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GOING CONCERN – KEY AUDITOR CONSIDERATIONS

ABSTRACT

The principle going concern is a fundamental assumption in the preparation and presentation of financial statements. It is a sensitive assessment in audit arrangement that, in the case of an auditor's mistake, can leave multiple negative consequences for the business of the audited entity and its stakeholders, but also for entire accounting profession, and because of that, auditors with caution to access this issue i.e. its emphasis in the audit opinion. There are many factors that affect the auditor's assessment of the assumption of going concern of the audited entity, and in the first row are the items and indicators from the financial statements as a general tool for assessing the financial health of the company. The aim of this paper is to research the positions and indicators of financial statements that auditors can use for the going concern assessment of business entities in Bosnia and Herzegovina, given the lack of research of this nature. On a sample of 148 audit reports for 2020 and 2021, the influence of the total assets, financial result of the period, liquidity coefficients, debt and current ratio, as well as the two-year trend of indicators on the auditor's assessment of the going concern of the audited entity were tested. The research showed that a negative business result, a higher debt ratio, a lower liquidity ratio, a lower current ratio and a decline in 3 of the 4 listed indicators increase the probability of emphasizing the issue of going concern in the audit report.

Keywords: *going concern, financial statements, auditor's reports, financial positions, financial indicators.*

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1. INTRODUCTORY CONSIDERATIONS

The basic assumption for preparation financial statements is going concern or continuity of operations. The importance of this assumption is based on the expectations of interested parties who make decisions about investment, granting loans and other types of cooperation that the company will continue to operate for the foreseeable future and provide for them the return on investment. Therefore, it is expected that management publishes through the financial reports all necessary information, not only about the financial state, success and other standard financial elements, but also about the estimated and expected business continuity. In the audit report, along with an assessment of whether the financial statements are truthfully and fairly presented, the second key point is the assessment of the going concern for the audited entity, too.

The long-term survival of the company was gained additional importance due to the failure of several previously powerful companies at the beginning of the 21st century, especially during the great economic crisis, whose audit opinion was not previously modified due to the assumption of going concern, which put this problem in increased focus, opening the question of how to improve the accuracy of auditors in such judgments and reduce the probability of errors.

Considering the sensitivity of the evidence procedure and the weight of the auditors' decision in respect of expressing an opinion about the going concern, factors and their influence on the judgment related to this issue have been dealt in numerous studies, as well as the techniques and procedures used. At the level of Bosnia and Herzegovina (BiH), there were not more researches that dealing with this topic, and so that there is an open area for analyse data from financial and audit reports and the tendencies of local auditors in diverting the public's attention to the going concern issue of BiH companies. Accordingly, the following research objectives were set:

- to determine the frequency of opinion modification due to going concern or emphasising that issue without modification of opinion in audit reports in BiH, and
- to determine financial indicators with the highest correlation related to the probability of emphasising the going concern issue in audit reports, based on a sample of companies from the Sarajevo Stock Exchange.

2. REVIEW OF RELEVANT LITERATURE

In the Conceptual framework for financial reporting (p.4.1), it is stated that financial statements are prepared under the assumption that the company will continue to operate in the foreseeable future, and that if the entity has the intention or need to liquidate or significantly reduce the scope of its operations, financial statements should be prepared on a different basis and it should be published. International

Accounting Standard (IAS) 1 – Presentation of financial statements elaborates the concept of going concern in the same way (p.25). International Standard on Auditing (ISA) 570 – Going concern deals with this problem in the most detail, explaining the concept, roles of management and auditors, as well as audit procedures and techniques in the going concern assessment process.

According to ISA 570 (p.15), the auditor has obligation to evaluate the appropriateness of management's assessment regarding going concern for the same period for which the assessment was made, in accordance with the Conceptual Framework and legal regulations. Audit assessment of the entity's business continuity, as well as the review of the set of financial statements, was conditioned by limitations due to which there is no guarantee that the assessment was done appropriate, and therefore, the auditing standards also emphasize the concept of reasonable assurance. There are numerous factors that influence on this assessment, among which the following stand out: financial strength and financial result of the audited entity. A recapitulation of the most famous models for going concern assessment created from 1930 to 2007 (about 180 of them) show that the two most used financial indicators are: the return on assets and the current ratio (Gissel, Giacomino and Akers, 2007). According to the study by Gallizo and Saladrigues (2016), the focus of this research will be on the following indicators:

- Return on Assets (ROA) - $\text{profit} / \text{total assets}$. (this indicator is mostly negative for companies with a modified opinion due to going concern),
- Debt ratio - $\text{short-term liabilities} / \text{long-term liabilities}$ (the higher indicator, generally, means the greater the probability of changing the opinion due to going concern),
- Current ratio - $\text{short-term assets} / \text{short-term liabilities}$ (it is expected that companies with a modified opinion due to going concern have a negative value of this indicator), and
- Liquidity ratio - $\text{cash} / \text{short-term liabilities}$ (the lower this ratio means, in general, the higher probability of obtaining a modified audit opinion due to going concern).

Additionally, the financial result as the most notable parameter of the income statement and the volume of assets as a key indicator of the balance sheet, although they can be observed together with other financial indicators, they deserve special attention (Carson et al., 2013). The reason is that they most explicitly indicate financial and business difficulties, especially if they extend over several consecutive periods.

ISA 520 – Analytical procedures require from auditors to use analytical procedures in the planning and completion phases of the audit, while in the phase of gathering evidence, the using of analytical procedures is recommended. Research conducted in the Republic of Croatia (Zenzerović, 2007) showed that the share of auditing companies that use analytical procedures for the assessment of going concern is greater than 75%, and that the share of audit firms that issued a modified opinion, as a result of the non-existence and/or inadequate disclosure of the going concern assumption, is greater than 50%. According to research conducted in the USA (Louwers, 1998), auditors direct the most focus on financial indicators and other indicators of financial difficulties. Research from Belgium indicated that larger audit firms were more precise in the going concern assessment (Hardies, Vandenhoute and Breesch, 2018). Researches in Indonesia (Farhana and Rahmawaty, 2020, Hakiki and Mappanyukki, 2022) showed that the greatest importance for the audit assessment of going concern had the financial difficulties measured by Altman's Z-score model, but the independence of the audit committee and the size of the audited company, too.

However, the going concern questioning, especially without a strong foundation in such an assessment, it can be disastrous for the auditor in case of an error, but also for the company itself in the case, and it is the so-called "self-fulfilling prophecy" (Susilawati, 2019) or situations in which the auditor's opinion threatens the viability of the company. Because of that, the researchers express their doubts about the auditor's practice of refraining from pointing out the problems of going concern companies. Research showed that in the first year of the pandemic, contrary to common expectations, the % of modified audit opinions regarding the issue of going concern reached in the USA a twenty-year minimum, below 20% (Audit Analytics, 2022), only to rise again in the next two pandemic years and reaching almost 30% in 2022 (Audit Analytics, 2023).

3. RESEARCH METHODOLOGY

The answers to research questions and hypothesis testing were provided by quantitative analysis of financial and audit reports for 2020 and 2021 of non-financial companies listed on the Sarajevo Stock Exchange with a capitalization more than 1,000,000 BAM. The criterion for forming the sample was chosen because these companies, due to their size, mostly belong to medium and large legal entities, which consequently are obliged to hire an external auditor, and at the same time it represents a sufficient sample of over a hundred companies. Financial companies were left out due to stricter supervision, as its result their going concern is rarely questioned, and additionally due to the fact that they have significantly different indicators in the financial statements.

The first group in sample was consisted of companies for which a modified audit opinion due to inappropriate application of the going concern assumption were issued, as well as companies for which a positive opinion with a note or emphasis on that issue were been issued. The second group in sample was represented by companies that in the observed two-year period hadn't audit opinion with apostrophized going concern issues. The computer program IBM SPSS Statistics was used for statistical processing of the collected data. More detailed information about the method of selecting the sample for the research were presented in Table 1.

Table 1. *Research sample*

Number	Sample classification	2020.	2021.
1	Initial sample (companies listed on the Sarajevo Stock Exchange with a capitalization more than 1,000,000 KM)	130	130
2	Financial companies	29	29
3	Companies without a published audit report	36	18
4 (1-2-3)	The final sample	65	83
5	Modified audit opinions	19	28
6	Modified audit opinions due to going concern	2	2
7	The emphasis of going concern issue without modification of opinions	12	17
8 (6+7)	The emphasising the going concern issue in the audit reports (regardless of whether the opinion has been modified or not)	14	19
9 (4+8)	Audit reports without emphasising the going concern issue	51	64

Source: *Author's calculation according to data from sase.ba*

Although 19 out of 65 in 2020, or 28 out of 83 companies in 2021 deserved a modified audit opinion, in only two companies, the assumption of going concern was cited as the reason for the modification: disclaimer of opinion. Considering this fact, the first group consists of companies whose going concern issue was emphasised in the form of a note, including the four companies with modified audit opinion, while the second group consists of companies that have not emphasised going concern issue in their audit opinion or in the form of a special note, regardless of opinion modification.

In addition to emphasising the issue of going concern in audit reports as a dependent variable, the following independent variables from financial reports were analysed through research: asset, financial result (profit, loss) and coefficients: ROA, indebtedness, liquidity and current ratio, as well as their relationship in 2021 compared to 2020. Namely, the trend of indicators plays an important role in the analysis of financial statements, so if they are unfavourable, and at the same time additionally worsened compared to the previous reporting period, it can be interpreted as sign of financial difficulties and endangered survival. The following hypotheses were tested:

H1. Companies from the Sarajevo Stock Exchange with a reported loss in the financial report of the current period have a higher probability of emphasising the going concern issue or modifying the audit opinion related to it.

H2. Companies from the Sarajevo Stock Exchange with a higher debt ratio have a higher probability of emphasising the going concern issue or to modifying the audit opinion related to it.

H3. Companies from the Sarajevo Stock Exchange with a lower current ratio have a higher probability of emphasising the going concern issue or to modifying the audit opinion related to it.

H4. Companies from the Sarajevo Stock Exchange with a lower liquidity ratio have a higher probability of emphasising the going concern issue or to modifying the audit opinion related to it.

H5. Companies from the Sarajevo Stock Exchange that recorded a decline in three of the four selected indicators (ROA, debt ratio, current ratio, liquidity ratio) have a higher probability of emphasizing the going concern issue or modifying the audit opinion related to it.

H6. Companies from the Sarajevo Stock Exchange with a lower asset value have a higher probability of emphasizing the going concern issue or to modify the audit opinion related to it.

4. RESEARCH RESULTS

The following tables summarize the obtained data, which are elaborated in more detail below.

Table 2. Statistical values of selected indicators

With/Without emphasis Going Concern issue (GC)		Asset value	Financial result	ROA	Debt ratio	Current ratio	Liquidit y ratio
2020	With emphasis GC (14)	915.633.092	13.687.689	1,49%	0,534	0,882	0,354
	Without emphasis GC (51)	8.296.347.052	113.356.685	1,37%	0,233	2,856	0,828
2021	With emphasis GC (19)	1.141.742.382	22.871.176	2,00%	0,507	1,096	0,282
	Without emphasis GC (64)	9.259.420.485	205.832.944	2,22%	0,237	2,064	0,615
Sum	With emphasis GC (33)	2.057.375.474	36.558.865	1,78%	0,519	1,001	0,314
	Without emphasis GC (115)	17.555.767.537	319.189.629	1,82%	0,235	2,369	0,697

Source: Author's calculation

Basic overview of the statistical values of the indicators for 2020 and 2021, as well as their summary values, shows that companies that had not been emphasised the

going concern issue had significantly higher asset values, as well as financial results and ROA, except ROA in 2020, and lower debt ratios and higher current and liquidity ratios, which is in line with the assumptions / hypotheses of the paper.

Pearson's correlation coefficient was used to test is there a correlation between individual independent variables and emphasising the going concern issue, either in the form of a special note or as a reason for modifying the audit report as a dependent variable. The results of the analysis were presented in table 3.

Table 3. *Correlation analysis*

Correlation of emphasising the going concern issue and observed variables			Pearson Chi-Square koeficijent
			Signifikantnost (0,05)
V1. Financial result	Profit	Loss	Accepted H1
With emphasis GC	63,6%	36,4%	4,73
Without emphasis GC	81,6%	18,4%	0,036
V2. Debt ratio	below the median	above the median	Accepted H2
With emphasis GC	33,3%	66,7%	4,72
Without emphasis GC	55,3%	44,7%	0,032
V3. Current ratio	above the median	below the median	Accepted H3
With emphasis GC	30,3%	69,7%	6,59
Without emphasis GC	55,7%	44,3%	0,017
V4. Liquidity ratio	above the median	below the median	Accepted H4
With emphasis GC	30,3%	69,7%	6,59
Without emphasis GC	55,7%	44,3%	0,017
V5. Drop of 3 out of 4 observed indicators by 25% or more	Drop of less than 3 indicators	Drop of 3 or more indicators	Accepted H5
With emphasis GC	73,7%	26,3%	6,1
Without emphasis GC	93,7%	6,3%	0,014
V6. Asset value	above the median	below the median	Rejected H5
With emphasis GC	39,4%	60,6%	1,91
Without emphasis GC	53,0%	47,0%	0,175

Source: *Author's calculation*

In 12 out of 33 cases with emphasis the going concern issue (36.4%), a negative financial result was recorded, while in only 18.4% of financial reports in which the

going concern issue were not emphasised, the loss of the reporting period was recorded. In conclusion regarding hypothesis 1, it was established that emphasising the going concern issue or modification of opinion on that basis is significantly more common in companies with a loss reported in the financial statement, i.e. H1 hypothesis was accepted.

66.7% of companies with emphasis the going concern issue in the observed years had a debt ratio above the median of the entire sample, while the majority of companies without an emphasis the going concern issue had a debt ratio lower than the median of the sample. A statistical test found that there is a significant difference between the two sets of companies within the sample and that it is significantly more likely that companies with a higher debt ratio will have a going concern issue emphasised in the audit report, as soon as hypothesis H2 was accepted.

69.7% of companies with emphasis the going concern issue (23 out of 33) recorded a current ratio below the median level of the entire set, while in the second sample group most companies had a current ratio above the median. A statistical test, with an error risk of less than 2%, found that a lower current ratio increases the chance of emphasising the issue of going concern in the audit report, resulting with the acceptance of hypothesis H3.

The relationship of emphasising the going concern issue and the liquidity ratio for the two groups within the observed sample is the same as for the current ratio. More than two-thirds of companies with apostrophe the going concern issue were grouped below the median according to the liquidity ratio, which with a reliability higher than 98% confirms the hypothesis H4. On the other hand, companies from the Sarajevo Stock Exchange that had a higher value of liquidity ratio were exposed to a lower risk that auditors call in question the continuity of their business.

Individual variables as indicators of the company's financial health may show a higher or lower correlation with the auditor's assessment of its long-term viability, but the assumption is that the deterioration of value in several of them should result in most cases in a weakening of the general condition and thus encourage auditors to question the sustainability of the business. The specific time context of the research - the period of the economic crisis caused by the pandemic - caused the deterioration of the indicators of numerous companies – one third of them recorded deterioration in three of four indicators, and more than half in at least two indicators. Therefore, considering the general trend of deterioration of the financial health of companies, a decline in three out of four indicators by at least 25% was determined as a criterion. More than a quarter of companies with emphasis the going concern issue recorded a decline of at least 25% in at least three indicators, against only 6% of companies that did not mention the above question. Pearson's correlation coefficient determines the acceptance of hypothesis H5.

Nevertheless, although the mean value of total assets by year and for the entire set supports the hypothesis H6, the statistical test does not provide a sufficient level of reliability to accept it. 60% of companies with an asset value below the median in the audit reports had the issue of going concern emphasised, while in the second group, the majority of companies recorded an asset value above the median. One of the key reasons why the hypothesis H6 was not accepted in the observed sample is the distribution of asset values within the two groups.

5. CONCLUSION AND RECOMMENDATIONS

Going concern, permanence or continuity of business is a basic accounting principle insisted by international accounting and auditing regulations and it is of great importance to users of financial reports who are interested in stability, existence and long-term sustainability of companies. External auditors have a key role in detecting and disclosing any material misstatements in financial statements, as well as those affecting the appropriateness of the going concern assumption and significant announcements regarding the same, and in their reports, apart from the accuracy and objectivity of the information presented and compliance with accounting standards and legal regulations, put an important emphasis exactly on this issue.

There are a handful of factors that influence to the final assessment of the adequacy of the going concern assumption, in the first place, these are indicators from financial reports as a tool for general judgment of the company's financial health and the basis on which the auditor substantiates his judgment expressed in the report. With this research, conditioned by the availability of information, part of the factors, predominantly of a financial nature and from financial reports, were processed. Based on the financial and audit reports of companies from the Sarajevo Stock Exchange, by using the Pearson correlation coefficient, asset values, financial result, ROA coefficients, debt, current and liquidity ratios were analysed. In the observed sample, it was determined that companies with recorded losses, lower liquidity and current ratios and higher debt ratio, have more likely for emplacing the going concern issue, which is in accordance with the set hypotheses, as well as the fact that emphasising the going concern issue is more likely in companies that record a decline in at least three of the four observed financial indicators. Contrary to the hypothesis, it was not established that the observed companies from the Sarajevo Stock Exchange that have a lower value of assets are more likely to have the going concern issue raised.

Although this study provides significant insight and deep understanding of the concept of going concern in the light of audit engagement, it is important to emphasize that there are also certain limitations of the research. Namely, the research was based on a sample of 148 companies in the territory of FBiH for the period 2020-2021. This means that it is possible that the results were influenced by the area and

time frame in which the research was done, and it is possible that the results would be different if some external factors were changed. An additional limitation of the research may be the focus on financial positions and indicators. Although financial statements are considered the most reliable picture of a company's operations, they alone cannot fully capture all the complexities of the business. Therefore, it is recommended to include in the future research non-financial variables that may indicate potential problems in the company.

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NEOGRANIČENOST POSLOVANJA – KLJUČNA REVIZIJSKA RAZMATRANJA

Sažetak

Načelo vremenske neograničenosti poslovanja temeljna je pretpostavka pri izradi i prezentaciji finansijskih izvještaja. Riječ je o osjetljivoj ocjeni u revizijskom angažmanu koja u slučaju revizorove greške može ostaviti višestruke negativne posljedice na poslovanje revidiranog subjekta i njegovih stakeholdera, ali i na cjelokupnu računovodstvenu profesiju, zbog čega revizori s oprezom pristupaju ovom pitanju tj. njegovom isticanju u revizorskom mišljenju. Mnogo je faktora koji utiču na revizorovu ocjenu pretpostavke vremenske neograničenosti poslovanja revidiranog subjekta, a u prvom redu to su veličine i pokazatelji iz finansijskih izvještaja kao općeg alata za procjenu finansijskog zdravlja kompanije. Cilj predmetnog rada je istražiti pozicije i pokazatelje finansijskih izvještaja koje revizori mogu koristiti prilikom ocjene neograničenosti poslovanja privrednih subjekata u Bosni i Hercegovini, s obzirom na nedostatak istraživanja ove prirode. Na uzorku od 148 revizorska izvještaja za 2020. i 2021. godinu, testiran je uticaj ukupne aktive, finansijskog rezultata perioda, koeficijenata likvidnosti, zaduženosti i tekućeg omjera, kao i dvogodišnjeg trenda kretanja pokazatelja na revizorovu ocjenu neograničenosti poslovanja revidiranog subjekta. Istraživanje je pokazalo da negativan poslovni rezultat, viši koeficijent zaduženosti, niži koeficijent likvidnosti, niži tekući omjer te pad u 3 od 4 navedena pokazatelja povećavaju vjerovatnost isticanja pitanja vremenske neograničenosti poslovanja u revizorskom izvještaju.

Ključne riječi: *neograničenost poslovanja, finansijski izvještaji, revizorski izvještaji, finansijske pozicije, finansijski pokazatelji.*

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