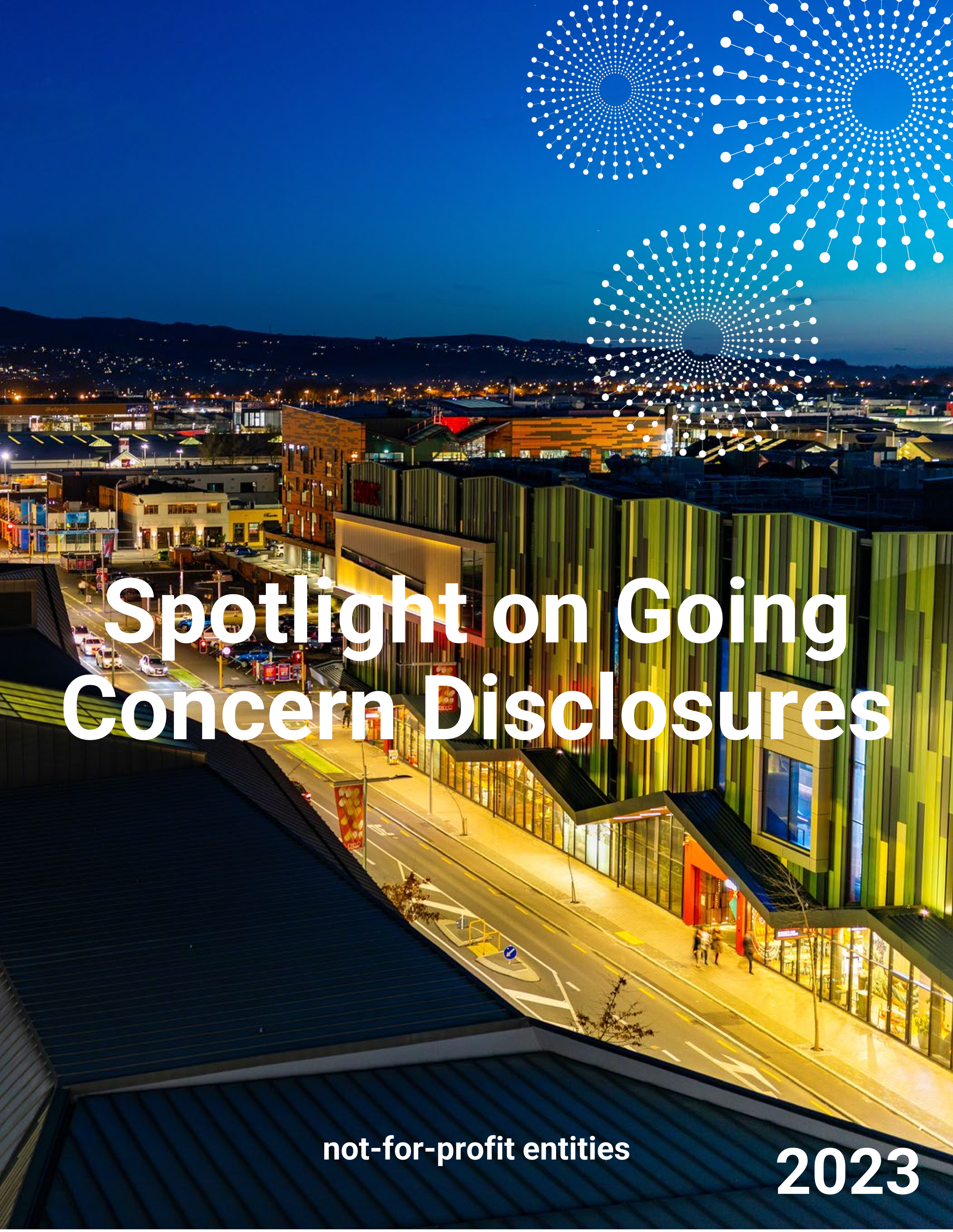


Spotlight on Going Concern Disclosures

not-for-profit entities

2023

Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

Contents

This is relevant for any not-for-profit entity that prepares financial statements in accordance with Tier 1, Tier 2 or Tier 3 PBE Standards as issued by the XRB. Tier 4 reporting entities use cash accounting and therefore are not required to consider going concern. However, there may be instances where disclosure of information about events occurring after the financial year is needed.

Disclaimer

Introduction

Economies globally and in Aotearoa New Zealand are facing multiple challenges that are expected to lead to slower growth. Like many sectors, the NFP sector is under pressure from the uncertainty and challenges on the economy and wider New Zealand society.

As a result, the financial and operating stability of many NFP entities is currently under increased stress due to:

- pressure on securing future revenue inflows from funders and public donations;
- rising demand for services due to increased economic hardship; and
- pressure on the availability of staff, including access to volunteers.

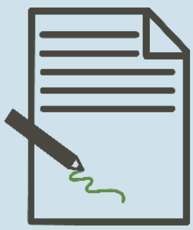
In this environment, those charged with the governance of NFP entities have a responsibility to explain to the readers of the financial statements when there are uncertainties about the entity's intention and ability to continue operating for the foreseeable future.

What do those charged with governance need to know?

All governing bodies need to be involved in assessing the entity's ability to continue as a going concern, whether it is appropriate for the entity's financial statements to be prepared using the going concern assumption and the adequacy of the related financial statement disclosures.

Going concern disclosures are a key area of interest to funders and individual donors who are looking for transparent and meaningful information to help them assess the NFP entity's operational and financial stability, including its ability to continue operating as a going concern.

Disclosures should not only be provided on whether an entity continues to be treated as a going concern, but also information about how that view was reached – including any significant judgements and/or material uncertainties considered as part of this assessment.



What accounting standards apply?

The relevant accounting standard requiring disclosures on going concern for Tier 1 and Tier 2 entities is PBE IPSAS 1 Presentation of Financial Statements. More specific requirements were added in August 2020 in response to the COVID-19 pandemic which resulted in significant disruption and uncertainties for many entities and led to an increased interest in going concern disclosures. These requirements continue to be relevant now, and in the future, to assist preparers to provide relevant and transparent information to resource providers and other users of financial reports.

For Tier 3 entities the requirements are contained in the Tier 3 Standard.

Overview of going concern

An entity is considered a going concern for financial statement preparation purposes unless those charged with governance of the entity either:

- intend to liquidate the entity or to cease operating; or
- there is no realistic alternative but to do so.

Financial statements are normally prepared on what is described as a 'going concern basis' that is, the entity expects to continue operating and meeting all of its obligations for the foreseeable future. In these circumstances the normal rules of accounting apply.

The need for a NFP entity to change how it operates or change the nature of its activities in response to the economic environment does not necessarily mean the entity is no longer a going concern – the assessment is primarily based on the governing body's consideration of the intention and ability to continue operating in the future.

Deciding if an entity is a going concern

Those responsible for the preparation of the financial statements take into account **all available information about the future** when deciding if the going concern assumption is appropriate.

This is at least, but not limited to, 12 months from the balance date of the financial statements.

This will involve looking at a wide range of factors, such as the current and expected performance of the entity, stability of expected revenue inflows, any external obligations such as borrowing, and access to other sources of funding.

There is no set formula or process for assessing whether the going concern basis of preparation remains appropriate, rather judgement is required based on all the information available at the time of this assessment. In periods of increased uncertainty, it is particularly important to document the basis and evidence for conclusions reached by those charged with governance.

What if an entity is not a going concern?

When a decision is made to liquidate an entity or to cease operating, or the entity has no realistic alternative but to do so, the financial statements should no longer be prepared on a going concern basis. In these circumstances, professional accounting and legal advice should be sought to confirm the entity's financial reporting obligations.

In these circumstances, the financial statements are prepared under an alternative basis of preparation, which should reflect the entity's particular circumstances, such as whether the entity's operations are to be transferred to another entity, sold or liquidated.

What do Tier 1 and 2 entities need to disclose?

The nature and extent of going concern related disclosures will depend on each entity's facts and circumstances. However, in general, it is expected that the going concern assessment will result in one of four possible outcomes. As outlined in Diagram 1 below, each of these outcomes results in different disclosure requirement considerations.

Diagram 1: Overview of going concern related disclosures

Going concern assessment outcome		Going concern disclosures
Have there been any events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern?	No	No specific going concern disclosures required, unless material to users
Yes		
Is there a material uncertainty regarding the entity's ability to continue as a going concern?	No	Information about **significant judgements and assumptions**
Yes		
Is the entity intending to liquidate, or cease operating or does it have no other realistic alternative but to do so?	No	Information about **events or conditions** giving rise to material uncertainties Information about how **management plan** to mitigate the effects of any material uncertainties Information about how assets and liabilities **may not be realised/discharged** in the normal course of business
Yes		
Going concern basis for financial statement preparation no longer appropriate.		Information that the going concern basis was not used, alternative basis of preparation, reason why the entity is not regarded as a going concern

When those responsible for the preparation of the financial statements have applied significant judgement in reaching the decision that an entity is a going concern, the auditor is required to consider whether the financial statements provide adequate disclosures about how these decisions were reached.

What do Tier 3 entities need to disclose?

If the entity plans to stop operating within 12 months from balance date or it is likely it will be unable to continue operating, the entity includes in the notes to the performance report:

A statement that the entity intends to stop operating or that it is unlikely the entity will be able to continue operating;

The reason why the entity intends to stop operating or why it may not be able to continue operating;

The estimated effect of the entity's circumstances on the amounts of the entity's assets and liabilities.

The impact of any changes will depend upon the particular circumstances of the entity.

- The impact on the recorded amounts of assets will depend upon whether operations are to be transferred to another entity, sold, or liquidated.
- Judgement is required in determining whether a change in the carrying amount of assets and liabilities is required.
- It is also necessary to consider whether the change in circumstances leads to additional liabilities or triggers clauses in debt contracts which will lead to the reclassification of those debts as current liabilities.

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