

Critical Review of the Going Concern Assumption in Light of Sustainability Debate

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Abstract:- This paper critically reviews the traditional accounting concept of the "going concern assumption" within the evolving context of the global sustainability debate. The going concern assumption, which presumes a business will continue to operate indefinitely, forms a fundamental basis for financial reporting. However, increasing awareness of environmental, social, and governance (ESG) factors, climate change impacts, resource depletion, and social inequalities challenges this long-held premise. This review explores how sustainability risks and opportunities, often long-term and systemic in nature, can significantly impact an entity's ability to continue as a going concern, potentially leading to material misstatements or inadequate disclosures in financial statements. We examine the limitations of current accounting standards in fully incorporating sustainability-related factors into going concern assessments and discuss the implications for financial statement users, auditors, and regulators. The paper proposes that a more robust integration of sustainability considerations is necessary for going concern assessments to remain relevant and reliable in an era of increasing environmental and social consciousness, suggesting potential avenues for enhancing reporting frameworks and auditing practices.

Keywords: potential, assessments, consciousness, enhancing

1. Introduction

The first sound that recognized the rapid grow of population and the future effect of this grow on resources was by Thomas Malthus in 1798, by introducing the theory of population. Long time period after Thomas essay, 33 countries officially approved the sustainability development in 1969. And the first official sound for sustainability concept was in 1987. In this regard Thomas theory focused on the need to equilibrium between resources and population. In 19th century, the concept developed to include the need for equilibrium between the environment, social and financial issues. In the economic field, enterprises consume resources to introduce their products and as a result get their profits. As long as sustainability concept developed, it becomes necessary for each enterprise to contribute maintain resources by take part of environment and human resources.

Lately, much research has been discussed what is known sustainability (Rounaghi, 2019; Uwuigbe, 2018; Shafi, 2020; Rahman and Kazmi, 2013). It defines sustainability as a concept contains three pillars: the environmental, social, and economic parts, and those parts are interconnected (Rounaghi, 2019). In the emerging markets almost, based on the researcher best of knowledge, all studies conducted to investigate the effect of sustainability on performance or business economic factors, with no testing of the reality of sustainability activities in emerging markets. If business reported or disclose around sustainability pillars for false leading, so, sustainability becomes a trademark that improves firm performance and monetary value of business only.

Rounaghi (2019) defines the environmental accounting as a wide area of accounting science provides reports for internal use to help managers take decisions about pricing, cost control, and capital budgeting, and its external function is to disclose environmental information for public and financial communities. The environmental factor is an important in this era due to the changes of environment and the effect of human and business behaviors on environment. Thus, it is important to be real actions taken by businesses to improve environment.

2. Literature Review

The going concern assumption, a fundamental principle in accounting, posits that an entity will continue its operations for the foreseeable future without the intention or necessity of liquidation. However, the sustainability debate has prompted a reevaluation of this assumption, urging stakeholders to consider long-term environmental, social, and economic impacts alongside traditional financial metrics. This literature review explores the critical dimensions of the going concern assumption in light of sustainability, focusing on recent studies that examine its implications for companies and investors.

The Going Concern Assumption: Definition and Importance The going concern assumption is essential for the preparation of financial statements, allowing for the deferral of expenses and the recognition of assets based on the premise of ongoing operations (International Financial Reporting Standards [IFRS], 2020). This concept enables firms to present a stable financial picture, which is crucial for maintaining investor confidence and securing financing (American Institute of CPAs [AICPA], 2019).

The Intersection of Sustainability and Going Concern Recent literature highlights the growing intersection between sustainability practices and the going concern assumption. According to Eccles et al. (2014), sustainable business practices can enhance corporate performance and, by extension, the reliability of financial statements grounded in the going concern assumption. Companies that integrate sustainability into their operations may mitigate risks associated with environmental regulations, social unrest, and market transformations, thus supporting their viability as going concerns (Porter & Kramer, 2011). For instance, the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) recommends that businesses disclose climate-related risks and opportunities, acknowledging that sustainability issues can significantly affect financial performance and investor decision-making (TCFD, 2017). This guidance points to a shifting paradigm where the going concern assumption must incorporate sustainability considerations, especially in industries susceptible to climate change impacts.

Critical Perspectives on Going Concern and Sustainability Despite the potential synergies between sustainability and the going concern assumption, critical perspectives emerge regarding their compatibility. Some scholars argue that current financial reporting frameworks inadequately capture the complexities of sustainability, leading to a distorted view of an entity's long-term viability (The Prince of Wales Accounting for Sustainability Project, 2019). For example, McPhail (2019) contends that traditional going concern assessments often overlook relevant non-financial factors, resulting in misinformation for stakeholders who seek to understand corporate sustainability efforts. Moreover, the reliance on historical data in assessing the going concern assumption may not effectively predict future sustainability challenges. As highlighted by Liu et al. (2020), firms that fail to adapt to a sustainable business model may face unforeseen liquidity crises, undermining the assumption of continuing operations.

Regulatory Perspectives and Future Directions Regulatory bodies are increasingly recognizing the importance of sustainability in assessing going concern. The IFRS Foundation is working towards integrating sustainability disclosure requirements into financial reporting standards to ensure a more holistic view of an entity's long-term viability (IFRS, 2021). This regulatory shift underscores the need for accountants and auditors to consider sustainability metrics systematically when evaluating a company's going concern status.

3. Sustainability as Long as with Capitalist and Communism Economies

The Last 100's year's prompt boisterous changes in the economic and accounting fields. In light of domination of capitalist economy on communism economy, the notion of resources limitation still activated. The highlights of resources limitation notion are based on who control resources, will control on economic decisions. Communism economy assumes that government has a full control on resources, in the same line capitalist transferred this control to individuals, and it becomes concentrated in hand of specific class of individuals (Chavance, 1999). Capitalist system and Communism system are two faces for the same coin, both of them are based on the control on resources(environment), information and human resources. In parallel Nash (1950, 1951) assumes that each player – in the economic application is the competitor – follow suitable strategy based on what is available for him to take the best decision and as a result the best result for him in his competition with other business, and he assumes that all resources are available for all competitors. Although, this theory is not applicable in light of capitalist economy. From the theoretical perspective, Nash equilibrium could be applicable, but in practice it is

not applicable in economic and business fields. For instant, diamond (or gold) has been controlled by some specific companies, and those companies keep diamond (or gold) in huge stores to control price. Also, a general common practical rule assumes that who knows more raise his wealth more and keep his private information without announcement. Thus, the accounting application of this practice is the accounting disclosures, which assumes that each competitor will give misleading information or omits substantial disclosures. Additionally, the revolution toward sustainability and environmental accounting between academics and the accounting institutions and bodies is delayed or it is not suitable now because it is a building on wrong foundation. This conclusion came from what everybody seen in the general practices of businesses around the world in light of capitalism, of controlling and destruction environment in the same line with controlling human resources in order to increase the wealth of the elite who have the huge businesses.

4. Going Concern Assumption

One of the most important assumptions in the accounting field is the going concern assumption. It assumes that the enterprise is continuing in the future to indefinite unless any symptoms of uncertainty appear, then enterprise should present its financial position based on other criteria (FASB, 2020). This indicates that if there are for example an expectation of insolvency, bankruptcy, or liquidation, the accountant will prepare the financial statements under a standard other than the international financial reporting standards (IFRS). The debates regarding going concern assumption have got wide concentration in the accounting literature, for example, Cormier et. al. (2000) developed a tool to evaluate going concern risk of an audit client specially after highly visible corporate failures. In the same orientation, Kuruppu et. al. (2003) discussed liquidation and bankruptcy prediction models for assessing going concern of the firm, they concluded that company liquidation model can be used as a valuable and accurate model by auditor in assessing going concern. One year later, Nogler (2004) went beyond testing the long-term effects of going concern opinion, he suggests that large firms are more likely subjects of acquisition while smaller go out of existence over time. Also, there is no long-term stigma-attached to having a going concern opinion between resolved going concern sample and matching sample in his research. Shirata & Sakagami (2008) discussed the difference between going-concern companies and non-going-concern companies by analyzing the nonfinancial information in the financial reports. The researchers concluded that nonfinancial key words in financial reports can be used to evaluate the financial position (going concern), so the researchers verified that it is possible to assess whether a company will continue or not based on qualitative data, without looking at financial numbers. Others examined the role of risk models used by auditors to judge going concern assumption of the firms. For instant, Young & Wang (2010) examined the appropriateness of auditor's judgment of going concern reporting using five-level risk class. They found that the level of under reporting of going concern risk by auditors implies they are more affected by the agency relationship than directors who are found to have incidence of underreporting of 57 percent.

As a background, going concern assumption should be reconsidered as a result of the case of uncertainty of the availability of the environmental resources and the global discussion about sustainability. Governments, companies, and institutions now are working together to find a solution of the resources scarcity and climate changes, which are threatens the business around the world, and as a result have impact at the macroeconomic level. This increased risk – specially in parallel with COVID-19 impact- plays important role on evaluating the ability of businesses to continue in the long term, which requires review the theoretical framework of accounting regarding the going concern assumption.

5. Conclusion

The intersection of the going concern assumption and the sustainability debate offers an evolving landscape for corporate reporting and assessment. While the traditional view of going concern remains valid, integrating sustainability considerations is imperative for a comprehensive evaluation of a company's future prospects. Future research should further explore the implications of sustainability on the going concern assumption, fostering a more informed understanding among stakeholders and enhancing the reliability of financial reporting.

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