounting is still valid and accordingly suitable disclosure may be made in the financial statements and the same shall be considered by the auditor *vis a vis* need to include a section on “Material Uncertainty Related to Going Concern” or Qualified or Adverse Opinion, as the case may be.

Case Study 3: Going Concern Basis of Accounting is not appropriate

ABC Ltd is a company which is into manufacturing of Yarn with two working Directors on Board each holding fifty percent equity. The Company was incorporated five years back. There was a dispute among both Directors and due to which both directors filed for liquidation of company. The Company has sufficient assets including movable and immovable assets to pay off the liabilities of the company. Liquidation process is at initial stage. What disclosures are required in the financial statements and audit report of the company?

Suggested Response

In the present scenario, as the Company has initiated liquidation process, it is no longer a Going Concern. Accordingly, the financial statements cannot be prepared using the going concern basis of accounting. In case, the financial statements have been prepared using the going concern basis of accounting, the auditor shall express an adverse opinion as per paragraph 21 of SA 570 (Revised).

In case the financial statements are prepared on an alternative basis (e.g. Liquidation basis), the auditor may be able to perform an audit of those financial statements provided that the auditor determines that such alternative basis is an acceptable financial reporting framework in the circumstances. The auditor may be able to express an unmodified opinion on those financial statements, provided there is adequate disclosure therein about the basis of accounting on which the financial statements are prepared, but may consider it appropriate or necessary to include an Emphasis of Matter paragraph in accordance with SA 706 (Revised) in the auditor's report to draw the user's attention to that alternative basis of accounting and the reasons for its use. (Paragraph A27 of SA 570(Revised)).

Case Study 4: Start Up Company incurring losses

A Start-up company is into manufacturing of E-Motor Bikes and E-Rickshaws has been setup during the year. The Company has a share capital of Rs. 1 lakhs and unsecured loans of Rs 500 lakhs. During the year, the Company incurred loss of Rs. 50 lakhs. The unsecured loan has been granted by the promoter of company from his savings and by mortgaging his assets and taking loans from banks and financial institutions in his personal capacity. Company is ready with the designs of products but is short of funds to launch the product and for marketing. Bankers have refused to provide finance. The promoter is discussing funding from PE investors and is hopeful of getting P/E investment for the project. How should the auditor gather sufficient and appropriate audit evidence to conclude on appropriateness of going concern basis of accounting? What disclosures need to be made in the financial statements and audit report?

Suggested Response

In the present scenario, there are indicators that the going concern basis of accounting may not be appropriate. However, the auditor may consider the following:

(i) The Company is a start-up and this is the first year of operations. The auditor should consider normal gestation period in similar industries.

(ii) The auditor should consider any available tax benefits, subsidy, other benefits available from governments.

(iii) The auditor may consider finance available to similar start-ups or companies in similar segment.

(iv) The auditor should obtain future projections with projected cash flows including means of financing.

(v) The auditor should obtain evidence to support future projections and cash flows which may include orders/ enquiries from prospective customers, evidence of negotiations with potential investors, feasibility studies, market research, etc.

(vi) The auditor may consider option available with the company of converting loan from promoter into equity.

Considering the facts, a material uncertainty exists regarding going concern basis of accounting. However, the auditor will need to exercise his professional judgement considering available evidence including its reliability and sufficiency to conclude whether going concern basis of accounting is appropriate. Accordingly, disclosures in financial statements and implications on audit report will be dependent on auditor's conclusion.

Case Study 5: Comfort Letter by promoters

A company is an exclusive seller in the country for retail sale of imported branded garments and was setup two years ago having share capital of Rs. 1 lakhs and unsecured loans of Rs 200 lakhs has accumulated losses of Rs.50 lakhs. The unsecured loan has been granted by the promoter of company along with his family. The Company is having negative net-worth and negative working capital. The promoters have sufficient net worth and have plans to invest in the business in future.

How should the auditor gather sufficient and appropriate audit evidence to conclude on appropriateness of going concern basis of accounting? What disclosures need to be made in the financial statements and audit report?

Suggested Response

The auditor should obtain and review management's assessment of going concern basis of accounting, which includes:

- Cash flow projections.

- Detailed business plan covering the period of assessment.
- Support for the entity's ability to obtain new funding.

The auditor may obtain a "Support Letter" from the promoter for financial support for at least next twelve months. In case of a support letter, auditor should assess intent and capability of promoters to provide financial support.

However, in the present circumstances, material uncertainty exists. Accordingly, the financial statements should include adequate disclosures including availability of financial support from promoters. The auditor should report under a separate paragraph "Material Uncertainty Related to Going Concern" if adequate disclosures have been given in the financial statements.

Case Study 6: Business Losses and no future business plans

XYZ Inc. is in business of real estate. Post Demonetization and introduction of GST, there was a recession in real estate sector due to significant dip in demand and liquidity crisis in economy. The Company is facing cash flow problems. The Company has huge unsold semi-finished and finished inventory in its books of accounts. As on date of balance sheet, management did not have any concrete future orders in hand and did not have any realistic future plans.

What disclosures need to be made in the financial statements and audit report?

Suggested Response

In the present scenario, it is evident that the use of going concern basis of accounting is not appropriate. Accordingly, the financial statements cannot be prepared using the going concern basis of accounting. In case, the financial statements have been prepared using the going concern basis of accounting, the auditor shall express an adverse opinion as per paragraph 21 of SA 570 (Revised).

In case the financial statements are prepared on an alternative basis (e.g. Liquidation basis), the auditor may be able to perform an audit of those financial statements provided that the auditor determines that such alternative basis is an acceptable financial reporting framework in the circumstances. The auditor may be able to express an unmodified opinion on those financial statements, provided there is adequate disclosure therein about the basis of accounting on which the financial statements are prepared, but may consider it appropriate or necessary to include an Emphasis of Matter paragraph in accordance with SA 706 (Revised) in the auditor's report to draw the user's attention to that alternative basis of accounting and the reasons for its use. (Paragraph A27 of SA 570(revised)).

Section B – Other Illustrative Examples

Illustrative Examples of the Auditor's Assessment of Whether Evidence Provided by Those Charged with Governance, Concerning the Attention They Have Paid to the Period of One Year from the Date of the Financial Statements, is Sufficient.

The examples given below are illustrative only. The purpose of the examples is to illustrate the application of the SA 570(Revised) to assist in clarifying their meaning in a number of commercial situations. These examples focus on particular aspects of the situations illustrated and are not intended to be a comprehensive discussion of all the relevant factors that might influence either the management's or auditor's assessment of the appropriateness of the going concern basis. As the auditor would need to exercise judgment in the circumstances described, it is possible that different auditors may arrive at different conclusions. These examples neither modify nor override the related Standards on Auditing.

Example 1 - A small company producing specialized computer application software

Corollary from the auditor's risk assessment (Read with paragraph 10-11 of SA 570 Revised)

This owner managed company employs a few highly trained and highly paid computer system designers to design application software for use by transportation enterprises, such as airlines and bus companies, in preparing their timetables and fare structures. Few companies are engaged in this field and the supply of suitably trained staff is limited. The system designers, who met at University, have been with the company since its formation. They all have an equity interest in the company.

Although the company has only been in existence for five years it has established a reputation for excellence in its field. Its reputation derives from the skill and expertise of its individual employees rather than from anything attaching to the company itself.

A significant amount of time is spent by the designers in pure research activities for developing new products. In addition, the time needed to develop individual systems relating to an established product can be considerable. In addition to designing new systems, the company maintains those systems that it has installed, on a contractual basis and undertakes training courses in the use of the systems for the employees of its customers.

The company is thinly capitalized and relies primarily on advances from its customers supplemented by short term bank borrowings for its day to day cash requirements.

The company employs a part time book-keeper to prepare the financial statements, cash flow forecasts and maintain the books of account.

The company has usually been in a position to choose which contracts it accepts and has not had difficulty in recovering its costs. The company is not economically dependent on any one transportation enterprise.

The company updates each month a rolling cash flow projection with a six-month time horizon. The company does not prepare projections for a longer period as it perceives its management need is to be able to manage effectively its short-term cash flow. The company has negotiated a line of credit with its bankers which it would be able to utilize to overcome short term cash shortages.

Assessment by the auditor

When the auditor assesses whether the directors have, in assessing going concern, paid particular attention to a period of one year from the date of the financial statements, the auditor:

(a) Reviews the cash flow forecasts for the six-month period from the date of the financial statements; and

(b) Enquires the directors about the steps they have taken to assess the appropriateness of the going concern basis for the subsequent six-month period.

The directors inform the auditor that they do not consider there is any need for cash flow forecasts to be prepared beyond six months because:

- The cash flow forecasts show a net cash inflow for the period;
- They have reviewed in detail the assumptions implicit in the forecast with the bookkeeper and concur with them;
- The company has a significant back-log of orders which will occupy half of the designers for at least the next year;
- The company is actively tendering for both systems design and maintenance contracts in the United Kingdom and Europe and is considering expanding into the Americas;
- The company has recently renewed its arrangements with its bankers for a further year;
- The design employees seem to be settled and stimulated and there is no reason to believe that they will leave the company in the foreseeable future; and
- In the unlikely event that the company did not win many of the tenders it could modify its existing expansion plans which have been necessitated by an increase in maintenance contracts. Rather than employ new staff to undertake this work existing staff could be reassigned to it.

The auditor concludes that the directors have paid particular attention to the period ending one year after their approval of the financial statements.

Example 2 - An enterprise in the fashion (or seasonal) industry

Corollary from the auditor's risk assessment (Read with paragraph 10-11 of SA 570 Revised)

This company employing 1,000 people designs and manufactures ladies fashion wear. Its business is seasonal, and it presents two major collections per year: one in the spring and one in the autumn.

The company has attracted established designers and they are regarded as one of the leading manufacturers.

Almost all of the company's sales orders are received from the major retailers when they show their collections. Although some of the garments are manufactured prior to the showing of the collection, a majority of them will be manufactured in the four months immediately following the showing.

The company's finance director is a qualified accountant with a staff of six persons. Because of the seasonal nature of the business, the company prepares its detailed budgets and cash flow forecasts until the end of the next season. The company's year-end is 30th June and the directors expect to approve the financial statements during October. Detailed cash flow forecasts are only available up to the end of February in the following year, i.e., a period of only four months from the approval of the financial statements.

The company which has been marginally profitable over the last few years has a small line of credit with its bank but is financed primarily through the factoring of its debtors.

Assessment by the auditor

When the auditor assesses whether the directors have, in assessing going concern, paid particular attention to a period of one year from the date of the financial statements the auditor would:

(a) Review the cash flow forecasts for the four-month period from the date of the financial statements; and

(b) Then enquire of the directors the steps they have taken to assess the appropriateness of the going concern basis for the subsequent eight-month period.

The directors inform the auditor that they do not consider there is any need for additional cash flow forecasts to be prepared beyond the end of February in the following year because:

- The cash flow forecasts show a net cash inflow for the period and the present cash position is strong because of a recent sale of debtors from the present collection;
- The directors have reviewed in detail the assumptions implicit in the forecast and concur with them;
- The designers are working on the next collection and they believe, based on discussions with some of the retailers, that they have some good general ideas which will appeal to their customers if translated into imaginative detailed designs;
- Discussions with the major retailers indicate that they expect demand to be high next season;
- The company's relationship with its factor is good and they do not expect any difficulties in selling their debtors in the future;
- The company anticipates no major capital expenditures in the next twelve months. Most of the machinery is less than five years old and in any event is financed by lease arrangements rather than by purchase; and
- The company has recently renewed its arrangements with its bankers for a further year.

The auditor concludes that the directors have paid particular attention to the period ending one year after their approval of the financial statements.

The two examples above illustrate that the auditor may conclude that the directors have paid particular attention to the period ending one year after the approval of the financial statements, even though they have not prepared cash flow forecasts for that period.

The auditor may conclude differently in other situations that the directors have not paid particular attention to the period ending one year after the approval of the financial statements. If this is the case, the auditor needs to consider the impact on the auditor's report which may be either:

(a) The auditor may conclude that there is a significant level of concern about the entity's ability to continue as a going concern (but the auditor does not disagree with the use of the going concern basis). In which case the directors include a note to the financial statements and the auditor includes a section on "Material Uncertainty related to Going Concern (in accordance with paragraph 22 of SA 570(Revised); or

(b) The auditor may conclude that the directors have not paid particular attention to the period ending one year from the date of approval of the financial statements but there is no significant level of concern. Then if the directors:

    (i) Refer to the period paid particular attention to, in the annual report, the auditor need not refer to the period in the basis of opinion; however

    (ii) If the directors do not refer to the period paid particular attention to, the auditor would do so in the auditors' report in accordance with paragraph 24 and A35 of SA 570 (Revised); or

(c) The auditor may conclude that the directors have not taken adequate steps to satisfy themselves that it is appropriate to adopt the going concern basis of accounting. Accordingly, there is a limitation of scope which gives rise to a qualified or adverse opinion in the auditor's report in accordance with paragraph A32 of SA 570 (Revised).

Example 3 - A big company in manufacturing industry, at start up stage with certain facilities in project stage

Corollary from the auditor's risk assessment (Read with paragraph 10-11 of SA 570 Revised)

This company is a subsidiary of a multinational group and has two manufacturing plants, located at different places. The company employing around 3,000 people in both the units directly on its payroll and further deployed around 10,000 people through various contractors. The employment of the people considered to be in equal proportion among the two units. One unit (Unit A) of the company manufactures product which is a raw material for the other unit (Unit B).

The company has made huge investments for establishing facilities at both the units running in thousands of million dollars. For Unit A, the company is facing lot of hurdles and construction of facilities at the unit had to stop due to various related statutory and environmental clearances from certain authorities. However, the construction work at Unit B is completed and it is in running condition post trial run based on purchased raw material from other sources from domestic and international market, since there are uncertainty for the start of construction work at Unit A in next six months and further expects to get the production from Unit A within twelve month from the date of start of construction work. The company is hopeful that within the next six months, all the pending statutory and environmental clearance would be obtained for smooth operation. Until then and till the commencement of production at Unit A, the management expects that Unit B would continue its operation in this manner based on procured raw materials though it is costlier than the in-house production of raw materials.

Assessment by the auditor

When the auditor evaluates whether the management have, in assessing going concern, paid particular attention to a period of one year from the date of the financial statements the auditor:

(a) Reviewed the cash flow forecasts for the twelve-month period from the period end date for the financial statements; and

(b) Then enquired the management the steps it has taken to assess the appropriateness of the going concern basis for the subsequent periods.

The management informed the auditor that they do not consider there is any need for additional cash flow forecasts to be prepared beyond the end of twelve-month period from the period end date for the financial statements for current year because of:

- The cash flow forecasts that show a net cash inflow for the period and the present cash position is strong because of a recent sale of debtors.
- Sanction of large long-term loans from the lead banker with repayment terms starting in next 3-4 years.
- Infusion of long-term loans from certain group company with repayment terms starting in next 3-4 years.
- Conversion of payment for creditors into long term buyer's credit facilities from the banks with option to rollover for maximum period available as per banking rules (e.g., three years from the date of shipment).
- Sanction of bill discounting limit with the bankers for the sale contracts.
- Various long-term sale contracts in place.

Based on the above facts, there may not be a *prima facie* going concern issue.

However, based on the audit evidence obtained, the auditor may conclude there may still be significant uncertainties in execution of the management's plan. In such scenarios, the auditor may conclude that the management has taken adequate steps to satisfy itself that it is appropriate to adopt the going concern basis of accounting and may feel it appropriate to include a detailed note in the financial statements. Further, the auditor should include a separate section on "Material Uncertainty related to Going Concern" in the audit report in accordance with SA 570(Revised)

Example 4 –A company in sugar industry

There are several aspects which differentiate Sugar Industry from any other normal manufacturing industry. Some of the peculiar aspects are as follows:

- Cyclicality in the business.
- Government control on sugarcane procurement and several stringent regulations on pricing of sugar and sugarcane.
- Manufacturing process.
- Sales pattern. (mostly unorganized despite huge consumption)

Corollary from the auditor's risk assessment (Read with paragraph 10-11 of SA 570 Revised)

The most peculiar aspect of sugar industry is its being seasonal in nature and cyclical variations. The sugar industry goes through a period of loss (when excess sugarcane is produced) and profit (when there is shortage of sugarcane). Such cycle can be understood with the following table.

<u>Sugar Industry – profit and loss making cycle</u>

<table>
<tr><td>Increased sugarcane produced</td><td></td><td rowspan="9">Period of losses</td></tr>
<tr><td>Increase in sugar recovery</td><td></td></tr>
<tr><td>Higher sugar production</td><td></td></tr>
<tr><td>Increased availability of the sugar in retail markets</td><td></td></tr>
<tr><td>Decline in sugar price</td><td></td></tr>
<tr><td>Reduced profitability</td><td></td></tr>
<tr><td>Delayed payment to farmers</td><td></td></tr>
<tr><td>High sugarcane arrears</td><td></td></tr>
<tr><td>Low area under cultivation</td><td></td></tr>
</table>

Low sugarcane produced		Period of profits
Decline in sugar recovery		
Low sugar production		
Increase in retail sugar prices		
Improved profitability		
Prompt payment to growers		
Increased cash availability with growers		
Increase in area under cultivation		

The cycle time normally ranges from 4 to 5 years. To reduce the effect of this cycle, now-a-days most of the new units are set-up with a cogeneration of power and distillery unit, so that they can be profitable even when the sugar unit is making loss.

Thus considering these peculiar aspects, it is important that any auditor conducting audit of a sugar industry should clearly understand the details of these processes so as to be able to conduct effective audit and to obtain sufficient appropriate audit evidence regarding compliance with the provisions of applicable laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements. Also, to perform specified audit procedures to help identify instances of non-compliance with other laws and regulations that may have a significant impact on the functioning of the entity and conclusion drawn on their judgment for using the going concern basis of accounting in the auditor's report. Refer **Annexure–I** of this Implementation Guide for the format of various types of audit reports that may be used based on facts as applicable to the specific situation.

Annexure - I

An Illustrative Template for the Format of Auditor's Report under Different Scenarios as Illustrated in this Implementation Guide

Part A: An example of such wording for Section on "Material Uncertainty related to Going Concern" in the auditor's report is given below:

We draw attention to Note X of the financial statements which indicates that the Company's net worth has got eroded as of March 31, 20XX and the Company's current liabilities exceeded its current assets. These conditions, along with other matters as stated in said note, indicate that a material uncertainty exists that may cast significant doubt on the Company's ability to continue as a going concern. Our report is not modified in respect of this matter.

Reporting under section 143(3)(h)

The matter described under material uncertainty related to Going Concern paragraph may have an adverse effect on the functioning of the Company.

Other reporting requirements under section 143(3) of the Companies Act, 2013 have not been included.

Part B: An example of such wording for paragraph that may be included in a qualified or adverse opinion, as appropriate in the auditor's report:

(i) Qualified opinion

An example of such wording for paragraph that may be included on qualified opinion in the auditor's report for **'Disagreement on Required Disclosures relating to Going Concern** is given below:

Qualified Opinion

We have audited the accompanying Financial Statements of XYZ Limited ("the Company"), which comprise the Balance Sheet as at

March 31, 20XX, the Statement of Profit and Loss for the year ended on that date, and the Statement of Cash Flows for the year ended on that date, and a summary of the significant accounting policies and other explanatory information (hereinafter referred to as "financial statements").

In our opinion and to the best of our information and according to the explanations given to us except for ***inadequate disclosure of 'Material Uncertainty Related to Going Concern' referred to in the "Basis for Qualified Opinion" section of this report,*** the aforesaid financial statements give a true and fair view in conformity with Accounting Standards prescribed under section 133 of the Companies Act, 2013('the Act') and other accounting principles generally accepted in India, of the state of affairs of the Company as at March 31, 20XX, the profit/ loss for the year ended on that date and its cash flows for the year ended on that date.

Basis for Qualified Opinion

The Company's financing arrangements expired and the amount outstanding to the tune of Rs……was payable on March 31, 20XX. The Company has been unable to re-negotiate or obtain replacement financing and is considering filing an application under Insolvency and Bankruptcy Code 2016. These events indicate a material uncertainty that may cast significant doubt on the Company's ability to continue as a going concern, and therefore it may be unable to realize its assets and discharge its liabilities in the normal course of business. The financial statements (and notes thereto) do not disclose this fact.

Reporting under section 143(3)(h)

The matter described under basis for qualified opinion paragraph may have an adverse effect on the functioning of the Company.

Other reporting requirements under section 143(3) of the Companies Act, 2013 have not been included.

Adverse opinion- Example 1

An example of such wording for paragraph that may be included on adverse opinion in the auditor's report for **'Incomplete**

Assessment and Disagreement on Required Disclosures relating to Going Concern' is given below:

Adverse Opinion

We have audited the accompanying Financial Statements of XYZ Limited ("the Company"), which comprise the Balance Sheet as at March 31, 20XX, the Statement of Profit and Loss for the year ended on that date, and the Statement of Cash Flows for the year ended on that date, and a summary of the significant accounting policies and other explanatory information (hereinafter referred to as "financial statements").

In our opinion and to the best of our information and according to the explanations given to us due to ***incomplete assessment and disclosure of 'Material Uncertainty Related to Going Concern' referred to in the "Basis for Adverse Opinion" section of this report,*** the aforesaid financial statements do not give a true and fair view in conformity with Accounting Standards prescribed under section 133 of the Companies Act, 2013('the Act') and other accounting principles generally accepted in India, of the state of affairs of the Company as at March 31, 2019, the profit/ loss for the year ended on that date and its cash flows for the year ended on that date.

Basis for Adverse Opinion

The Company's financing arrangements expired and the amount outstanding to the tune of Rs. ……was payable on March 31, 20XX. The Company has been unable to re-negotiate or obtain replacement financing and is considering filing an application under Insolvency and Bankruptcy Code 2016. These events indicate a significant doubt on the Company's ability to continue as a going concern, and therefore it may be unable to realize its assets and discharge its liabilities in the normal course of business. The financial statements (and notes thereto) do not disclose this fact. Despite significant uncertainty as described above, these financial statements have been prepared on going concern basis of accounting.

Reporting under Section 143(3)(h)

The matter described under basis for adverse opinion paragraph may have an adverse effect on the functioning of the Company.

Other reporting requirements under Section 143(3) of the Companies Act, 2013 have not been included.

Adverse opinion- Example 2

An example of such wording for paragraph that may be included on adverse opinion in the auditor's report **where auditor has concluded that the entity is not a going concern** is given below:

Adverse Opinion

We have audited the accompanying Financial Statements of XYZ Limited ("the Company"), which comprise the Balance Sheet as at March 31, 20XX, the Statement of Profit and Loss for the year ended on that date, and the Statement of Cash Flows for the year ended on that date, and a summary of the significant accounting policies and other explanatory information (hereinafter referred to as "financial statements").

In our opinion and to the best of our information and according to the explanations given to us these financial statements have been ***prepared on going concern basis of accounting even though the company is no longer a going concern as described in the "Basis for Adverse Opinion" section of this report, and accordingly*** the aforesaid financial statements do not give a true and fair view in conformity with Accounting Standards prescribed under Section 133 of the Companies Act, 2013('the Act') and other accounting principles generally accepted in India, of the state of affairs of the Company as at March 31, 2019, the profit/ loss for the year ended on that date and its cash flows for the year ended on that date.

Basis for Adverse Opinion

The Company is in the business of real estate which is currently undergoing a recession due to significant dip in demand and liquidity crisis in economy. The Company is facing cash flow problems and has significant unsold semi-finished and finished inventory in its books of accounts. The company does not have any concrete future orders in hand and the management does not have realistic future plans. These events indicate a significant doubt on the Company's ability to continue as a going concern, and therefore it may be unable to realize its assets and discharge its liabilities in the normal course of business. The financial statements (and notes thereto) do not disclose this fact. Despite significant uncertainty as described above, these financial statements have been prepared on going concern basis of accounting.

Reporting under section 143(3)(h)

The matter described under basis for adverse opinion paragraph may have an adverse effect on the functioning of the Company.

Other reporting requirements under section 143(3) of the Companies Act, 2013 have not been included.

Annexure - II

Illustrative Format of Support Letter is given below:

On the Letter-head of the Parent Company (XYZ Limited)

Date: March 31, 20XX

M/s ABC Limited

Address: XXXX, India

Dear Sirs,

Sub: Letter of Support for financial assistance to M/s ABC Limited for ongoing projects and operations

We, XYZ Limited ('the Parent Company') confirm that we will provide financial support to M/s ABC Limited ('the Company') in order to meet the shortfall in its fund requirements over banks and other borrowings to meet out the projects which are in progress and other liabilities including loans from other group companies (if any), for a period of not less than 12 months from the date of financial closure of accounts of the Company for the year ended March 31, 20XX.

This letter is being issued at the request of M/s ABC Limited in respect of support for considering it as a going concern for the financial year ended March 31, 20XX.

Thanking you,

Yours truly,

Authorized Signatory