The Role of Financial Analysis in Measuring the Continuity of Enterprises from the Viewpoint of the Auditor

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Abstract

The study aims to try to design a framework to guide auditors when assessing the assumption of continuity as one of the accounting assumptions that builds upon Auditor to his opinion. Was reached many of the results of this study the most important; The enterprises that are experiencing problems in repaying its obligations in the short term means the inability to continuity in the term, but does not necessarily mean that their inability to continuity in the long term as it is possible to continue to engage in business in the long term, The International Auditing Standard No. (570) and U.S. auditing standards Bulletin No. (59) contain clear guidance for the auditors can be guided them to identify the extent of continuity of enterprises to engage in the activity.

Keywords: *Liquidity ratios, Continuity, Financial failure, Profitability, Analytical procedures, Audit standards*
Problem of the study

Introduction

The assumption of continuity is one of the basic assumptions in accounting theory and is derived from this assumption many of the principles, and is in addition to that represents one of the criteria that the auditor to make sure to apply when auditing the enterprise. And the other extreme of continuity is to stop practicing the activity (liquidation), It was address this subject because of some cases where a report Auditor and with that clean enterprises exposed to bankruptcy cases leading to liquidation, and this of course impact on the credibility of the audit profession. And this study on the subject of continuity in an attempt to provide a model helps Auditor to measure the ability of enterprises to continuity in the activity, and thus improve the audit report which is based on stereotypes, in addition, they are trying to reflect the professional care given by Auditor to one of the most important accounting assumptions; and explains that interested in them from the start when planning the audit process. And can be achieved through the use of indicators analytical procedures and how to take advantage of them when the auditor to audit the overall performance of the entity, as can be achieved also interesting aspects of descriptive data, which is as important as the quantitative aspects, so it must be integrated aspects of descriptive and quantitative assessment entity's ability to continuity in the activity.

There is a belief among many auditors that the process of financial analysis carried out by the auditor considers not essential function for the main activity, and this belief is the impact on the ability of auditors to predict the risk of enterprises stopped practicing their work. And generally can express this problem as follows:

1- Does not use financial analysis as one of the analytical procedures when assessing the assumption of continuity; by most auditors, is shown clearly through displays many of the enterprises are audited at risk to stop practicing its activities after a brief period of audit (less than a year).
2- The financial crises affect the continuity of the enterprises after a brief period of audit led to undermine confidence in the audit process.

The importance of the study:

Importance of the study summarized in the following points:

1- Submission of an attempt to contribute to improving the professional judgment of the External Auditor with respect to the prediction of the continuity established in the conduct of its work.
2- Make an attempt to extract a method which can develop the capacity of Auditor to planning and audit process to improve its ability to predict possibility of continuity enterprises in activity.

Objectives of the study:

The objectives of the study are as follows:

1- illustrate how to use indicators of financial analysis to determine the ability of enterprises to continuity in the conduct of their activities and maintain their customers.
2- To build a general framework to guide auditors in planning the audit, as well as on the use of indicators of financial analysis to support their professional judgment regarding the ability of enterprises to continuity in the activity.

Questions of the study:

For the purpose of finding solutions to the problem of the study and the achievement of its objectives researcher seeks to answer the following questions:

1- What are the implications on the non-use of indicators of financial analysis during and after a audit process when planning for professional judgment to the auditors in predicting bankruptcy of enterprises that are audited?
2- Do you provide International audit Standard No. (570) and U.S. audit standards Bulletin No. (59) specific instructions to guide auditors when assessing the continuity of enterprises to engage in the activity?

Methodology of the study:

Researcher used the inductive and deductive approach, which was based on the inductive approach when formulating the problem of the study, while relying on the second when formulating the study questions.

Organization of the study:

To achieve the purpose desired from this study were divided into three points took the first point the assumption of continuity and the risk of failed enterprises, and the second auditing standards related enterprises continuity in activity, thirdly was addressed to proposed framework to assess the ability of enterprises to continuity in the activity.

Previous studies:

1- Study (مطر, 2001, pp. 7-63):

The study aims to explore the indicators used by the auditors and financial analysts in Jordan in predicting the failure of financial companies and then identify aspects of the agreement and the difference between these two groups in terms of the nature of these indicators or in terms of their relative importance and serve the study of other social groups of investors, lenders and others, and provide them with an early warning about the possibility of default in the companies in which they invest and those that are in the process of investment, which help them to avoid the risks associated with the bankruptcy of these companies, the study followed the descriptive analytical approach and style of the case study, the study found the need to provide indicators to detect the failure of companies, is situated to perform this task on auditors, financial analysts, and it guided by a set of indicators shows how continuity of the company, the study recommended the auditors and analysts to hold on to their responsibility social of care to enlighten social groups risks of financial failure, and by providing early indicators in a timely manner about the prospect of failure.

2- Study (إدريس, 2005):

The problem of this study is the prevalence of financial failure for companies and how to reduce them use effective for financial analysis which is based on financial statements that appropriate and in accordance with the rules accepted accounting principles. Was the importance of the study in: that the financial analysis tool with a feature active help in making decisions.

The role of the financial analysis of the data give corporate performance indicators and to contribute to the provision of appropriate information to users of financial statements that enable them to make decisions.

The study found that auditors , accountants and financial analysts are responsible for providing early indicators of accidents failed companies with a view to reducing the financial damage and moral implications of this faltering , also reached to the importance of guided some of the indicators used to assess the company's ability to continue or not and pointed to the importance of the use of mathematical models or to predict the statistical probability of failure for companies and also a researcher pointed out that there is an agreement between the majority of researchers according to their specialization that there is a relationship between financial analysis and good planning.

Financial ratios have a direct impact on controlling also pointed to the agreement all researchers to predict financial failure can occur in the absence of financial analysis.

First: The assumption of continuity and the risk of failed enterprises:

This includes the following:

1-1 Concept of the presumption of continuity.
1-2 Evolution of responsibility on the auditor assess the ability of enterprises to continuity in the activity.

1-1 Concept of the Assumption of Continuity

The assumption continuity of the important assumptions in accounting and the consequent many of the principles, perhaps the most important and most notably the principle of historical cost. This assumption is based on the premise that viewing or observation made on the nature of the accounting unit is that the most appropriate accounting units are organized in order to work for an indefinite period Therefore, it is often said to be a logical step to acknowledge the necessity of looking at the accounting unit on it continues to exercise its work indefinitely under normal circumstances and for this are evaluated most of the assets pursuant to this assumption on the basis of historical cost , and this assumption explains the reasons for using the basis historical cost to evaluate the resources instead of using current value , as well as procedures for the depreciation of fixed assets , and that the distinction between fixed assets and current and long-term liabilities and current is the result of the application of the assumption of continuity, and so the assumption is meaningless if it is decided to liquidate established any inability to continue. Can build on the development of this assumption within the things necessary due to the application of accounting generally acknowledges this assumption generally within the entire accounting process .And if I want to be a assumption of continuity acceptable general acceptance if a necessary support for the subsequent assumptions must be considered intuitive environment.

And as applied generally axiom continuity accounting assumes that the unit will continue to exercise its operations for a period long enough to implement existing commitments. But Sterling(Glauter,1978, P295) believes that as long as the liabilities belonging to different periods , the new liabilities must be made in the future and continuously to implement all liabilities , and this really makes the assumption is obvious for continuity and as a mean life of non-specific, and if there is evidence that the accounting unit will not last in existence for a long time enough should not be applied generally accepted accounting standards , and according to *Sterling* it is located on the accountant's responsibility to inform the beneficiaries of the financial statements so. And so we find that the reason behind the continuity intuitive consideration is that generally supports the use of historical cost as opposed to liquidation values (current value) and also supports the utility theory in the assessment. Most theorists are not agree on the above interpretation of the continuity intuitive and many of them are not established within intuitions appropriate, Chambers (Chambers, 1965,P219) constant mentions that the entity is the entity that adapts itself through the sale of its assets through its normal practice activities - through regular liquidation as opposed to obligatory liquidation - and therefore an intuitive assumption supports his hypothesis regarding the appropriateness of the Current cash Equivalent.

And from the second side , ***Mattessich*** (Glauter,1978,P298) Offers a hypothesis on the life expectancy of the economic entity without the need to assume that it will be extended indefinitely, and this means that the life of a small her, and mentioned *Vatter* that the concept of continuity is not a assumption intuitive, but it condition or the reality of the special inherent for business can be verified, and it is therefore considered continuity hypothesis and reality it is just an extension of the measurement process.

He says *Sterling* (Chambers, 1965, p294) in his response considering that continuity as hypothesis the reality as false and misleading, and rather than as assumption intuitive, it must be considered predictable (means, it predicted it to occur), in addition to that as soon as our assumption that economic entity will not be forced into liquidation does not never justified the adoption of the assessment is based on the historical cost as the other valuation may be more appropriate.

We conclude from this - according to these views - that intuitive continuity should not be interpreted as assuming intuitive the current situation (and reality) and not be a justification for the use of historical cost or the concept of benefit when evaluating assets, but it intuitive appropriate lead to information concerning assets and liabilities and future operating activities. Continuity impose a kind of coherence or the link between the past and the future, although it does not necessarily have to be the future replica or duplicate of the past, in the case of lack of continuity - imposed liquidation - the entity should not use normal accounting procedures and the accountant's responsibility to disclose the enterprise's inability to continuity in the activity. Researcher consistent with some of the opinions that dealt with the assumption of continuity , which believes that continuity means that the entity will continue to engage in activities indefinitely as long as there is no evidence to the contrary, and this requires a course based on the principles and standards accepted accounting principles , this side accounting , but from the standpoint of auditors to acknowledge as the year of the assumption of continuity, it lack the conviction and undergo absolute this delivery he if dealing with this assumption that predict expected to occur , which requires him to necessarily use different procedures for audit that supports him this prediction , and therefore available to him and make sure conviction regarding the ability of the entity subject to audit continuity in the conduct of its activities. And the main reason for raising the issue of continuity in this research stems from the philosophy that any action would influence this assumption is not necessarily affect the rest of the assumptions and the accounting principles generally accepted, which will reflect negatively on the audit report, which is based on the opinion artistic about the sincerity and fairness of the financial statements conformity what extent the allegations outlined economic entity in its financial statements with the announced standards, they represent assumptions and accounting principles (profit projects), Add to that the increasing incidence of bankruptcy in recent times leading up to the liquidation and faced by enterprises and companies after a brief period of review, which affected the credibility of audit process by a third party - the beneficiary -, add to that the increasing demand on the responsibilities of Auditor on his assessment of the assumption of continuity with note that this responsibility is not in isolation from the audit process as a whole, in other words, that does not cost the Auditor specifically for that procedure. And generally can extract the most important symptoms and manifestations of the inability of enterprises to continuity in the activity as follows: 1 - insolvency. 2 - failure.

Second: Auditing standards related enterprises continuity in activity:

Will be addressed through the following points:

1- International Audit Standards (IAS .No. (570))
2- Statement Audit Standards (SAS No.(59))

1- International Audit Standards (IAS. No. (570))

This standard is intended to establish standards and provide guidance on the responsibility of the Auditor on the assumption of continuity assessment when reviewing the financial statements. Will be addressed through the following points (ICAS, 1993, p11):

1 -1 the nature of the responsibility of management and auditor for evaluating the assumption of continuity.
1-2 Risk indicators assumption of continuity from the viewpoint Standard No. (570).
1-3evidence for the appropriateness of the assumption of continuity in accordance with the standard number (570).

1 -1 the nature of the responsibility of management and auditor for evaluating the assumption of continuity:

This point is made from two sides; first the responsibility of management, and the second the responsibility of references. And we'll explain it as follows:

First side: the responsibility of management:

The management assessment of the entity's ability to continuity in the activity. And management within the framework of preparation the financial statements may not be there is a clear requirement on the department's assessment of the ability to continuity, however, the management responsibility to assess this assumption and given that the basic assumptions underlying the process of preparation of financial statements.

There are many factors that affect management's estimate of the presumption of continuity and that must be taken into consideration and these factors are:

a) The uncertainty outcome of an event increases whenever the event is related to the future, and most of the parties that have an interest in financial reporting requests from management taking into account all the factors that are available.
b) That any judgment about the future depends on the information available at the time of sentencing, so it is likely that subsequent events conflict with this provision, which was reasonable time it was released.
c) The outcome of events influenced by the size of the enterprise and the complexity of its business and the nature and circumstances of the activity. And there are many events or circumstances that may constitute alone or combined uncertainty in the continuity established in the activity , for example ; financial events such as indicators withdrawal of financial support by creditors and debtors, and a net inflow of negative cash from operations , and take financial ratios reversed what is required , and events operating like a vacuum manager, and the loss of the main market or concession or license , as well as other events , such as non-compliance with the requirements of the capital market or legal requirements, and lawsuits pending against the property and that may be adjudicated often in invalid enterprise.

The second side: Auditor responsibility:

Limited liability references in evaluating the appropriateness of the use of the assumption of continuity management in the preparation of financial statements, the references to verify demands in spite of that there is no explicitly oblige the administration to conduct a specific assessment of the ability of established continuity in the activity. Auditor cannot predict future events that would cause stop the company from engaging in activity, and this requires of course that does not understand the audit report, which is devoid of signal to any warning about the uncertainty continuity established that ensures capacity to do so, and this is in fact what creates expectations gap in the auditing, because the express auditor to his opinion but financial statements are for a single unit. So researcher finds that it was imperative that there is a clear definition and precise about that auditing standards, as long as there are things that could be interpreted is what they are about continuity.

1-2 Risk indicators assumption of continuity from the viewpoint Standard No. (570)

There is some risk that the auditor observed on the fact that continuity may not be appropriate. And has clarified paragraph (6) of the standard risk indicators which raised the question about the possible continuation the company may come from the financial statements or from other sources. And explained this paragraph are some examples of these indicators, which must be observed by the auditor. It should be noted that a one or more of these indicators does not always mean that the assumption of continuity is questionable. And these indicators can be divided into three groups as follows:

Group A: Financial Indicators: and include:

1- The financial position represent on the net liabilities or net current liabilities.
2- It's for the date of payment of loans with specific periods and there is no real expectation for renewal or paid or highly depended on short-term loans to finance long-term assets.
3- Appearance the basic ratios negatively.
4- Large operating losses.
5-- Late the distribution of profits or stopped.
6- Inability to pay creditors in a timely manner benefits.
7- Difficulties in the application of the loan agreements.

Group B: operational indicators: and include:

1- Loss of administrative leaders without compensation.
2- Loss of a major market, excellence or license or a major supplier.
3- Labor difficulties or shortage important facilities.

Group C: Other indicators: and include:

1- Failure to implement major requirements or legal.
2- Legal proceedings pending against the company could result in provisions cannot be implemented.
3 - Changes in laws or government policy.

1-3 Evidence for the appropriateness of the assumption of continuity in accordance with the International Audit Standards No. (570):

The auditor should design procedures to obtain evidence to prove assisted in the formation of opinion on the extent of the entity's ability to continuity in the activity and highlights the importance of these procedures when doubt arises in this capacity, as may be necessary to take additional measures or update the information already obtained, As indicated in paragraph (10) that when you analyze cash flow and profitability , and other appropriate expectations , that the auditor to ascertain the extent of confidence in the established system that has been through the preparation of such information. As it to make sure that the assumptions upon which these expectations are appropriate. And Auditor attention to the fact that the longer the time period of the plan and anticipated events it not be relied upon. As it is often the focus is on the plans that have a significant impact on the ability of the company to pay all its obligations in the foreseeable future. And the auditor to obtain evidence to prove sufficient and appropriate that these plans and the process will likely be applied and that the results of these plans will lead to the improvement of the general situation of the company. The Auditor mostly to obtain written statements from the administration of these plans.

2- Statement Audit Standards (SAS No. (59))

Will be addressed through the following points:

2-1 Basic requirements.
2-2 Methods of application.

2-1 Basic Requirements

The auditor to evaluate whether there is significant doubt in the ability of the company's continuity in the activity for a reasonable period of time not exceeding usually one year from the date of auditing financial statements, and with that the auditor is not required to design audit procedures specifically to identify the circumstances and events that indicate a problem in the continuity of the company. For auditors to study the results of the regular audit and determine whether these results indicate the presence of significant doubt about the assumption of continuity, if it turns out the existence of that doubt upon that:

a - Get information about the administration's plans to alleviate the problem
b- Assess the possibility of actual implementation of the plans.
c - To identify those elements is particularly important for easing the problem of the continuity of the company, and plan and perform the audit procedures to obtain audit evidence about those elements. Add to that if the financial information is important for the future management plans, The auditor to ensure the validity and adequacy of which were based on assumptions by management to solve the problem of continuity (AICPA, 1996).

2-2 Methods of Application

These methods include three sides as follows (2004 ،حماد):

First: procedures: According to the bulletin Standard No. (59), the auditor evaluates the entity's ability to continuity and according to his knowledge specific to the conditions and events related to the prevailing, means it does not need to procedures designed to identify those circumstances and events function on the existence of the problem of continuity, where enough regular audit procedures;, which include:

a - Analytical procedures.
b - Check the following events.
c - Revision liabilities by the terms and the terms of the debt agreements and loans.
d - Read the minutes of the meetings of shareholders, board of directors and the technical committees of the Board of Directors

Second: the study of management plans: After the auditor examine these circumstances and events may consist has complained substantially about the entity's ability to continuity in the activity so it study management plans, and include this study is on the following themes: Theme I: plans to reduce expenses or postponed. Theme II: plans to increase equity. Theme III: Plans to borrow money or restructure debt. Theme IV: plans for the disposal of assets.

Third: predictions study of management: According to the bulletin Auditing Standard No. (59), the auditor is not required to examine the administration forecasts, but upon reading these predictions. And Auditor should give special attention to the cash flows and the implementation of management plans taking into account that the company would continue to exist within a year from the date of the current balance under audit. And Auditor when studying these predictions follow the following steps:

The first step: getting on assumptions related to management, including the following:

1- General economic conditions.
2 - Economic conditions in the industry-wide.
3- Sales.
4 - Cost of sales.
5 - The cost of the work.
6 - Expenses and plant and equipment expenses.
7 - Selling expenses and general administration.
8 - Income taxes.
9 - Borrowed money, interest expense and duration of the credit facilities.

Step Two: Identify the sources of management and assumptions, especially with respect to:

1- Basic and fundamental assumptions of forecasts or expectations.
2- Assumptions that are usually uncertain or sensitive to change.
3- Deviant assumptions about historical trends.

The third step: to ensure the internal consistency of the assumptions: You must be the administration internally consistent assumptions, and examples of this consistency:

1- To have a logical relationship between the net cash flow, sales, expenses, debtors and creditors.
2- To have a logical relationship between sales and cost of goods sold, labor, rent, and advertising.
3-To have a logical relationship between the income statement items and balance sheet as follows:
a - sales and accounts receivable. b - Cost of sales and inventory. c - Sales and working capital.

Third: the proposed framework to assess the ability of enterprises to continuity in the activity**:**

Includes the following points:

3.1 The use of financial analysis in the evaluation of the assumption of continuity.
3-2 use to predict the future in the evaluation of the assumption of continuity.
3.3 Summary of the proposed model to assess the assumption of continuity.

3.1 The use of financial analysis in the evaluation of the assumption of continuity

Will we begin this point to clarify the relationship between liquidity and continuity of the company's activity, where the relationship is in two phases of the impact of liquidity on the continuity of the company, the first stage in the short -term, and the second phase in the long term. Companies may face the risk of failure in the continuity of the activity in one term, depending of course on the degree or amount of liquidity available to it, and models to predict the failure of companies that have already dealt tried to find a relationship to certain variables that have a correlation with liquidity in the short and long term; for example, model Beaver address ratios in the short term, such as the ratio of surplus cash to total assets. And long-term rates such as the ratio of debt to total assets. And also a model Altman addressed in the short -term rates, such as the ratio of net working capital to total assets, and long-term rates such as the ratio of retained earnings to total assets. And applying the same note on the rest of the models conclude that all of the models that have already dealt with are actually working on a study of the state of the company in terms of liquidity in the short term and the long term .

So it will be our focus here on the descent that have a link directly or indirectly on the company's liquidity in the short term and long term, in addition to the methods of financial analysis, such as the study of the trend of the values of absolute and analysis of vertical and try to take advantage of them in the analysis over the dimensions timetables short- and long- . And therefore it can use financial analysis in the evaluation of the assumption of continuity as follows:

a - The use of financial ratios
b - The use of other methods
a - The use of financial ratios

After reviewing all the previous models - that relate to evaluate the ability of enterprises to continuity in the activity - which used financial ratios, can be classified these ratios according to the time of the impact of a liquidity squeeze on the continuity of enterprises in the activity, as well as ratios of other related - directly or indirectly -liquidity enterprises, as in table (1), and that table is clear to us that there are (16) in the short-term rate from which to judge the liquidity and quality of enterprises, compared to (10) in long-term rates;, which have been used in models that have already been addressed. And shown in Table (2) Summary of these ratios.

Table (1): Liquidity Ratios and Classification According to the Timetable for its Impact on the Continuity of Companies

No.	Ratio	Type of ratio
First: the impact of liquidity in the short term: the impact can be measured by the following percentages:		
1	The ratio of net working capital to total assets	Liquidity
2	The ratio of net profit before interest and taxes to total assets	Earnings
3	The ratio of sales to total assets	Activity
4	The ratio of net profit after tax to total assets	Profitability
5	The ratio of cash to total assets	. Cash flow
6	The ratio of liquid assets to total assets	Liquidity
7	The ratio of liquid assets to current liabilities	Liquidity
8	The ratio of earnings to total assets	Earnings
9	Percentage of profit before interest and taxes to total interest paid	Leverage
10	The ratio of current assets to current liabilities	Liquidity
11	Percentage of profit before interest and tax to shareholders ' equity	Earnings
12	The ratio of net profit before tax to intangible assets	Earnings
13	The ratio of net operating cash flow to total debt	Cash flow
14	Turnover debtors	Activity
15	Inventory turnover rate	Activity
16	Indicator internal defense or defense time period	Liquidity
Second: the impact of liquidity in the long term: the impact can be measured by the following ratios:		
1	The ratio of retained earnings to total assets.	Earnings
2	Ratio of the market value of shareholders' equity to total liabilities.	Leverage
3	The ratio of equity to total liabilities.	Leverage
4	The ratio of equity to total assets	Leverage
5	The ratio of total assets to total liabilities.	Leverage
6	The ratio of total equity to total fixed assets.	Leverage
7	The ratio of debt to total assets.	Leverage
8	Capitalization rate = the average market value of the company's ordinary shares over five years / Total long-term loans	Leverage
9	Ratio of the market value of shareholders' equity to total assets.	Leverage
10	Turnover assets.	Activity

Source: prepared by the researcher

Table 2: Summary of Classification Ratios Used as a Basis for Predicting the Failure of Enterprises

Particular	In the short-term	In the long-term	total
Liquidity ratios	5	-	5
Activity ratios	3	1	4
Leverage ratios	1	8	9
Profitability ratios	5	1	6
Cash flow ratios	2	-	2
Total	16	10	26

Source: prepared by the researcher

b - The use of other methods:

Means other methods of analysis horizontal and vertical analysis of the terms of the financial statements, the following explanation for this:

I - Financial Analysis horizontal: intended to compare the figures contained in the financial statements for several consecutive financial periods, and an example of the comparison between the net profit over a period of several previous periods. And may be a comparison of the financial ratios as compared to the current ratio at the end of the year under audit with the current ratio in the previous periods. It should be noted that the realistic outcome of this type of analysis the greater the rise time range for the comparative periods. For the purposes of assessing the capacity of enterprises to continuity in the activity it can perform financial analysis of the horizontal range ratios previously classified on the basis of both the short and long term, as it helps this analysis to identify areas where there is a difference widely requires him command of Auditor should be discussed and examined, as Auditor can also make a horizontal components analysis ratios in absolute terms and on the basis of previous schedule-rated, ultimately leading to the integration of the analysis process in both its quantitative and relative, and be input to determine the relative importance of the items that subject to audit, and requires necessarily from auditors effort and careful when interpreting each of the absolute change of the items as well as the change in the form of a percentage of the absolute change; In addition to the financial ratios. In general, the auditor do his attention on items that include a relatively large changes in the financial statements.

II. Analysis vertical: defined as the way by which the expression of each item in the financial statements as a percentage of the item and one particular referred to the amount of the base, it is based on the study of structural and which aims to transform the elements of financial statements to units of uniform or participating in basis of certain possible which to make comparisons more useful, where it is the expression of every element of the financial statements as a percentage of one of the important elements.

The Summary so that it Auditor can expect a degree of reasonability to the appropriateness of the assumption of continuity in the company's activity the subject of audit by:

- The use of financial ratios that have a correlation with liquidity, which have been classified to affect the liquidity ratios in the short term, and the impact on liquidity ratios in the long term.
- Using trend analysis (horizontal) to set ratios classified in the above point, as well as the values of items that include these ratios.
- The use of structural analysis (vertical) components ratios contained in the above point.

And so can Auditor to conceptualize reasonable to assess the entity's ability to continuity in practice the activity, at the same time have fulfilled some generally accepted auditing standards and that, for example, that do care professional due diligence, and also works to collect evidence of adequate and suitable for conducting Rated this assumption with some objectivity.

3-2 use to predict the future in the evaluation of the assumption of continuity:

To achieve Auditor forecasting purposes it:

1- Determine the source adding that Auditor forecasts rates and liquidity indicators.

2-Comparison between the predictions of the financial ratios and industry standards for determining the amount of deviation, and this would explain the auditors to the effectiveness of management's plans and expectations towards the future activities of the company. And then explain to management's assessment of Auditor to the continuity of the company in the future.

3- A comparison between forecasts and actual results, and this would make it clear to the commitment of auditor established plans developed and their efficiency in running processes as planned.

And it must be emphasized that the prediction has become a cornerstone of financial planning in economic projects , and one of the most important tools used in this area are prediction financial statements , which include the income statement , and the statement of financial position , statement of cash flows , which are prepared for a subsequent fiscal period based on certain assumptions . And Auditor study assumptions upon which to build these lists and make sure of reasonableness to take into account in addition to the company's historical performance both circumstances and potential now and in the future, taking into account the environmental conditions around, so that he can rely on financial ratios predicted.

The auditor also checking out some the things that depends upon the success of expected financial statements are prepared and then its effectiveness as a tool to predict, and these things are as follows:

1 -That is characterized by the actual data, which is the basis for preparation of financial statements expected to objectivity and comprehensiveness, that is, the data extracted from the accounting records and be prepared in accordance with generally accepted accounting principles and in accordance with the objective measurement methods.

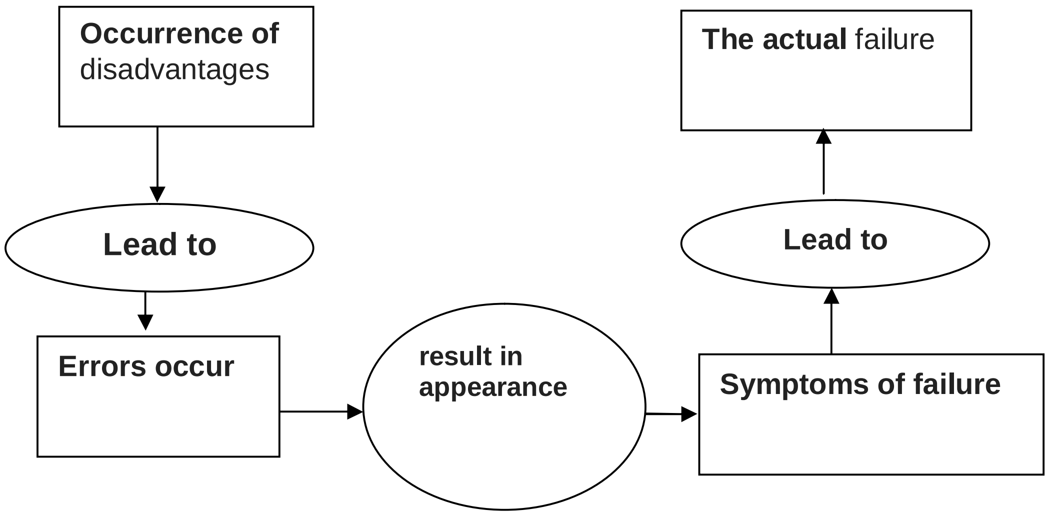
2-That characterized the models and methods used to predict the objectivity and comprehensiveness; meaning that those models are built under the scientific approach takes into account all the variables affecting the activity prediction place with a focus on controlling factor (such as the amount of sales at building expectations for sales).

3- To be replaced predictable period of time reasonable, since the shorter the forecast period increases the accuracy of forecasts and vice versa.

4 - Taking into account the effects on forecasts due to changes or shifts that occur at the phenomena or variables covered by the forecast model, for example, the equation of the regression line, which was derived to build a model to predict sales may not be suitable for predicting sales of the company itself after it doubled the size of its activity and changed environmental conditions surrounding; therefore, must take into account circumstances developed to build a new regression equation may change the number of variables.

After a Auditor to reassure the safety of the assumptions on which are expected financial statements are prepared, they can then derive the expected financial ratios, and in this context it focuses on liquidity in the short ratios, which aims to verify the appropriateness of the assumption of continuity also expect management and thus governance the accuracy of management's expectations of the assumption of continuity. And The auditor also not forgetting the aspects of descriptive, which can be addressed through model Argenti and which is known in the business world under the name of (A-Score) (مطر, 2003, p 370) and is based on different standards combine financial indicators and qualitative or descriptive, If the second gives greater weight, and this model can be used by Auditor to the discovery of the dangers related to the financial failure of enterprises. And notes on this model as described below; encompassing most aspects of descriptive advocated by the International Standard on audit No. (570), as well as bulletin standard American audit No. (59) and which requires Auditor studied and from which to explore the risk of failure, which is facing the enterprise. So researcher finds that the adoption of this model by Auditor offers a great service next to the quantitative aspects of the report on the ability of enterprises to continuity in the activity. According to this model (Argenti) he sees that the company failed in the following stages:

Figure 1: Stages of Corporate Failures Prepared by the Researcher



And in the actual application of the model, given all of the stages leading to the failure of the actual degree match with the relative weight and specified in the model are as follows:

1- Defects the relatively weight of	43
2-Errors the relatively weight of	45
3- Symptoms the relatively weight	12
Total	100

And has suggested Argenti for each of the three elements of the previous set of detailed indicators as shown in Table (3), then put the standard for the use of the model to assess the status of the company under study and according to the following scale:

1- Be a small probability of failure if the total score less than (18) degrees.
2- Be a reasonable probability of failure if the total score is greater than 18 degrees and less than 35 degrees.
3-Be a strong probability of failure if the total score (35) degrees or more.

And noted that the Argenti model provides a valuable contribution to the descriptive side cover and which is neglected by most of the previous models concerned with assessing the ability of enterprises to continuity in the activity.

Table (3): Descriptive Criteria Indicators to Judge the Failure or Not Enterprises

stage	Indicators	Standard or the relatively weight in the model
Ddisadvantages (Failure Regulatory)	1-Autocratic management	10
	2-combining the position of Chairman of the Board of Directors and Director-General	8
	3- the low efficiency of the executive management	6
	4- low efficiency of financial management	5
	5- defect in the internal control system	3
	6- Defective accounting systems and management information systems	3
	7- defect in the appointment and promotion systems and training	3
	8- the deterioration of staff spirits	3
	9- high staff turnover	2
Total		43
Errors (Failure Financial)	1- growing steadily in size and higher debt leverage indicators	18
	2-a major expansion and is not justified in the company's activity	15
	3-to engage in large projects more than energy company	12
Total		45
Symptoms	1-bad financial indicators	5
	2-Excessive creative accounting procedures	4
	3-Change in accounting policies frequently with the large number of reservations in the Auditor's report	3
Total		12
Total		100

Source: (Translate by Researcher) أمين السيد أحمد لطفي، التحليل المالي لأغراض تقييم و مراجعة الأداء و الاستثمار في البورصة، الدار الجامعية، الإسكندرية، 2006م، ص 712

3.3 Summary of the proposal model to assess the assumption of continuity:

Given the importance of the decisions of the auditors regarding the uncertainty of the ability of enterprises to continuity in the activity and the impact on the users of financial statements, it can put the two points in an integrated framework to work to help auditors identify the extent of continuity of enterprises in the activity.

The framework is based on three aspects as follows:

First: the quantitative aspect; and is derived from models that relate to the prediction of failing financial of enterprises, which previously dealt with, and this includes the examination financial indicators and trends negative with the need to take classification time into consideration (short-term and long-term), and only these indicators:

1 - Profitability. 2 - Liquidity included by cash flow ratios. 3 - Leverage. 4 - Indicators of activity.
Second: the descriptive side; and is derived from the auditing standards and specifically the International Standard on audit (570) and the Bulletin of the American Standard audit No. (59), and this aspect includes:

1- Study of the economic and regulatory conditions related to the company under audit.
2- Assess the efficiency of management.
3- Assess the company's internal activities.
4- Changes in the application of accounting principles.

Third: Examine the events subsequent to the date of preparation of the financial statements.

Detailed below of these aspects:

First: the quantitative aspect:

The auditor examined the financial indicators and the negative trends that help him in the report on the extent of the entity's ability to continuity in the activity. And generally are those indicators on the following:

1- Profitability: considered one of the important objectives of the entity's economic as it will fail to continuity in activity without a profit sufficient in the long term, so they are considered one of the important indicators to predict the ability of established continuity in the activity, and this explains to us that profitability is one of the one of the most important variables for models that have been dealt and that means measuring or predicting the financial failure of enterprises. And the following indicators can be used to express profitability and serving the forecasting process and improve the appreciation of Auditor regarding the assumption of continuity:

- The percentage of net profits before interest and taxes to total assets(Short Term) - Gross profit ratio (Short Term)
- The ratio of net profit (Short Term)
- Return on assets ratio(Short Term)
- The ratio of net profit after tax to total assets(Short Term)
- The ratio of net profit before interest and tax to shareholders' equity(Short Term)
- The ratio of net profit before interest and tax to intangible assets(Short Term)
- The ratio of retained earnings to total assets(long Term)
- The rate of return on investments(Short Term).

2- Liquidity included cash flow ratios: from one of the important elements. There are two points of view with regard to the importance of liquidity ratios in predicting the ability of enterprises to continuity in the activity, where you see the first view that liquidity ratios can be used as a basis for predicting the failure of installations (الجزار, 1981, p 436), while the second view believes that the liquidity ratios of signals can appear inconsistent over time, as they are affected by the action taken by the administration to provide cash and meet its obligations and therefore do not help to predict the failure of enterprises(Hambrick, 1988,p8).

And notes that all of the models that addressed the issue of predicting the failure of enterprises not only dealt with liquidity ratios only, so the researcher believes that it is incumbent on the auditor examine indicators of liquidity ratios with the study of the results of other indicators, and the second view enhances our rating timetable for ratios on the basis of short-term and long term, given that the enterprise has been trying to improve the liquidity situation in the short term by sell some assets, which reflects its future impact on activity. In general the following ratios can be used when assessing the liquidity:

- Net working capital (Short Term)
- The ratio of net working capital to total assets(Short Term)
- The ratio of cash to total assets (cash flow ratio). (Short Term)
- The ratio of net operating cash flow to debt (cash flow ratio). (Short Term)
- The ratio of liquid assets to total assets. (Short Term)
- Defensive indicator. (Short Term)

- The ratio of current assets to current liabilities. (Short Term)
- The ratio of liquid assets to current liabilities. (Short Term)
- The ratio of liquid assets to total liabilities. (Short Term)

The auditor also study the negative trends and clarified by the international standard No. (570) and Bulletin standard No. (59), which are as follows: - frequent operating losses. - The existence of a deficit in working capital. - A negative cash flow. - Lower sales. - Lower gross profit. - A decline in net profit. - The emergence of basic financial ratios adversely. - Inability to pay creditors in a timely manner benefits. - Rely heavily on short-term loans to finance long-term assets.

3- Activity indicators: There are a range of ratios that reflect the activity, and is considered the most important in the field of quality testing and quality of liquidity as follows: - Inventory Turnover (Short Term) - Turnover debtors (Short Term) - Turnover assets (the percentage of sales to total assets) (short Term)

In addition, the auditor should examine changes in stock prices in different periods, as the negative changes may refer to the company's inability to continuity in the activity. Where some believe that the changes in stock prices may be considered an early warning signals to the risk of corporate failures(Foster, 1986,pp555- 559), and is, I believe, more reliable analysis of the ratios given that equity markets are more sensitive to information that is not reflected in the financial statements, and can be seen clearly through the manipulation that has been in the company (Enron) inflating the nominal value of shares through profit imaginary (accounting procedures creative),this manipulation was discovered through the sudden decline of stock prices in the stock market.

4- Leverage: These ratios associated with the company's financing structure, the high degree of leverage means a high degree of risk and measuring the degree of financial leverage as follows:

$$DFL = \frac{EBIT}{EBT}$$

DFL represent Degree of Financial Leverage
EBIT represent Earnings Before Interest and Tax.
EBT represent Earnings Before Tax.
And in the case of preferred shares in the capital structure is determined by the degree of leverage as follows:

$$DFL = \frac{EBIT}{EBT[DP/(1-T)]}$$

DP represent Dividends for Prefer Stock
T represent Tax Income Rate

Therefore, the auditor examine the company's debt to have it is one of the factors that may lead to failure, as it identify the extent of compliance with loan agreements, as the non of commitment is threatened by the entity's ability to obtain new debt in the future. And the most important ratios that can be used as follows:

- Total shareholders' equity to total fixed assets. (Long term)
- Total shareholders' equity to total assets. (Long term)
- The market value of shareholders' equity to total liabilities. (Long term)
- The market value of shareholders' equity to total assets (Long term)
- Total debt to total assets*. (Long term)
- Total shareholders' equity to total liabilities. (Long term)
- Total assets to total liabilities. (Long term)
- Profit before interest and taxes to total interest paid. (Short Term)

- The capitalization rate. (Long term)

The auditor also examined the following information (descriptive) when examining the debt, which is in fact derived from the International Standard on Review (570) and the standard bulletin (59): 1 - rely heavily on short-term financing. 2 - rely on a single source of funding. 3 - Inability to debt rescheduling. 4 - to pay higher interest rates than the dominant market rates. 5 - non to repay the debt in a timely manner. 6 - the non to obtain new financing. 7 - increasing reliance on debt financing. And Summary so that it can be said that the proposed quantitative model to predict the ability of enterprises to continuity in the activity includes thirty financial ratio are as in Table (4), which summarizes the financial indicators of these ratios on the basis of the range time.

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* This ratio is one of the most important indicators in predicting the ability of enterprises to continuity in the activity, where the average this ratio in enterprises which went bankrupt about (3) and is twice the ratio in enterprises did not go bankrupt. For more details, please refer to:

Levitan, A.S. and Knoblett, J.A.(Indicators of Exceptions to the Going Concern Assumption), Auditing: A Journal of Practice and Theory, Fall 1985, P. 29

Table (4): A Summary of the Ratios Proposed Quantitative Model to Predict the Ability of Enterprises to Continuity

Particular	Number of ratios in short term	Number of ratios in long term	total
Liquidity ratios (including two cash flow ratios)	9	-	9
Activity ratios	3	-	3
Leverage ratios	1	8	9
Profitability ratios	8	1	9
Total	21	10	30

Prepared by the researcher

We note that the liquidity ratios, including cash flow ratios and relative weight in the proposed model is equivalent to the relative weight of the leverage ratios and profitability, accounting for 30% each, while the ratios activity and relative weight in the form of 10%. It also notes that the financial ratios in the short term are relatively weight in the form of 70%, while a financial ratios in the long term and relatively weight in the form of 30%.

Second: the descriptive side:

These aspects include the following:

a - the study of the economic and regulatory conditions related to the company:

Auditor should study the economic and regulatory conditions related to the industry in which the company operates, and that may have a direct impact on the assumption of continuity, for example the case of deflation.

The auditor also knowledge of dominant laws and governing the work of the company, and to make sure of the company consists of commitment and the extent of that obligations.

b - Assessment of management efficiency: The efficiency of management affect a large extent on the success or failure of the enterprises, so the auditor assess the efficiency of management in the exercise of its appreciation to fit the assumption of continuity, which is the most important assumptions underlying the preparation of financial statements and which are the responsibility of management (the process of preparing the financial statements).

And Auditor can do so as follows:

1- study management plans, where the auditor should examine their assumptions management's expectations. As well as by evaluating management plans to deal with unexpected events that recognize the behavior of the future management of the face of these events, and whether management plan for the disposal of some assets? Or to borrow new funds or debt restructuring? Or to reduce or defer expenses? Or are planning to increase property rights?.

2-Study management plans to deal with risk, and examples of those risks (Kakacek, 1984,pp 28-35), the credit risk and that may be exposed to the company as a result of the inability of one of the parties in the implementation of the contracts agreed upon, and market risk as it may entail carrying the company for losses as an inevitable result of the change in interest rates or stock prices or the prices of the products or the price of foreign exchange, and liquidity risk is that may result from the company's inability to meet its obligations as a result of the lack of sufficient cash, and may be the reason that there are no errors relating to non-sound of the interview between cash inflows and cash outflows.

And the auditor make sure that you follow the proper management of the methods to avoid the risk that the company may be exposed to or reducing adverse impact that may entail . As the auditor to make sure that the disclosure has been adequately and appropriately in the financial reports for the risks that may be exposed to the company and that may affect the decisions of users of these reports , as the non-disclosure leads to a decrease in trust of the users of those reports in the information they contain , as well as they may endure as a result of losses and therefore it may take legal action against the company's management or auditor for compensation , which could affect the company's ability to continuity in the activity and abuse of the audit profession.

c - the evaluation of the company's internal activities : An examination of information relating to the company's internal activities may sometimes refer to the existence of difficulties related to the operator , so the auditor examine this information carefully, and is that information that are related to the internal activities as follows:

1- Individuals; The information studied by Auditor represent in: Quick turnover in jobs, having basic functions filled by individuals do not have sufficient skills, and dispense with basic members or administrators without compensating them, and strike at work leads to stop working.
2- Marketing; and information is studied by the auditor: dependence on a single product, and rely on a particular market, focusing on a particular client, and good is knowledge of competitors and customers.
3- Production; and information is studied by references in: the existence of idle, exploited energy, and rely on the production of a particular product, and high production costs affect competition.

d - Changes in the application of accounting principles: the auditor examined changes in the application of accounting principles, which may some companies abuse the application of accounting principles in order to hide the problems of insolvency (accounting procedures creative), and through the application of accounting policies that lead to increased profits in short-term, so be careful and Auditor that examines these changes carefully and be sure of the need to disclose any changes in the application of accounting principles.

Third: Examine the events subsequent to the date of preparation of the financial statements:

Auditor examine events after the date of preparation of the financial statements, as this may result in what refers to the existence of problems related to the ability of companies to continuity in the activity, and an example of such subsequent events as follows: 1 - a disaster uninsured. 2 - The expropriation of some of the company's assets. 3 - The bankruptcy of a major customer. 4 - Loss of a major supplier. 5 - Low market prices for the stock.

Results and Recommendations

First: Results:

1- The companies that are experiencing problems in repaying its obligations in the short term means the inability to continuity in that term , but not necessarily mean that their inability to continuity in the long term as it is possible to continue to engage in business in the long term. The companies that are experiencing problems in repaying its obligations in the short-term and long - term means that they fail to continuity in the conduct of its activities in the short and long term , which means bankruptcy. In other words , the failure may not necessarily lead to bankruptcy and therefore cannot use the term to refer to the bankruptcy of failed companies .
2- Most of the models that attempted to assess the ability of companies to continuity in the activity - such as model Altman - The classification of financial ratios used in accordance with the timetable for the impact of a liquidity squeeze on the assumption of continuity, and worked these models to test the quality of liquidity using ratios or financial indicators such as profitability, activity and financial leverage .In other words, this result is related that he could not predict the ability of companies to continuity in the activity of by relying solely on liquidity ratios they must test the quality of these ratios.
3- Integrated into the process of assessing the ability of companies to continuity in the activity using quantitative proposed model and the proposed descriptive model, where each side works in the proposed model to address the evaluation process from the perspective of a private (quantitative and descriptive). And this evaluation process helps in improving the external audit report and through narrow the expectations gap on the responsibility of Auditor for evaluating the assumption of continuity.
4- Included model quantitative proposed to assess the ability of companies to continuity in practicing the activity on thirty (30) Financial ratio , distributed on the basis that the financial ratios in the short term a weight relative to the model increased by 70 %, while rates in the long-term relative weight in the form 30% . And included a typology of the ratios that make up the model ratios liquidity , including ratios cash flow relative weight of 30% in the proposed model, and rates of activity relative weight of 10% , and rates of leverage relative weight of 30%, and rates of profitability relative weight of 30% of the proposed model . Therefore we can say that there are many financial ratios with multiple meaning and interpretation , as well as the disqualification of all financial ratios for all purposes or for different decisions. The descriptive proposed model is the outcome of the International audit Standard No. (570) and the American audit standard No.(59).

5- The reliance on liquidity ratios only indicators to predict the extent of the ability of companies to continuity in the activity may not give a true indication of this assumption, so use other indicators beside the liquidity ratios from which to determine the quality and liquidity ratios. Add to that the division of financial ratios in the short- and long-term and their impact on liquidity provides input to identify the extent to which companies in the business continuity.
6- International Auditing Standard No. (570) and U.S. auditing standards Bulletin No. (59) contain clear guidance for the auditors can be guided them to get to know the extent of the ability of companies to continuity in practice activity.

Second Recommendations:

1- We recommend auditors when applying the proposed model to assess the assumption of continuity companies into Auditing considering the all sides, which is in the quantitative aspect, and the descriptive, which summarizes the statement by the International audit Standard No. (570) and American audit standard No. (59) and represented by the model Argenti, by examining the events subsequent to the date of preparation of the balance sheet.
2- We recommend Auditor when deciding to rely on the results of the analytical procedures in the planning Auditing process to take into consideration the relative importance of the item concerned and other review procedures and accuracy that can predict the results of the analytical procedures.
3- We recommend the auditors need to improve their performance and abilities regarding the evaluation of the ability of companies to continuity in the activity, and provide warning signs about the dangers of corporate failures for users of financial statements and can be achieved through the use of the proposed model.
4- We recommend the auditors not to rely on liquidity ratios only to evaluate the assumption of continuity for companies subject of Auditing, as they give often the rule is not true, but they test the impact of liquidity on the continuity of companies in the short term and long term through financial indicators related to the required quality and the quality of liquidity and illustrated by the proposed model in the indicators of financial leverage, and activity indicators, and profitability indicators, in addition to cash flow indicators.
5- We recommend that researchers in the field of Auditing continuously search for alternatives that would help auditors to improve their ability to predict the continuity of companies to engage in business in order to increase the credibility of the outputs of the accounting system on one side, and on the other side work to narrow the expectations gap.

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