

May 31, 2007

Mr. James Sylph
 Technical Director, IAASB
 International Federation of Accountants
 545 Fifth Avenue, 14th Floor
 New York, NY 10017

Re: Exposure Draft: *Proposed Redrafted International Standard on Auditing (ISA) 570 (Redrafted), Going Concern.*

Dear Mr. Sylph:

The American Institute of Certified Public Accountants (AICPA) is pleased to comment on the above referenced exposure draft. We commend the International Auditing and Assurance Standards Board (IAASB) on its proposed revisions to International Standard on Auditing (ISA) 570, which clarify the auditor's responsibilities with respect to management's use of the going concern assumption in the preparation and presentation of financial statements. Although we support the issuance of redrafted ISA 570, we note that the auditing guidance in the exposure draft is predicated on International Accounting Standard (IAS) 1, *Presentation of Financial Statements*, which requires management to assess the entity's ability to continue as a going concern. Because a parallel accounting requirement does not exist in U.S. generally accepted accounting principles, the proposed standard is not entirely suitable for audits conducted under U.S. generally accepted accounting principles. Since the IAASB is only requesting comments on changes to ISA 570 resulting from applying the clarity drafting conventions and their effect on the content of the ISA, our comments do not reflect issues related to that difference.

Responses to Questions for Respondents

Q1. *Are the objectives to be achieved by the auditor, stated in the proposed redrafted ISA, appropriate?*

We believe that the objectives as stated in paragraph 9 are appropriate when viewed in conjunction with an accounting framework requiring management to assess the entity's ability to continue as a going concern. (Footnote 2 of the explanatory memorandum in the ISA 570 exposure draft identifies such a framework.)

Q2. *Have the criteria identified by the IAASB for determining whether a requirement should be specified been applied appropriately and consistently, such that the resulting requirements promote consistency in performance and the use of professional judgment by auditors?²*

² The IAASB has identified the following criteria for determining the requirements of a Standard:

- The requirement is necessary to achieve the objective stated in the Standard;
- The requirement is expected to be applicable in virtually all engagements to which the Standard is relevant; and
- The objective stated in the Standard is unlikely to have been met by the requirements of other Standards.

In determining the requirements of a Standard, the IAASB will consider whether the requirements are proportionate to the importance of the subject matter of the Standard in relation to the overall objective of the engagement. The criteria, which are intended only to assist the IAASB in appropriately and consistently determining requirements, may be refined as further experience is gained.

We believe that the criteria for determining whether a requirement should be specified have been applied appropriately and consistently.

The following are recommended changes to the ISA related to substantive issues, and an appendix containing other recommendations.

Recommended Changes Related to Substantive Issues

1. The phrase “may cast significant doubt upon the entity’s ability to continue as a going concern” is used in IAS 1 in the discussion of going-concern disclosure requirements. We recommend that the word “may” be deleted from the phrase “may cast significant doubt on the entity’s ability to continue as a going concern” in the exposure draft when the auditor has already concluded that substantial doubt exists, for example, in paragraphs 17 through 20. The phrase “cast significant doubt” connotes an uncertain condition; the addition of the word “may” unnecessarily dilutes the concept if the auditor has already concluded that substantial doubt exists.

2. We recommend moving paragraph 5 to the section of the exposure draft entitled “Evaluating Management’s Assessment” in the application and other explanatory material section of the ISA because we believe that the paragraph provides application guidance to the auditor. Also, to clarify the guidance and improve the follow-up to the lead-in of the paragraph, we recommend the following changes to paragraph 5:

5. 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 the future outcome of events or conditions which are inherently uncertain. The following factors are relevant to that judgment:

- The degree of uncertainty associated with the outcome of an event or condition. **Uncertainty** increases significantly the further into the future a judgment is being made about the outcome of an event or condition. 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 **manner and** degree to which ~~it~~ **the entity** is affected by external factors ~~all affect the judgment regarding the outcome of events or conditions.~~, **for example, economic conditions and changes in laws and regulations.**
- ~~Any judgment about the future is based on~~ **The** information available at the time at which the judgment is made. Subsequent events may be inconsistent with a judgment which was reasonable at the time it was made.

3. To clarify paragraph 16a, and because we believe that requiring the auditor to evaluate the reliability of a forecasting system goes beyond the objective of an audit of financial statements, we recommend the following changes to the exposure draft:

16. When events or conditions have been identified which may cast significant doubt on the entity’s ability to continue as a going concern, the auditor shall:

- (a) Obtain sufficient appropriate audit evidence to determine whether or not a material uncertainty exists through performing additional audit procedures, including consideration of ~~other~~ mitigating factors. When ~~analysis of~~ **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, the auditor shall:
 - (i) ~~Evaluate~~ **Assess** the reliability of the ~~entity's information system for generating such information~~ **underlying data generated to prepare the forecast**; and
 - (ii) Determine whether ~~there is adequate support for the~~ assumptions underlying the forecast **are reasonable, and that there is adequate support for the assumptions.**

In addition we noted that paragraphs 29a and 29b of extant ISA 570 identify four procedures, all of which are considered guidance. In the exposure draft, the first two procedures have been elevated to requirements, and the last two procedures are now included in paragraph A20 as optional procedures. We recommend that the last two procedures, which are currently in paragraph A20, be added to paragraph 16a and elevated to requirements, as follows:

(iii) Compare the prospective financial information for recent prior periods, if available, with historical results

(iv) Compare the prospective financial information for the current period with results achieved to date

4. We recommend the following revisions to the first sentence in paragraph 20 to reflect practice, and to the second sentence of the paragraph because we believe the report should identify the event or condition:

20. If adequate disclosure is not made in the financial statements, the auditor shall **request that management revise the financial statements to include the proper disclosure. If management refuses to do so, the auditor shall** express a qualified or adverse opinion, as appropriate (See ISA 705 (Revised), "Modifications to the Opinion in the Independent Auditor's Report"). The auditor shall ~~include specific reference~~ **state** in the auditor's report ~~to the fact that there is a material uncertainty that may cast~~ **s** significant doubt about the entity's ability to continue as a going concern **and shall describe the condition or event giving rise to the material uncertainty.**

5. We recommend that an example of the circumstance described in the last sentence of paragraph 22 be provided because we question why an auditor would be comfortable in a situation in which management had not performed any analysis.

22. If management is unwilling to make or extend its assessment when requested to do so by the auditor, the auditor shall consider whether there is a need to modify the opinion in the auditor's report as a result of the auditor's inability to obtain sufficient appropriate audit evidence. It is not the auditor's responsibility to rectify the lack of analysis by management. In some circumstances, however, the lack of analysis by management may not preclude the auditor from being satisfied about the entity's ability to continue as a going concern.

6. Because small entities are not necessarily able to respond quickly to exploit opportunities, we recommend the following change to paragraph A1:

A1. The size of an entity affects its ability to withstand adverse conditions. Small entities ~~can~~ **may be able to** respond quickly to exploit opportunities, but may lack reserves to sustain operations.

7. We recommend deleting the word “debtors” from the third bullet in paragraph A4 because debtors do not provide financial support

A4. The following are examples of events or conditions that, individually or collectively, may cast significant doubt about the going concern assumption. This listing is not all-inclusive nor does the existence of one or more of the items always signify that a material uncertainty exists.

- Indications of withdrawal of financial support by ~~debtors and other~~ creditors.

8. We recommend the following changes to paragraphs A14 and A15 (a) because the guidance is also applicable to larger, less complex entities, and (b) to more fairly portray practice in smaller entities and in larger, less complex entities:

A14. ~~The~~ **In many cases, the** management of smaller entities is less likely to **may not** have **prepared** a detailed analysis of its assessment of the entity’s ability to continue as a going concern. ~~In some cases, management may not have prepared a detailed assessment,~~ but instead **may** rely on in-depth knowledge of the business and anticipated future prospects. Nevertheless, in accordance with the requirements of this ISA the auditor needs to be satisfied as to the entity’s ability to continue as a going concern. Discussion with, and inquiry of, management in particular, of the financing of the entity in the medium and long-term may be appropriate in a small entity environment, provided that management’s contentions can be corroborated by sufficient documentary evidence and are not inconsistent with the auditor’s understanding of the entity. Therefore, the requirement in paragraph 13 for the auditor to request management to extend its assessment may, for example, be satisfied by discussion, inquiry and inspection of supporting documentation, e.g., orders received for future supply, evaluated as to their feasibility or otherwise substantiated.

A15. Where a smaller entity is largely financed by a loan from the owner-manager, it may be important that these funds are not withdrawn. For example, the continuance of a small entity in financial difficulty may be dependent on the owner-manager subordinating a loan to the entity in favor of banks or other creditors. In such circumstances the auditor may obtain appropriate documentary evidence of the subordination of the owner-manager’s loan. Where an entity is dependent on additional support from the owner-manager, the auditor may evaluate the owner-manager’s ability to meet the obligation under the support arrangement. In addition, the auditor may ask for a specific written representation confirming the owner-manager’s intention or understanding. **The auditor’s considerations related to smaller entities, discussed in this paragraph and in paragraph A14, also may be applicable to entities that are larger though not very complex, and are therefore analogous to smaller entities.**

9. We recommend that (a) paragraph A-15 be revised to require the auditor to obtain a specific written representation from the owner-manager confirming his or her intention and understanding that his or her loan to the entity is subordinate to loans made to the

entity by banks or other creditors and that (b) the substance of paragraph A-15 be moved to paragraph 16 as a sub item.

Thank you for the opportunity to comment on this exposure draft. If you have any questions regarding the comments in this letter, please contact Judith Sherinsky at +1-212-596-6031, jsherinsky@aicpa.org or Sharon Walker at +1-212-596-6026, swalker@aicpa.org.

Respectfully submitted,

A handwritten signature in cursive script that reads "Harold L. Monk, Jr.".

/s/ Harold Monk, Jr.
Chair, Auditing Standards Board

Appendix: Other Recommendations

1. To more accurately describe how assets and liabilities are recorded, we recommend the following change to the third sentence in paragraph 2 of the exposure draft:

.... When the use of the going concern assumption is appropriate, assets and liabilities are recorded ~~on the basis that~~ **at an amount that reflects the probability and extent to which** the entity will be able to realize its assets and discharge its liabilities in the normal course of business.

2. Because the words “could be” are too open ended, we recommend the following revision to paragraph 24:

24. When there is significant delay in the approval of the financial statements by management or those charged with governance after the balance sheet date, the auditor shall inquire as to the reasons for the delay. ~~When~~ **If the auditor believes or has determined that** the delay ~~could be~~ **is** related to events or conditions relating to the going concern assessment, the auditor shall perform those additional audit procedures necessary, as described in paragraph 17, as well as consider the effect on the auditor’s conclusion regarding the existence of a material uncertainty, as described in paragraph 18.

3. To clarify paragraph A2, we recommend the following editorial change:

A2. Conditions of particular relevance to small entities include the risk that banks and other lenders may cease to support the entity, **as well as** the ~~possibility of the possible~~ loss of a principal supplier, major customer ~~or~~, key employee, ~~and the possible loss of the~~; **or** right to operate under a license, franchise, or other legal agreement.

4. To clarify the 17th bullet in paragraph A4, we recommend the following revisions:

- Pending legal or regulatory proceedings against the entity that may, if successful, result in claims that ~~are~~ **the entity is** unlikely to be ~~satisfied~~ **able to satisfy**.

5. To more closely reflect the requirement in paragraph 10, we recommend the following revision to paragraph A5

A5. Paragraph 10 requires the auditor to ~~evaluate~~ **consider whether there are** events ~~and~~ **or** conditions ~~relating to the~~ **that may cast significant doubt on the entity’s ability to continue as a** going concern ~~assumption~~ when performing risk assessment procedures. This allows for more timely discussions with management, including a discussion of management’s plans and resolution of any identified going concern issues.