



## ADDING VALUE THROUGH THE PLUS FACTOR

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## Going Concern: Directors Responsibilities!

While economic indicators suggest that we may have seen the worst of the recession, we are still in difficult economic times and the impact of the recession is still being felt in many areas.

Annual accounts can convey a positive message for some, but for others, accounts and the disclosures within them, paint a very different picture. Deterioration in trading and cash flow can often lead to working capital deficiencies and unhealthy balance sheet ratios.

### In these circumstances, what are directors' responsibilities?

Very clear guidance is available on this, both from accounting standards and a recent publication from the Financial Reporting Council:

- Directors are required to make and, importantly, document a rigorous going concern assessment of their company when preparing annual accounts. In making this assessment, the review should cover a period of at least 12 months from the approval date of the accounts.
- If going concern is an issue, directors must give balanced, proportionate and clear disclosures regarding going concern to ensure that the accounts give a true and fair view.

### What does this mean for you in reality?

There is always uncertainty in business, but the real issue is whether uncertainties regarding going concern are so fundamental that they require to be disclosed.

For example, in a business with long term contracts, a history of profitability, cash generation and sufficient banking facilities, there would likely be little uncertainty. But, what if a major contract expires in a few months' time and the banking facilities are due for renewal a few months later?

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ACCOUNTING  
OUTSOURCING

9 QUEENS ROAD  
ABERDEEN  
AB15 4YL

TEL: 01224 625111

FAX: 01224 626007

email: [accountants@aab.co.uk](mailto:accountants@aab.co.uk)

web: [www.aab.co.uk](http://www.aab.co.uk)

Generally, where such uncertainties exist, directors should be demanding and reviewing projections based on different scenarios to highlight whether there is a potential problem.

Although hopes and expectations may be that contracts will be renewed, it is essential to consider the implications if they are not:

- What opportunities are there to replace lost business?
- How quickly can the business respond?
- What are the implications for staff?
- What ongoing requirements are there for premises and equipment?

Many companies also have banking covenants which are subject to regular review. Companies with good management information systems generally have up to date financial information and budgets for the year ahead, but these need to be tested against differing scenarios so that the board and management have an early warning of potential issues.

With the changes in availability and pricing of credit over the recent past and immediate future, good information is a prerequisite for discussions with lenders regarding financial requirements.

### **What about directors of small companies - do the requirements apply to them?**

Of course, the extent of the review and work involved depends on the size and complexity of the business. However, the requirements do apply to ALL, regardless of size.

An early discussion with your accountants or auditors will help to establish the nature of the review, evidence required and possible outcomes in terms of disclosure.

This may prompt a discussion with lenders on the renewal of facilities. Indeed, the guidance from the Financial Reporting Council states that directors should seek confirmation from lenders over principal terms and conditions where there is a degree of uncertainty.

These discussions may also highlight the best time to sign the accounts, subject to lenders' requirements and filing deadlines. For example, it may be more appropriate to finalise accounts when facilities have been renewed or an asset sold to provide access to new funds. Such events could be disclosed in the accounts, sending a positive message to readers and also protecting directors from making either inadequate disclosures, or disclosing uncertainties which have been successfully addressed before the accounts were signed.

### **In conclusion, there are three key questions to be asked:**

1. Are you concerned about the implications of assessing going concern for your business?
2. Are you engaging in discussions with your advisors and lenders at the right time?
3. Is appropriate and reliable information available to optimise such discussions?

In any event, action and timing thereof is critical. If you have not thought about these things already, it is never too early to start and you should expect your contact at Anderson Anderson & Brown LLP to be bringing up this issue sooner rather than later.



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web: [www.aab.co.uk](http://www.aab.co.uk)