Going concern at completion

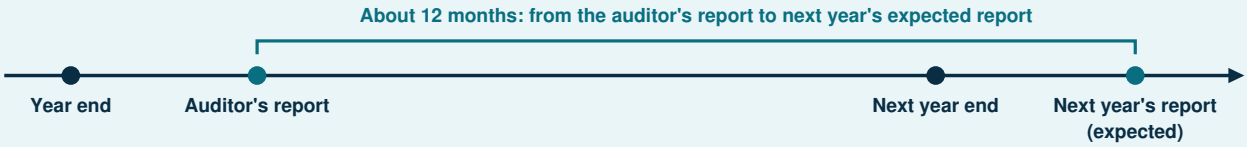
MODULE 4 | 4.1.2 | STUDENT COMPANION

When events or conditions raise significant doubt about whether the entity can keep going, the auditor must do more work to decide whether a **material uncertainty** exists: evaluate management's assessment and its **plans**, test the **cash flow forecast**, look for new facts and obtain **written representations**. Every mitigating plan needs its own evidence, and support from others needs evidence of both the supporter's **intention and ability**. At Voltana, a signed refinancing offer, a forecast that survives a downside and covenants still met lead to a conclusion of no material uncertainty.

When doubt exists: the extra procedures

1. **Ask for an assessment** — If management hasn't assessed going concern yet, ask it to
2. **Evaluate the plans** — Is the outcome likely to improve the situation? Are the plans feasible?
3. **Test the forecast** — Where it's central: reliable data? Assumptions adequately supported?
4. **Look for new facts** — Has anything emerged since management made its assessment?
5. **Get written representations** — From management, about its plans and their feasibility

How far ahead the auditor looks in Australia



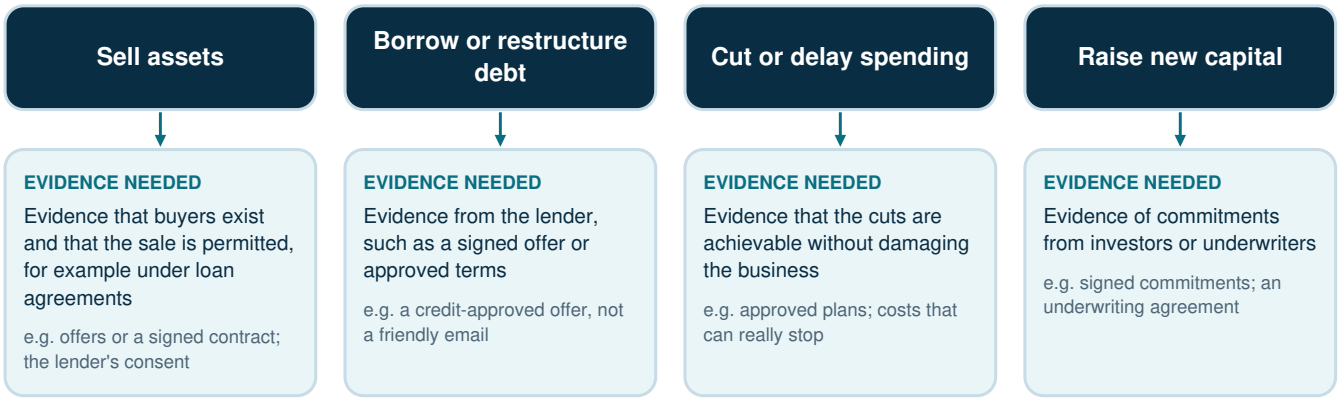
So it reaches past the end of the next financial year (ASA 570, Aus 13.2). Revised ASA 570, for periods beginning on or after 15 December 2026: at least 12 months after the financial report is approved.

How far ahead each party looks

Who	The period
Management (accounting standards)	At least twelve months from the end of the reporting period, taking into account all available information about the future
Auditor: current ASA 570 (Aus 13.2)	About twelve months: from this year's report date to the expected date of next year's report, so past the end of the next financial year
Auditor: revised ASA 570	For periods beginning on or after 15 December 2026: at least twelve months after the financial report is approved; if management's assessment is shorter, the auditor asks it to extend it

The forecast. Where a cash flow forecast is central, the auditor tests the data behind it (is it from a reliable system? how accurate were past forecasts?) and challenges each assumption against what the auditor knows about the business. The most useful questions are about **sensitivity**: which assumption, if it failed, would leave the entity short of cash, and what would a reasonable downside look like?

Every mitigating plan needs its own evidence



Plans that rely only on management's confidence aren't evidence at all.

Letters of support: four questions

A smaller company may rely on its owners not to demand repayment of their loans; a subsidiary may rely on its parent. A letter of support helps only if the auditor is satisfied about both the supporter's intention and its ability to provide the support.

Question	Why it matters
Is it legally binding, or only a statement of present intention?	An intention can change tomorrow; a binding commitment can be enforced
How long does it last?	Support that can be withdrawn at any time gives little comfort
Does it cover the whole assessment period?	Support that ends early leaves a gap exactly when it may be needed
Can the supporter afford it?	Examine the supporter's own financial statements, cash and other commitments: a promise is only as strong as the person or company behind it

Case note: Probuild (from Module 2). The lesson returns to Probuild for one point: support is only as good as the supporter's willingness and capacity to keep giving it. Past support proves nothing about the future.

Source: Wilson Bayly Holmes-Ovcon announcement (23 February 2022).

Testing Voltana's forecast and finance

Item	What the team did	Result
Sales growth of 10%	Compared with actual sales for July and August	About 7% above last year: below the 10% assumed, so the downside case matters
Gross margin back to 32%	Ran a downside case with no margin recovery (and no growth)	Still enough cash to operate until the facility matures
About $15m released by selling older models	Checked against prices achieved after year end	Assumption checked against real sales
Refinancing of the $60m facility (due 1 August 2027)	Obtained the bank's letter directly and confirmed its terms	Signed, credit-approved offer to extend to 2029; standard conditions already met
Interest cover covenant	Recalculated after the Module 3 corrections	EBIT about $13.2m: about 3.8 times, above the minimum of 3

Voltana: the going concern conclusion

A binding refinancing offer

- The $60m facility matures on 1 August 2027, inside the assessment period
- August: the bank's signed, credit-approved offer to extend it to 2029; standard conditions already met
- Obtained directly from the bank; terms confirmed

A forecast that survives a downside

- Assumes 10% sales growth, gross margin back to 32%, about $15m released from older stock
- July-August sales about 7% above last year; stock prices after year end checked
- Downside (no growth, no margin recovery): still enough cash until maturity

Covenants still met

- EBIT about $13.2m after the Module 3 corrections
- Interest cover about 3.8 times, against the bank's minimum of 3

→

Conclusion

The going concern basis is appropriate, and no material uncertainty exists

Change one fact
one letter different

Suppose the bank had issued only an **indicative term sheet**: willing to discuss an extension, but no commitment. The refinancing stays uncertain and the facility falls due inside the assessment period, so a **material uncertainty** is likely: clear disclosure in the statements, plus its own section in the auditor's report.

Two other outcomes. If the going concern basis isn't appropriate at all, for example because the directors intend to liquidate, statements prepared on the going concern basis are materially misstated and the auditor expresses an **adverse opinion**. If management won't make or extend its assessment when asked, the auditor considers what that means for the evidence and the opinion: the scope of the audit may be limited. The Exam Reference Pack (page 6) maps every going concern outcome.

Practice questions

MODULE 4 | 4.1.2 | TRY THESE BEFORE THE WORKED ANSWERS

Question 1 - Four plans at Keelhaven Boats

Keelhaven Boats Pty Ltd (imagined) builds aluminium fishing boats and small ferries. After two years of losses, its $2m overdraft is due for review in March 2027. To show it can keep going, the directors put forward four plans. Evaluate each plan and say what evidence it needs.

The directors' plan	Evidence you would need, and your view of the plan
(a) Sell the vacant waterfront yard beside the factory for about $3m. The bank holds a mortgage over it.	
(b) Convert the $2m overdraft into a five-year term loan. The bank's relationship manager has said in an email that he is 'supportive'.	
(c) Cut 15 production jobs from October and delay building a new paint shop.	
(d) Raise $4m by issuing new shares to the founding family and a private investor.	

Question 2 - Two letters of support

Keelhaven's auditor expects to sign the report in September 2026. Judge each letter.

The letter	How much comfort does it give, and why?
Letter A, from Brinkhaven Holdings Pty Ltd (imagined), which owns 60% of Keelhaven: a deed approved by Brinkhaven's board, promising whatever funds Keelhaven needs to pay its debts as they fall due until 31 October 2027, and not to call in its own $2m loan before then. Its latest audited statements show net assets of $40m and cash of $6m.	
Letter B, from Keelhaven's founding managing director, who owns the other 40% and has lent the company $1.5m: 'I currently intend to keep supporting the company and have no plans to call in my loan.' It has no end date, and most of his wealth is his shares in Keelhaven.	

Question 3 - Keelhaven's cash flow forecast

Identify the three most sensitive assumptions in the forecast below, and give a procedure to test each one.

Item (year to 30 June 2027)	$m	Key assumption
Receipts from boat sales	14.4	160 boats at an average $90,000 (last year: 130 boats at $88,000)
Ferry contract progress payments	2.5	A contract with a regional council, expected to be signed in October
Proceeds from selling the vacant yard	3.0	Sold by December at the agent's appraised value
Payments for materials	(8.6)	Aluminium prices 10% lower than this year
Wages and overheads	(9.8)	15 jobs cut from October
Interest and loan repayments	(1.1)	Overdraft renewed in March 2027
Net cash flow for the year	0.4	Opening overdraft $1.5m; limit $2.0m

Worked answers

MODULE 4 | 4.1.2 | WORKED ANSWERS - ATTEMPT THE QUESTIONS FIRST

Question 1 - Keelhaven's four plans (suggested)

Watch for plans that contradict each other: cutting 15 production jobs sits awkwardly with a forecast that needs 23% more boats.

Plan	Evidence needed, and comment
(a) Sell the yard	An agent's appraisal and, better, written offers or a signed contract; the bank's consent, because it holds a mortgage and may take the proceeds to reduce the debt; the timing of settlement; confirmation that the yard isn't needed for production
(b) Convert the overdraft	A friendly email isn't a commitment. Look for a signed, credit-approved offer or approved new terms, with any conditions and covenants, before the March 2027 review
(c) Cut jobs, delay the paint shop	A board-approved plan, the redundancy costs (cash goes out first), and whether the remaining staff can still build the boats the forecast assumes; whether the paint shop contract can be delayed without penalty
(d) Issue shares	Signed, unconditional commitments from the investors, evidence they can pay (for example bank statements), the timetable, and any shareholder approvals needed

Question 2 - The two letters (suggested)

	Comfort	Why
A	Substantial, once verified	Legally binding, approved by Brinkhaven's board, and it runs to 31 October 2027, beyond the twelve months after a September 2026 report. Brinkhaven appears able to pay: confirm the board minute, read its audited statements and recent cash position, and check that the deed can't be withdrawn
B	Little	Only a statement of present intention, not binding, with no end date; his ability is doubtful because his wealth depends on Keelhaven itself. At most it supports the other evidence

Question 3 - The most sensitive assumptions (suggested)

Closing overdraft = $1.5m - $0.4m = $1.1m, only $0.9m inside the $2.0m limit, so losing any of these three would breach it:

- **The yard sale ($3.0m by December):** obtain the agent's appraisal, any offers or a signed contract, the settlement date and the bank's consent; check whether the bank will take the proceeds.
- **The ferry contract ($2.5m, not yet signed):** read the council's tender documents and correspondence, ask for the signed contract and payment schedule, and check Keelhaven can deliver on time.
- **Boat sales of 160 (23% more than last year):** compare with the order book, deposits taken and dealers' orders; compare July to September actual sales with the forecast; check how accurate past forecasts were. Every 10 boats is about $0.9m.

Also check the overdraft renewal itself (evidence from the bank) and the aluminium price assumption (supplier quotes), and ask management for a downside case combining the risks.