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LETTER OF COMMENT NO. 17

Mr. Russell G. Golden  
Director of Technical Application and Implementation Activities  
Financial Accounting Standards Board  
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Norwalk, CT 06856-5116

8 December 2008

**Proposed Statement of Financial Accounting Standards, *Going Concern*  
(File Reference No. 1650-100)**

Dear Mr. Golden:

We appreciate the opportunity to comment on the Proposed Statement of Financial Accounting Standards, *Going Concern* ("Proposed Statement"). We support the Board's initiative to provide, as part of the accounting literature, guidance on the preparation of financial statements as a going concern that would make explicit management's responsibility to evaluate a reporting entity's ability to continue as a going concern.

However, we have serious concerns regarding the FASB's proposed adoption of the IASB's time horizon for management's assessment of an entity's ability to continue as a going concern. The proposed timeframe is not the same as the guidance currently set forth in both the standards of the Public Company Accounting Oversight Board and the Auditing Standards Board of the American Institute of Certified Public Accountants, AU Section 341, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern* (AU Section 341). We believe that developing accounting guidance in this area that differs from existing auditing standards will result in unnecessary complexity in financial reporting and will not serve the interests of users of financial statements. We strongly encourage the FASB to retain the time horizon in AU Section 341 until such time as the FASB and the auditing standard setters can jointly consider the accounting and auditing standards in this fundamental area of financial reporting. In conjunction with such a project, we would continue to support the current time horizon in AU Section 341, as discussed further below.

The going concern assertion is one of the most fundamental assertions in financial reporting and, therefore, represents one of the most critical assertions considered by users of financial statements. We believe that it is imperative that management and auditors evaluate an entity's ability to continue as a going concern using the same guidelines. We do not believe that management, as preparers of financial statements, can effectively divorce its consideration of management's going concern assessment from the similar evaluation made by the auditor. Developing inconsistent standards in this area does not improve financial reporting. Rather, it creates unnecessary complexities in financial reporting by allowing for the possibility for management and auditors to reach different conclusions using the same information and judgments about the future.

In applying AU Section 341, the auditor must assess whether or not the audit report should include an explanatory paragraph expressing substantial doubt about the entity's ability to continue as a going concern. In developing AU Section 341, the Auditing Standards Board deliberately selected a finite time horizon over which the auditor would need to make such an evaluation due to the inherent difficulties in predicting future events. An auditor's report that is modified to express substantial doubt about an entity's ability to continue as a going concern can become a self-fulfilling prophecy. Lenders, suppliers, regulators, and customers frequently react to the circumstances giving rise to the auditor's conclusion by demanding repayment, withholding credit, imposing restrictions or conducting business elsewhere, thereby limiting the entity's ability to remain viable. For this reason, the auditor's conclusion with respect to an entity's ability to continue as a going concern is one of the most important judgments made during the course of the audit. Current events have demonstrated all too clearly the difficulty of making such determinations in rapidly changing markets.

While AU Section 341's evaluation time horizon of "not beyond one year" is a bright line, it is one that is well understood by preparers, auditors, and users. We believe the expansion of the time horizon in the FASB's exposure draft to a less precise view of the future that is "at least, but not limited to, 12 months" will present preparers and auditors with new challenges. One specific situation frequently encountered in practice relates to a borrower's need to obtain a waiver of a lender's rights to demand payment due to a debt covenant violation. In practice, that waiver tends to be for at least one year and one day from the balance sheet date in order for the entity to possibly be able to classify the obligation as noncurrent, as well as for the entity to demonstrate to the auditor the entity's ability to remain a going concern for the time horizon prescribed in AU Section 341. Under the guidance in the Proposed Statement, the entity would be potentially unable to obtain a waiver of sufficient length in time that would allow it and its auditors to conclude that there is not substantial doubt about its ability to continue as a going concern, thus potentially making it difficult to obtain liquidity from other sources in order to remain viable.

Consider also an entity with a large debt balloon payment due 14 months after its current balance sheet date. Without refinancing this debt, it could be forced to declare bankruptcy. Under the current auditing standards, it is possible that the auditor could conclude that a report modification is not required, but under the Proposed Statement, management may conclude that there is substantial doubt as to the entity's ability to continue as a going concern. Such a disconnect between the audit report, where users of financial statements are accustomed to seeing information about an entity's ability to continue as a going concern, and the notes to the financial statements does not serve the needs of users of the financial statements.

The current financial and economic environment has demonstrated the fundamental importance of liquidity, both in markets and for entities. We do not believe that it would be an improvement in financial reporting, or otherwise in the public interest, for the FASB to adopt a standard that would potentially contribute to limiting the availability of liquidity to entities in the current environment.

We also are obviously concerned with a potential increase in litigation resulting from the proposed time horizon. Challenges to the judgments reached by financial statement preparers and auditors regarding going concern issues are commonplace in financial reporting litigation today. Using classic "20/20 hindsight", when an entity fails after issuing financial statements on a going concern basis and receiving a "clean" audit opinion with respect to those financial statements, plaintiffs frequently

assert that the judgment of the financial statement preparers and their auditors "must have been flawed," as "proved" by subsequent events. It can reasonably be expected that such litigation would only increase in frequency were the time period being assessed extended, or were there a lack of consistency between the standards applied by the financial statement preparers and the auditors.

Finally, in contrast to the Board's view expressed in the Proposed Statement, we believe that the proposed time horizon represents a significant change in current practice and would create significant implementation issues for both management and auditors, as we have discussed throughout this letter. If the Board were to proceed with the change in the time horizon at this time, we do not believe that there would be an adequate amount of time between the issuance of a final standard and the expected effective date of the *FASB Accounting Standards Codification*<sup>TM</sup> on 1 July 2009 for constituents to address the expected implementation issues, especially in the current financial and economic environment. If the Board would like the proposed guidance to be effective upon ratification of the *FASB Accounting Standards Codification*<sup>TM</sup>, then we urge the Board to retain the time horizon in AU Section 341.

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We would be pleased to discuss our comments with the Board or its staff at your convenience.

Very truly yours,

*Ernst & Young LLP*