



SECTION 2

THE IMPACT OF THE “GOING CONCERN” ON AUDITORS’
JUDGEMENT. ANALYSIS OF THE ITALIAN CONTEXT FROM
AN INTERNATIONAL PERSPECTIVE

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Abstract

The present work aims to analyse the concept of going concern on the one hand, through a case study of three companies which have recently come under observation of the CONSOB and have been inserted in the so-called “black list” and, on the other, the consequences that the removal of the presumption of continuity can have on the kind of assessment the auditors make. The aim of the present work is twofold: the first part analyses the principle of going concern from a business and economic perspective. Once this has been completed, the work will go on to offer an overview of the dynamics that can bring a company to a crisis point, and how these affect the judgments expressed by the auditors***.

Keywords: Going Concern, Continuity, Black List, Audit

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1 Introduction

The economic situation in Italy, being heavily influenced by the global financial crisis, threatens the ability of companies to maintain and consolidate their business activities over time. The fact of uncertainties, often nothing to do with the company itself, can cast doubt on the presumption of continuity. This context is a threat to a company’s future, and thus demands greater attention on the part of administrators and auditors, whose role it is to verify all the facts carefully, so as to be in a position to decide what criteria and procedures to adopt when drawing up the company accounts and expressing their professional judgement. All this falls within the current debate on the analysis of the “going concern”, reiterated in article 2423 of the Civil Code, the first item of which

states, “the evaluation of the accounts is to be carried out in line with the criterion of prudence, and with a view to the future prospects of the company concerned.” One can also find the same concept in international accounting regulations, in particular in the IAS (items 23 and 24).

If, after making a thorough assessment, the management of a company believes that a number of factors put at risk the company’s ability to continue operating, explicit reference to this must be included in the company balance sheets.

The drafting of a budget on the assumption of the company’s certain market future in a context in which such an assumption is untenable, implies considerable risks both for the administrators and for the organs of control, above all in the case of default. The person whose job it is to inspect the company accounts must

carry out certain procedures so as to be in a position to ascertain the correctness of the work of the administrators. In brief, the auditor must verify whether the conclusions reached by the administrators are valid and/or whether there are grounds to suspect that there are serious doubts as regards the company's future, which should be included in the company financial statements. For all aspects linked to the work of auditing we refer specifically to the auditing rule no. 570 "going concern".

At this point it is important to mention that in December 2014 the ISA Italia auditing rules were adopted, under the aegis of the Ministry of Finance; this was the result of a collaboration between a number of the professional associations and orders: ASSIREVI (Italian auditors), CNDCEC (National Council of Chartered Accountants), INRL (National Institute of Statutory Auditors) and CONSOB (Italian Securities and Exchange Commission) with reference to articles 11 and 12 of the Italian law (D. lgs. 39/2010).

What emerges clearly from all this is the presumption of going concern is by no means to be taken for granted; indeed, it is reasonable to doubt whether such an assumption holds for a number of companies, and whether it will continue to hold for many others in the foreseeable future.

Talking these considerations as a starting point, the present work aims to analyse the concept of going concern on the one hand, though a case study of three companies which have recently come under observation of the CONSOB and inserted in the so-called "black list" and, on the other, the consequences that the removal of the presumption of continuity can have on the kind of assessment the auditors make. Recently, in fact, we have witnessed a progressive reduction of the issuing of clean bill of health by auditors at the expense of an increase in assessments with reservations or, indeed, declarations withholding any judgement at all.

The aim of the present work is twofold: the first part analyses the principle of going concern from a business and economic perspective, underlining the diverse factors involved, as well as the variety of strategies that can be adopted to overcome business crises and, hopefully, to return to normal conditions. Once this has been completed, the work will go on to offer an overview of the dynamics that can bring a company to a crisis point, and how these affect the judgements expressed by auditors, in particular the correctness and truthfulness of the information contained in company financial statements.

2 Going concern and auditor: literature review

The concept of going concern was first regulated with the approval in 1995 of Document 21 by the Joint Commission for the drawing up of Auditing regulations by the National Council of Chartered

Accountants and the National Council of Accountants and Commercial Inspectors (Cndcr, 1995). Although, given the somewhat one-sided view of the matter, this document has certain limitations, it clarified how the work of the auditor should help assess the reliability of the account (Marasco, 2004), even though this is no absolute guarantee of the company's ability to operate in the future. Following a process of harmonization of the rules governing international auditing, Document no. 21 was integrated in Auditing Regulation 570, which was issued in October 2007 by the Joint Auditing Commission. This principle deals with the responsibilities of the auditor when reviewing a company's books, in particular how the company management use the presumption of going concern in their reports (Aspes, Campedelli, 1999; Marasco, 1995; Bava et. al., 2012).

The presumption of going concern has been the object of numerous studies both by academics and accountants and they all agree on the need for this condition to be periodically reviewed by the administrators when drawing up company financial statements (Caratozzolo, 2006; Quatraro, 1992; Quagli, 2003; A.Av.v., 2007; Superti Furga, 2004). In the case where this presumption cannot be made all other auditing principles (competence, consistency in applying assessment criteria and so on) will no longer be deemed tenable (Pontami, 2011).

The following elements undermine the presumption of going concern (Carrieri, 2008; Braidotti et. al., 2009; Soprani, 2009; Cndcr, 1995):

1. negative equity and lack of working capital;
2. negative structural margins;
3. difficulties in obtaining new credit lines or finance for investment;
4. negative cash flow;
5. impossibility of meeting debt repayment deadlines;
6. the fact of heavy losses from running costs;
7. violation of covenants contained in loan contracts;
8. sizeable reductions of market share;
9. the presence of legal battles the outcome of which could have serious consequences for the company's future viability and many others.

The first paragraph of Article 2423 and the accounting principle OIC 11 state that, when drafting a financial statement, the different items must be carefully evaluated with a view to the company's prospects as a going concern, in other words the assets and liabilities must be accounted for on the assumption that the company is in a position to carry on operating and capable of dealing with its liabilities as part of its normal economic activity (Carrieri 2008; Oic, 2005).

Further normative regulations in relation to the presumption of going concern are contained in the first paragraph of Article 24238 of the Civil Code, as well as in the modification of Article 1 of 2/2/2007 (D. Lgs 2/2/2007, no. 32), which - with reference to the

minimum content of the financial assessment of the business management - required the administrators to describe the current and future risks their company may be exposed to³.

On the subject of going concern, for companies who resort to markets for risk capital, in February 2009 the supervisory authorities - the CONSOB, the Bank of Italy, and the IVASS (formerly ISVAP) - issued a unitary document which, inspired by the recommendations of a number of international professional bodies, supplied further clarifications not only on the behaviour that administrators and auditors are obliged to adopt with regard to the drawing up compulsory financial statements, but also on the control systems that companies must put in place in order to ensure that the potential risks, current or future, are stated publically in a clear and transparent manner, as well as the uncertainties that the company may have to face in the future running of the business⁴. In brief, the document of the aforementioned three agencies recommends that, with a view to improving the transparency of financial statements and the grounds on which assessment of whether a company is a going concern is based, the information must be clearly set out, preferably the section concerning accounting policies. In the event that this is not possible, publication of the financial statement must be postponed until such time as this has been made available.

The OIC has also devoted considerable time and attention to the going concern concept; in the accounting principle devoted to general considerations on the theme of issuing financial statements document 11 issued by the OIC makes it clear that: "the issuing of a financial statement understood as a tool for providing information on the equity, financial and economic situation of a working company, that is to say a company characterised by going concern, is based on accounting principles". This means that in the event of lack of evidence to support the assumption of continuity, the normal principles of accounting used when drawing up financial statements cannot be applied. The assumption of continuity has been further clarified with the publication of document OIC 29⁵.

The auditing principle no. 570 supplies a series of indicators whose function is to set the alarm bells

ringing (Bava et al, 2012), by summarising the major existence-threatening dangers that can place the future prospects of a company at risk.

Among the ones listed by the aforementioned document we find those financial and economic factors which can involve, for example, negative equity or deficit of operating capital, fixed term loans nearing their repayment deadlines with no or little sign of the money available to repay the debt or extend the loan. Another warning signal is an overdependence on short-term loans to finance long-term activities, previous financial statements or forecasts that express negative cash flow, the inability to honour loan repayments and so on.

With regards to the going concern debate overall, one has to observe capital in its dynamic form, i.e. its ability to generate future income. In this context, therefore, the economic value of capital can be given a specific definition: it is the present value of the prospect of future gains, evaluated on the basis of the risks to which such gains are exposed.

Company indicators used by managers, however, can often be influenced by situations that are difficult to quantify in monetary terms, such unforeseen events as, for instance, the loss of administrators, or key managers without any prospect of finding adequate replacements, the sudden loss of important markets, distribution contracts, concessions or suppliers. Many of these aspects are observed by the auditor during their periodic visits, and point to problems that can often lead to business crises.

Other indicators that can have an impact on the running of a company are, for example, a reduction of capital below the legal limit, or irregularities concerning other legal norms, legal or tax disputes which in the event of an adverse ruling could lead to financial penalties that the company could ill afford to meet; the same applies to fines incurred for polluting or the extra money required for the recycling of waste produced by the company and so on.

From an international perspective we find that the going concern concept underpins accountancy rules and practice (Braidotti et al, 2009).

Moreover, in paragraphs 23 and 24 it is affirmed that the statement must be drawn up on the understanding that the company's future prospects are sound, apart from the situation where the ownership intends to go into liquidation or cease operating (Soprani, 2009; Forgione, 2008).

3 Planning for the future, professional judgement and the auditor's report

Faced with the uncertainties that can make the going concern requirement problematic, the company management could set out their future plans, planning a series of direct actions aimed at recovering economic and financial equilibrium thereby maintaining and reinforcing the company's advantages vis-à-vis their competitors. Such plans are usually

³ Still on the subject of the aforementioned document, for the companies who have to draft consolidated balance sheet, since the year 2008 they have been obliged to provide in their statement a reliable and thorough analysis of the company's situation and the trend and result of the company's performance, as well as a description of the major risks and uncertainties to which the company is exposed.

⁴ Banca D'Italia- CONSOB- ISVAP: Document 2. information to be supplied on the financial relations of the going concern, on the financial risks, on the control of the reduction in value of the company's activities and on the uncertainties regarding the use of estimates.

⁵ For further information see "OIC, Principi contabili dei CNDC dei CNR" modified by the OIC in relation to the reform of company law, op. cit. from page 19 onwards.

elaborated by the management with the help of qualified advisors. Carrying out these plans is entrusted to a figure within the company or an outsider with special competence in the specific case. The usefulness of such strategies, however, tends to diminish over time, given that if the difficulties are not overcome straight away, the problems within the company can be accentuated as a result of further unfavourable events or conditions, in this way exacerbating the company's problems.

Through such plans the economic and financial results are forecast on the basis of the decisions the company intends to put into future operation (Carboni, 2009), or with the elaboration of a business plan through which the would-be entrepreneur will be in a position to respond to a variety of demands, concerning the products on offer, the markets targeted, the nature of the competitive advantage that the company believes it can achieve, the economic potential of the business plan and the number of resources required.

After identifying all the probative elements collected, the task of the auditor is to carry out a comprehensive examination of the financial statement and its reliability (Pisoni et al, 2012), through final analytical procedures, or analysis of the indices, trends or key elements in order to ascertain whether the account overall is in line with the evidence the auditor has uncovered, his/her knowledge of the business sector and the type of business involved. The legal role of the auditor is to express, through a final report, a professional opinion on whether the accounts conform to legal standards and whether they give a truthful and reliable picture of the company's situation as regards its assets, its economic and financial position and so on. This opinion, contained in the report, is expressed in the terms stipulated by Article 14 (D. lgs 39/2010); it can be positive without reservation, positive with reservations, negative, or the auditor may feel unable to express an opinion. Furthermore, the auditor can draw attention to certain aspects requiring elucidation.

The auditor's report should contain:

- a) the legal grounds on which the auditor's opinion is based;
- b) the recipient of the report, i.e. the person who has appointed the auditor to carry out the work of drafting the report;
- c) an introductory section containing the account in question and the different responsibilities undertaken by the auditors;
- d) the nature and import of the budget, detailing the purpose of the inspection, the work carried out and whether there is sufficient information provided;
- e) the auditor's professional opinion;
- f) requests for further information if required;
- g) an opinion on the reliability and clarity of the budget statement;

h) the date and place of issue as well as the signature of the auditor who has carried out the inspection.

If, after having gone through all the necessary procedures, the auditor considers that the assumption of going concern is based on solid foundations and the management has supplied a clear plan of the future direction of the company in question, the auditor will express a positive opinion without reservations; if the information is not entirely satisfactory, the auditor will express a positive opinion with certain reservations and in the case where information is lacking a negative opinion (Manzana, 2009). Where the administrators provide a feasible and well-reasoned strategy for overcoming the crisis, the auditor can give a clean bill of health, even when doubts about the company's future remain. Otherwise the auditor may approve the budget statement, but add a note underlining the on going problems.

Recent clarification on the different types of judgement on the verification of the concept of going concern, in particular on the use of the disclaimer, i.e. the impossibility of expressing an opinion, has been supplied in a research paper by Assirevi⁶. This paper makes it clear that the auditor should abstain from forming an opinion only in extreme cases, for example where details of numerous serious problems and uncertainties are provided in the company accounts. When, on the other hand, such problems are not fully addressed in the company accounts, the auditors are advised to express reservations or give a negative opinion, if they consider that such omissions have the effect of making the company accounts as a whole unreliable.

4 Ideas, aims and research methods

The lack of evidence for considering a company a going concern, or where serious doubts remain as to its future can be traced to events and/or conditions prior to the effective default of the company. This being the case, the duty of administrators, auditors and inspectors is to analyse, demonstrate and verify that the future prospects are such that the company can be considered a going concern, and thus in a position to draft financial statements and accounts in line with regulations governing them.

In the light of all this, the present work proposes to start by analysing the concept of the going concern with reference to three public companies quoted on the Milan Stock Exchange whose situations were so

⁶ ASSIREVI is a private non profit association of auditing companies started in 1980, and successively recognised. Its aim is to analyse various issues connected with the work of auditing in order to support a technical and professional support to members and spread the word about the role of the auditors. The professionals involved in the work of the association number roughly 6,000 spread throughout the country. The association numbers 14 consultancy firms among its members, that currently make up the majority of firms that carry out audits for public authorities (Enti di Interesse Pubblico).

critical that they came under review of the CONSOB and were inserted in the black list⁷. The paper will then go on to examine what are the consequences for a company when it fails to be considered a going concern, according to the different types of opinion expressed by the auditor.

The three case studies concern the following companies: Meridiana Fly (formerly Eurofly), Viaggi del Ventaglio and EEMS. The study has a dual aim. To start with, we analyse the grounds for which each company was no longer

considered a going concern (financial, economic problems etc.). We then go on to focus on the effects that the uncertainties and problems have on the opinions expressed by the auditors, regarding the truthful and reliable representation of their predicament in the company accounts.

The choice to consider Meridiana Fly, Viaggi al Ventaglio and EEMS was based on the fact that they represent widely different spheres of activity, but also because of the different ways they responded to their crisis. The outcomes differ: some succeed in overcoming their difficulties, while others, try as they might, are unable to break free from their predicament. Moreover, each company experiences a different sort of difficulty, and adopts a wide range of strategies in the hope of returning to normal operational conditions.

The aim of our work, the results of which are reported in detail in the final section, is to represent the different factors that can culminate in a loss of going concern status, and the strategies that can help a company overcome a crisis. The paper then provides an overview of the dynamics that can lead to a crisis and the repercussions of this on the opinions expressed by the auditors with reference to the correct and truthful representation of the company's situation in budget statements.

5 Methodology

The research was carried out in a series of phases:

1. in the first phase after analysing the compulsory documentation available on-line we extracted the risks and danger signals brought to light by the administrators. We analysed the budget statements, consolidated accounts, the work of

statutory auditors, the minutes of board meetings on company performance, the documents of corporate governance and the auditors reports;

2. in the second phase we studied the restructuring plans proposed by the administrators;

3. in the third and final phase we analysed the opinions expressed by the auditors on the uncertainties regarding the company's future, and hence their judgement on whether the company was a going concern.

As regards Viaggi del Ventaglio, this company was inserted in the black list in February 2005. At the time it was struggling with numerous problems, including notable losses which had led to a reduction of working capital by over a third. Given this situation, the CONSOB deemed it necessary to keep the market updated on the company's financial and economic situation, so that potential investors would be in a position to make an informed choice. The information on the company's situation runs from October 2005 until May 2010, after which on 15 July 2010 the company officially went into receivership (Tribunale Civile e Penale di Milano- Sezione Falimentare Fasc. No. 517/10).

Regarding Meridiana Fly, it was included in the black list in 2007. The data available revealed considerable operating losses of over 11 million euros. As a consequence the CONSOB requested the disclosure of data in order to keep the market up to date with the developments of the economic and financial situation of the company with the aim of notifying potential investors. Compulsory notification of the situation followed and from 2007 every request was respected (transparency regime) until June 2013 when the company was delisted. Thereafter, the company withdrew from the Stock Market in the hope of facilitating rescue operations with other subjects working in the same sector. Today the company continues to operate in the air travel business.

Since June 2013, when the company was delisted, Meridiana Fly has been under no obligation to disclose its net financial position⁸.

The third company analysed is EEMS. This company was included in the black list relatively recently, on 30 September, 2012. It was given special attention by the CONSOB on account of its 51 million euro losses. Upon joining the black list EEMS was obliged provide monthly data on its business and debt situation. The table below provides information on the company's net financial position up till March 2015.

⁷ The CONSOB has among its roles "the protection of investors and the transparency of the property market". It decides when a company should go on the blacklist, which was set up in 2002. The companies on the list find themselves "in a situation of multiple losses". The reasons which trigger the Consob's decision to put a company on the black list and thereby put it under surveillance are generally backed by the firms whose task it is to carry out the auditing of these companies financial statements. The companies on the black list are obliged to supply monthly updates on their situation to the capital markets. The number of companies on the black list has varied over the years from 15 at the end of 2006 and 17 in 2007 up to 23 in March 2015. This confirms a sharp increase in the number of companies in difficulty over the past few years.

⁸ In June 2013 Meridian Fly left the Milan Stock Exchange. After delisting the company hoped to undertake extraordinary measures including agreements with other companies operating in the same sector. According to the CEO the company left the Stock Market to concentrate on recovering profitability,

Table 1. Viaggi del Ventaglio blacklisted in October 2005

Company	NFP 31 October 2005	NFP 31 October 2006	NFP 31 October 2007	NFP 31 October 2008	NFP 31 October 2009	NFP 31 October 2010	NFP 31 October 2011	NFP 31 October 2012	NFP 30 Giugno 2013
I Viaggi del Ventaglio	-105,5	-55	-10,4	-20,7	-15,3	-17,1	nd	nd	nd

Note: NFP= Net financial position

Source: <http://www.soldionline.it>

Table 2. Eurofly blacklisted August 2007

Company	NFP 31 August 2007	NFP 31 August 2008	NFP 31 August 2009	NFP 31 August 2010	NFP 31 August 2011	NFP 31 August 2012	NFP 30 June 2013
Eurofly (Meridiana Fly)	-11,402	-11,263	-4,07	-12,16	-6,72	-68,22	nd

Source: "Black list Consob", document retrieved from www.marketmovers.it

Table 3. EEMS Italia blacklisted September 2012

Company	NFP 30 September 2012	NFP 30 June 2013	NFP 31 December 2014	NFP 31 March 2015
EEMS Italia	- 51,21	- 28,62	- 30,80	- 35,06

Source: "Black list Consob", document retrieved from www.marketmovers.it

5.1 The Eurofly group

Eurofly s.p.a. was set up in Turin in 1989, focusing mainly on air passenger transport and other activities related to the use, repair and maintenance of aircraft. There have been many changes both as regards the company management, and its modus operandi in the constant research for a better product to meet the demands of its customers.

In 2006 Eurofly was forced to face difficulties that were not only cyclical, i.e. linked to the increasing level of competition in the business, especially the growth of low cost airlines (Carboni, 2009), but also structural, i.e. linked to the company's commercial and industrial internal processes. These negative factors led to a serious fall in profitability. Nor was the situation helped by other factors, such as climatic and political instability in certain key areas of the globe where the company operated, for instance in Egypt and the Caribbean. Moreover, profit margins in the air charter operations declined as a result of difficulties in the tour operator sector, which was dependent, in its turn, on changes in the purchasing habits of its clientele; another problem to contend with was an increase in the cost of fuel, as well as in the repair and maintenance of the company's fleet. Interest rates in the USA and Europe rose at the time, thereby worsening the credit situation; to make matters worse, certain travel companies were unable to repay what they owed, a sign of the general deterioration in the credit worthiness of the tour operator sector as a whole. Finally, the company suffered further losses from the fact that their reserves were held in dollars at a time when the dollar lost value vis-à-vis the euro.

The company closed its operations in the year 2006 with losses of over 29 million euros (compared with losses of just 2.8 million euro in 2005)⁹.

Gross earnings (EBITDA) were minus 9.5 million euro, compared with plus 4.7 million in 2005.

As we can see the net financial position suffered a deterioration in 2006, compared with the previous year, by over 23 million euro, as a result of the company's worsening performance. In particular, operating activities absorbed up to 28.8 million euro; investment and disinvestment generated a profit of 2.7 million euro, financing and capital operations generated an overall financial flow of 7.9 million euro. When the company closed its doors it presented a net financial position of minus 27.9 million, 7.9 million of which was current net debt.

5.1.1 The auditor's ruling on the Eurofly balance sheet, the industrial plan 2007-2009 and the group's recovery

The consultancy firm Deloitte & Touche concluded that it was impossible to express an opinion on the company's balance sheet of 31 December 2006, on account of a number of uncertainties relating basically to the lack of information about the rescue plan launched by the board in an attempt to overcome the serious difficulties that had led to the heavy losses¹⁰.

⁹ "Bilancio d'esercizio al 31 dicembre 2006", document found on www.meridiana.it

¹⁰ "Bilancio d'esercizio al 31 dicembre 2006", document found on www.meridiana.it

Table 4. Previous losses 2005/2006. Amounts in Euro/000

	2006	2005	Difference
Revenue from sales and services	289.835	271.474	18.360
Other revenue	6.858	6.512	346
Total revenue	296.693	277.986	18.706
Direct commercial costs	8.163	3.200	4.962
Revenue net of direct comm. costs	288.530	274.786	13.744
Fuel	88.947	72.472	16.475
Staff costs	43.390	39.143	4.247
Maintenance services and materials	40.347	33.137	7.209
Other operating costs and wet lease	71.077	84.156	(13.079)
Other business costs and overheads	19.125	14.160	4.965
Costs subtotal	262.886	243.068	19.818
EBITDAR	25.644	31.718	(6.074)
Operating leases	35.120	27.034	8.086
EBITDA	(9.476)	4.684	(14.160)
Amortization	6.260	4.836	1.424
Impairment of non-current assets	2.465	0	2.465
Other adjustment provisions	5.649	2.000	3.649
Allocation of provision and charge funds	2.090	559	1.531
Amortization and provisions	16.464	7.396	9.068
EBIT	(25.940)	(2.712)	(23.228)
Financial income/costs	(5.322)	42	(5.364)
Profit before tax	(31.263)	(2.671)	(28.592)
Taxes	(2.123)	1.685	(3.809)
Result of the divestiture of activities	0	1.581	(1.581)
Profit for the year	(29.139)	(2.775)	(26.364)

Source: "Concise Profit and Loss/Revenue account of Financial Statements 2006", retrieved from www.meridiana.it

Table 5. Net financial position

Amounts in Euro/000	2006	2005
Funds	5.149	32.272
Derivatives included in included in cash	-	8.477
Cash	5.149	40.749
Current financial claims	3.000	-
Current bank debt	9.273	18.529
Banking contracts included in banking debts	-	8.142
Current part of non-current debt	2.312	2.203
Other current financial debts	4.500	-
Current financial debt	16.085	28.874
Current net financial debt	7.936	(11.875)
Non-current financial credits	8.000	18.906
Non-current bank debts	3.783	4.270
Debt securities	-	-
Other non-current debts	24.138	30.604
Non-current financial debt	27.921	34.874
Net financial debt	27.857	4.093

Source: "Financial Statements 2006", retrieved from www.meridiana.it

Given the company's serious predicament, the board set out a three year recovery plan for the period 2007-2009. The project envisaged an upturn in activity through the intervention of and close collaboration with the shareholder Meridiana spa, a focus on short haul domestic flights on a limited number of routes with the aim of increasing income,

improving efficiency and reducing unit costs, as well as obtaining better conditions as regards the purchasing of supplies and external services, through the setting up of a computerised platform covering

organisation and competences¹¹, research and the protection of niche markets in order to secure a competitive advantage over business rivals. The plan envisaged the reconversion of the company from one involved exclusively with charter flights, to a commercial airline. Moreover, the plan entailed debt restructuring, in other words a renegotiation with its creditors—the three main banks, which together held 80% of the debt¹²—and two injections of capital, one in kind, i.e. through the conferring of goods from the main shareholder Meridiana, and the other in cash through capital markets.

On 28 June 2007 the board approved the industrial plan for 2007-2009. The fulfilment of the provisions contributed to the financial and economic recovery of the group. The problems concerning the future development of the company were considered overcome, thereby ensuring a healthy balance sheet for the year up to 31 December 2007.

Even though some uncertainty still remains as regards the company's future, the administrators claim that the company is a going concern. After the delisting from the Milan Stock Exchange the company continued to operate and on 31/12/2012, thanks to the backing of the parent company AKFED it became possible to obtain credit. In particular, AKFED undertook to: release added financial resources, underwrite new shares following an injection of capital, and reconvert loans into net assets. Despite the uncertainty surrounding future scenarios and the doubts concerning the company's ability to continue operating, thanks to the considerable support of the holding company, Eurofly had sufficient resources to continue operating. On 18/03/2014 AKFED formally committed itself in writing to continued support of the company through a series of financial undertakings, not unlike those given formerly, thereby ensuring enough equity and financial resources to justify the assumption of going concern. Nevertheless, the auditing firm declared itself unable to express any opinion as regards the financial statement of 31/12/2013.

5.2 *Viaggi del Ventaglio and EEM Italia*

We decided it would be illuminating to compare the case of Eurofly with the other two companies, whose difficulties led to their respective auditors feeling unable to express any opinion on their financial statements. These two companies are Viaggi del Ventaglio, which began operating in 1976 in the tourist and package holiday sector, and EEM Italia which made semi-conductors from 1969 until 2012, when it ceded certain activities and now operates in the photovoltaic sector.

From an analysis of the economic and financial situation of the Viaggi del Ventaglio group in 2009,

we find a reduction of their debt situation, which can be attributed, in part, to a reduction of their debt to factoring companies, owing to a suspension of credit by the latter, and partly to a reduction of debts to banks, both in current accounts and loans.

One worrying factor, however, was the money owed to suppliers in terms of unpaid credit lines.

As a result in 2009 the company management attempted to set up a series of negotiations for the relinquishing of different assets as well as for the cession of control of the company and the recapitalisation through new partners. For a number of reasons, summarised in the company report, these negotiations did not produce a positive result and the shareholders assembly, in July 2009 after approving the financial situation in which capital had descended below the legal minimum on account of a loss of 15m euro, decided to fully cover the loss through a reduction of capital to 120m euros and a new increase in capital of up to 77m euros, with the undertaking to raise 6m euros by 30 November. The assembly also nominated commissioners to liquidate the company if by 1 December the above-mentioned sum had not been paid into the company accounts.

In December 2009, having recognised that the 6m euro had not arrived and that the three liquidators had not accepted the mission, the board decided to wind up the company, delegating to the chair the task of applying to the courts to be taken into receivership. The chair was also mandated to call a new assembly to nominate other liquidators who, on acceptance, would present the request for receivership to the Court in Milan. On 18 February 2010 the company's request was accepted by the Court (former article 166 bankruptcy law) on the basis of a plan proposed by the company. In order to extinguish its debt the idea was to sell off the assets, and to realize the value of trademarks, specialised personnel and so on. Next, the plan entailed the cession of operating branches of the group to a new company (Newco) and, finally, the conversion of the credit held by third parties into shares of the group leader. However, in July 2010 the receivership was revoked by the commissioner appointed by the Court on the grounds that the party concerned had proposed an increase in capital, whereas Article 2447c.c. requires a reduction of capital to cover the losses. Moreover, the party had not given a deposit to cover the costs in line with Article 163, no. 4. Furthermore, the new proposal also contained other unacceptable elements: on the one hand it entailed the repayment of privileged creditors through the issue of shares without any prior demonstration of the likelihood of a worse outcome through the bankruptcy courts, thereby violating Article 160, para. 2 of the Bankruptcy Law, and on the other the profiles presented concerning future decisions regarding capital were far too vague, all of which rendered the new proposal uncertain and unacceptable. Owing to the liquidators' inability to formulate a credible rescue package, therefore, the Court had no alternative but to declare the company bankrupt.

¹¹ "Piano industriale 2007/2009 press conference 28 June 2007", document found on www.meridiana.it

¹² "Press conference 28 December 2007", document found on www.meridiana.it.

Table 6. Net financial debt (in thousands of Euro)

	2009	2008	Difference
Fund	425	374	51
Other available available funds	3.474	14.301	(10.827)
Liquidity	3.899	14.675	(10.776)
Current financial credi	1.569	1.022	547
Current bank debts	8.179	9.544	(1.365)
Current part of non-current debt	2.931	3.015	(84)
Other current financial debt	4.290	18.348	(14.058)
Current financial debt	15.400	30.907	(15.507)
Group net financial debt	9.932	15.210	(5.278)
Non current bank debt	602	885	(283)
Other non-current financial debt	4.460	4.557	(97)
Group net non-current financial debt	5.062	5.442	(380)
Group net financial debt	14.994	20.652	(5.658)

Source: "Consolidated financial statements 2009", document retrieved from <http://www.fallimentoivvspa.it/>

The report of the consultancy firm PKF Italia spa on the company accounts of the Viaggi del Ventaglio group concluded without expressing any opinion¹³. Given the losses by the company which had reached the limit stipulated in Article 2446 of the Civil Code, uncertainties given the lack of any real negotiation with the banks either as regards finding the necessary resources to overcome the conditions of financial crisis or as regards the restructuring of the debt. Moreover, there were uncertainties over the outcome of a dispute concerning the non-payment of rents, relating to contracts with a number of hotels, which could lead the company into further difficulties. All this cast serious doubts on the company's ability to continue in business and hence the assumption of going concern.

5.2.1 Analysis of the economic and financial situation of the EEMS group on 31 December 2012 and the report by Reconta Ernst & Young spa

From analysis of the company accounts of the EEMS Italia group we can see a reduction in turnover compared with 2011. In the course of 2012 the semiconductor sector suffered a downward trend, as the continuation of the global economic crisis had a decidedly negative effect on the sales of electronic goods, leading to heavy losses in the DRAM commodity segment. Faced with this difficult situation the company began procedures to get out of loss making areas, and these were realised in the years 2012 and 2013 through the cession of assets by EEMS Sozhou and EEMS Suzhou Technologies in favour of the Chinese group Wuxi Taiji Industrial¹⁴. The photovoltaic sector recorded a drop of 37% compared with the previous year. In particular, the renewable energy resources sector suffered a blow due to yet another change in the regulations governing the

industry which came into force in August 2012 (V° Conto Energia), hindering market operations, i.e. limiting installations of less than 12 Kw and reducing incentives.

For all these reasons the company approved an industrial plan for 2013-2016, in an attempt to concentrate on specific market sectors, on the grounds that certain areas were characterised by a premium price for European products and by small plant size less affected by competition from Chinese manufacturers and an improvement in production costs as a result both of the automation of production lines and from the direct supply of raw materials from Taiwan at low cost. The plan also foresaw the sustainability of the company as a going concern through debt restructuring and the concession by the banks of the resources required to guarantee the revival of the company's activities. Discussions are on-going and new facts and developments could emerge at any time, which could prejudice the outcome.

Reconta Ernst & Young, who were appointed to carry out the audit of the company accounts, issued on 31 December 2012¹⁵ underlined the impossibility of expressing an opinion on account of the grave uncertainties as to the outcome of the restructuring with the credit institutions, which cast considerable doubt on the company's ability to carry through its plan and honour its commitments. In the year 2013 the administration decided to renegotiate the previous financing agreement, but the parent company met with serious difficulties which made it unable to carry out part of the repayment before 31 March 2014.

¹³ "Corporate Governance 2008/2009" document found on <http://www.fallimentoivvspa.it/>

¹⁴ "Bilancio consolidato e di esercizio al 31 dicembre 2012," document found on www.eems.com

¹⁵ "Relazione della società di revisione del 18 giugno 2013" document found on www.eems.com

Table 7. Selected data from the Profit and Loss/Revenue account

Data in thousands of Euro	2012	2011	%
Total operating income and expenses	67.712	107.153	- 37%
Operating income before amortization and recovery/devaluation of non-current activities	(12.166)	(8.983)	35%
Operating income	(27.560)	(27.617)	0%
Result of the period of activities expected to continue	(38.697)	(29.938)	29%
Result of the period of activities expected to be yielded	(47.987)	(6.250)	
Total overall net profit	(86.684)	(36.458)	138%
Number of shares	43.597.120	43.597.120	
Number of Employees in activities expected to continue	224	224	

Source: "Consolidated financial statements 2012", retrieved from www.eems.com

The peculiar nature of the photovoltaic sector where the group now operates in, owing to unstable prices and the continual modifications of the regulations governing the industry, has led to a marked reduction in sales, compared to the forecasts in the recovery plan. Nevertheless, in spite of the uncertainties, the administrators were convinced that there were good grounds for believing in the company's future, and thus achieving the goals set out in the industrial plan. The auditors, however, bearing in mind the aforementioned uncertain financial and economic landscape felt unable to express any opinion as regards both the consolidation accounts of 31 December 2013 and the six monthly abbreviated statement in August 2014. In detail the auditors' doubts concerned the duration of the crisis, the negative equity and the lack of financial equilibrium; moreover, the parent company was not in a position to honour its undertakings. This being the case there were no grounds for launching a new sustainable industrial plan. The administrators, on the other hand, maintain that the presumption of going concern must be related to the definition of an agreement with new investors, as well as the positive conclusion to their request for an agreement with creditors/admission into receivership presented by the parent company. To sum up, the prospects remain unclear and not particularly hopeful, and consequently the auditors have withheld any opinion on whether the company can be considered a going concern.

6 Conclusions

The aim of this work is twofold: first, through a case study of three companies, who had come under the watchful eye of the CONSOB and inserted into the so-called blacklist, an analysis was carried out into the concept of going concern, and secondly we looked at what happens when a company is no longer considered a going concern, with particular reference to the auditor's judgement. Indeed, in a time like the present with businesses struggling to cope with the economic and financial crisis, this concept has come under increasing review, especially as there are numerous factors that threaten a company's survival.

The companies analysed are: Viaggi del Ventaglio, Meridiana Fly and EEMS. They were all

included on the CONSOB blacklist at different times, and hence subject to continuous scrutiny and required to supply periodic updates in order to keep the market informed on their situation. As regards the three companies, our objective was to understand not only their economic and financial problems and the uncertainties that had determined the loss of going concern status, but also how all this affected the judgements expressed by the auditors.

In the case of Eurofly, this company was obliged to provide updates on its situation up to its delisting from the Milan Stock Exchange in June 2013. Thereafter the company concentrated on setting up extraordinary measures with other subjects operating in the same sector, and it continues to operate today providing services in the air travel business.

The variety of problems encountered led the Eurofly board to set up a three-year plan for 2007-2009. The achievement of the conditions entailed in the plan contributed to the company's recovery. Yet doubts remain as to the company's future. The management has confirmed that the group has access to adequate financial resources to continue operating in the future thanks to the support of the parent company AKFED, which committed itself formally in March 2014 to support the company through a series of financial interventions all of which should guarantee the company's future as a going concern. Despite this the auditors fear that significant problems remain unsolved, which could in certain circumstances in the future drag the company back into difficulties, and thus they feel unable to express an opinion on the company accounts issued on 31/12/2013.

In the second case study analysed concerning Viaggi del Ventaglio, in the year 2009 the management undertook a number of negotiations with a view to offloading certain assets as well as ceding control of the company and recapitalisation through the entry of new partners. This strategy proved unsuccessful, however, and in July 2009 a shareholders meeting was convened to ratify a situation in which the company's equity had fallen below the minimum allowed by law. Negative equity, failure to honour loan covenants, and the lack of progress in negotiations with credit institutions on finding the necessary resources to overcome the crisis all led to the company going under. On the 18

February 2010 the company entered into receivership. Given the liquidators' inability to come up with a credible rescue plan, the Court declared the company bankrupt. In the light of all this and in particular of the company's heavy losses, on the same date the report of the consultancy firm PKF Italia on the company accounts of the group concluded that it was not in a position to express any opinion.

In the final case study on EEMS Italia the various negative results on the running of the company led to the drafting of an industrial plan for the 2013-2015 period. Whether the plan has been a success is still a matter of debate and the recovery is still uncertain, also because future events may occur linked to the sectorial difficulties in general which are impossible to predict and therefore assess. Nevertheless, EEMS continues to operate, despite still being included in the black list, and despite a series of negative financial results, which have led the auditors, today as in the past, to declare themselves unable to express an opinion on the company's prospects.

From the results of the three case studies it emerges that the three companies have numerous common elements as regards the circumstances that have triggered the loss of going concern status. Obviously this work does not pretend to be exhaustive in its reach, yet it does help to focus attention on certain situations which if not adequately dealt with can trigger crises and therefore put the company's future at risk. Some companies do everything possible to tackle their predicament, by making strategic decisions, restructuring plans, renegotiating the debt burden and searching for new inputs of capital, yet all these efforts are no guarantee that they will overcome their difficulties.

Turning now to the opinions expressed by the auditors in the case studies, we can see that, notwithstanding the work of the administrators in supplying all the financial information required, the auditors still feel unable to express an opinion given the uncertainties and the possibility of negative developments in the economy at large which could impinge on the companies involved and put their survival at risk.

In conclusion, when things go well everything is much simpler and any financial problems can be dealt with within the company, but when the company's future is threatened maximum professionalism is required. The key issue is not merely a drop in profits but the company's survival, and also involves the financial and legal responsibilities of the administrators as well as the wellbeing of creditors and everyone else involved.

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