How to prepare your assessment of Going Concern

Contents

June 2023

SAYER | VINCENT

What is going concern?

In order to approve a set of statutory accounts, trustees and directors are required to confirm that it is appropriate to prepare the accounts on the basis of going concern. You have to consider appropriate information to form your opinion as to whether the organisation will have sufficient funds to continue in operation meeting liabilities as they fall due for at least the 12 months from the date the accounts are approved.

Requirements for auditors

As your auditors, we need to give a specific opinion on whether or not the organisation is a going concern within our audit report that is published as part of your financial statements.

We shall request from management their assessment of the going concern basis. Management could mean trustees, directors or the senior executive team depending on the size and structure of the organisation.

Auditors are also required to stand back and consider all the evidence obtained during the course of the audit before concluding. This will need to be carried out in the final stages of the audit and will cover whether management's assessment of the going concern basis is appropriate and whether a material uncertainty related to going concern exists. Therefore, even though the majority of the audit process will be complete, please do expect additional queries from the audit team at this stage as this part of the process needs to be formally documented.

What information do you need to provide for your auditor?

In order to help us, as your auditor, consider your assessment of going concern, please provide:

- Management accounts to date
- A budget or forecast from the date of the management accounts and for a period of at least 12 months from the approval date
- A cash flow forecast covering the same period
- The supporting narrative that details the assumptions you have used in the preparation of the above – this is considered further below

- When requested by your auditor, evidence on a sample basis to support any key assumptions such as documentation to support the confirmation of agreed future funding, or confirmation of key liabilities such as pension or lease commitments.

Explain your process and provide evidence

It will also be helpful for us to understand the process you have used to assess going concern. So, who has prepared the information, how and when has it been reviewed, were any significant changes made and are there any minutes available documenting any discussions held.

Scenario planning

Where there are uncertainties about significant amounts of income (as is often the case) you should include different scenarios to show the effect if not all planned income is received and what you are able to change in expenditure in these circumstances, **for example**:

- Plan A – budget or forecast as above
- Plan B – if fundraised income is 33% [vary income stream or percentage as appropriate] lower than in Plan A – what adjustments would be made to expenditure
- Plan C – if fundraised income is 66% [vary income stream or percentage as appropriate] lower than in Plan A – what adjustments would be made to expenditure

Similarly, you may also have expenditure that fluctuates significantly as a result of factors outside of your control, as we have seen recently with inflation, energy costs, and the impact of increased interest rates on borrowings. Within your worst-case scenario, it may also be necessary to increase your expenditure and test the impact of this on your cash and reserves position.

If your organisation can continue even in a worst-case scenario then you can conclude there are no material uncertainties affecting going concern.

What assumptions might you need to make?

The most important element of any budget or forecast is the **narrative explanation** supporting it so that it is clear how the numbers have been put together.

When you are assessing going concern, you will need to consider external factors and key events. Risks to viability that may impact on your assumptions may include:

Financial risks:

- Overall financial sustainability due to the risk of a global economic downturn
- The impact of inflationary pressures such as on the cost base of the organisation, or on the ability to fundraise as cost of living pressures impact on household incomes
- Loss of or delay in receiving funding as significant events may need to be cancelled
- Potential for reduced funding, particularly from individual giving due to the impact of the cost of living crisis on personal budgets
- Pressures on working capital if there are delays in paying invoices or processing funding applications
- Significant pressures on your cost base due to the impact of inflation, and rising energy costs and/or interest rates
- Operational closures due to workforce shortages
- Significant decreases in asset values, including listed investments
- The availability of sources of finance linked to performance covenants

Non-financial risks:

- Reliance on a major donor whose support may not continue in the future
- Disputes between the trustees and/or the senior management team
- High turnover or long term absences within the trustee board or senior team
- Lack of engagement in the business or financial strategy of the organisation
- Reputational risks related to the quality of services you are providing
- Any other risks that you may have identified within your risk register that could impact on the continued operations of the organisation

For registered charities, you will need to reflect the impact of the above within the trustees' annual report in the section on principal risks and uncertainties and in relation to future plans.

Solvency and liquidity – what are your financial strategies?

Where you have significant pressures on cash flow or on financing more medium term capital projects or repaying significant liabilities, you may have already started thinking about your financial strategies. These should be explained within your assessment, and may include:

- Meetings you have held with your funders to discuss future commitments, funding increases or perhaps the timing of the agreed payment plan
- Agreed strategies you may have in place around paying your suppliers
- Any engagement you have had with your bank to discuss facilities that might be available, or the renewal of any existing facilities

- Whether or not your consider your investment portfolio to be part of working capital, and whether any planned draw downs of capital will be made
- Whether you plan to sell any assets in support of working capital (and whether there are any restrictions or other legal requirements that may need to be considered)
- Any plans you have to put borrowing or other financial facilities in place, and what security may be required against them

The Financial Reporting Council has general guidance on going concern and reporting on solvency and liquidity risks. This includes going concern factors, guidance on the assessment process and the associated reporting requirement. The guidance is intended to serve as a proportionate and practical guide for non-listed entities, and can be found at: www.frc.org.uk/Our-Work/Publications/Accounting-and-Reporting-Policy/Guidance-on-the-Going-Concern-Basis-of-Accounting.pdf.

Are there any material uncertainties?

Management and the trustees/directors will need to assess the financial and operating outlook and identify any material uncertainties that impact on the organisation's ability to continue operating.

A material uncertainty is something that may cast 'significant doubt' on the organisation's ability to continue operating, examples of these might be a:

- breach of bank covenant or risk over future support
- significant funding stream renewal or re-tender
- continued operational / unrestricted deficits
- onerous loan financing
- Charity Commission or other regulatory investigation

You will need to assess which of the following applies to your organisation:

1. Going concern basis is appropriate and there are no material uncertainties
2. Going concern basis is appropriate but there are material uncertainties
3. Going concern basis is not appropriate as you anticipate you will have to cease operating within twelve months

For options 1 and 2, you should explain why this is the case in the financial statements (in the accounting policy section) and in the trustees'/directors' report. In a trustees' report, we would expect this will impact the risk section and the future plans and may also impact the achievements for the year.

For option 2, if the uncertainties are severe, you may wish to delay signing the accounts until you have more certainty.

For option 3, the audit shouldn't be a priority. You may need professional advice to help you keep afloat or explain what you should and should not do in an insolvency situation, or to help you prepare management information and cash flow forecasts, but the historic financial information is less critical. Please let us know if you are in this situation and we can help you get the right support.

What if the going concern basis is not appropriate?

In certain cases, an entity will not be a going concern, such as when it is planned to be liquidated or its activities are transferring within a group structure. In this case, a different basis of accounting will need to be adopted and you should have a separate conversation with your audit partner or manager about this.

What might be more critical is when you carry out your assessment and as a result consider that your organisation might not be able to continue on a going concern basis. The Charity Commission offers guidance through its publication CC12 (Managing a charity's finances) which can be accessed via the link below:
https://www.gov.uk/guidance/financial-difficulties-in-charities

Please also do contact us so that we can discuss your assessment and support you to consider next steps.

Checklist to help you prepare your assessment

Actions to complete in respect of our going concern assessment	Complete
Communicate to the board of trustee the concept of going concern and the commitment that is being made when the accounts are approved	☐
Document an agreed process for how going concern is going to be reviewed and who will be responsible for preparing the initial report	☐
Prepare an initial draft paper setting out your assessment.	☐
Confirm that the paper includes documentation of:	
• what information you have used to prepare the report	☐
• an explanation of the scenario planning you have considered	☐
• an explanation of any assumptions used in your assessment	☐
• details of any financial strategies in place or you are planning to undertake	☐
• details of any material uncertainties you have identified	☐
• your overall conclusion on going concern	☐
• your proposed disclosure for the trustees' annual report for approval	☐
Submit the paper to your audit committee for recommendation, or to the board for approval as appropriate (on a timely basis, and before the accounts are planned for approval)	☐
Submit the paper to your auditor for review and comment	☐
Provide any supporting evidence to your auditor as requested	☐
Confirm that the trustees' annual report has been updated for the agreed disclosure	☐
Approve the specific representation within the Letter of Representation on going concern	☐

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