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Report on a financial feasibility study, Supplements the Guide for a Review of a Financial Forecast, October 1982; Statement of position 1982, Oct; Statement of position 1982, Oct

American Institute of Certified Public Accountants. Financial Forecasts and Projections Task Force

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Auditing Standards Division

Statement of Position

Report on a Financial Feasibility Study

**Supplements the *Guide for a
Review of a Financial Forecast***

October 1982

**Prepared by the Financial Forecasts and Projections Task Force
American Institute of Certified Public Accountants**

NOTICE TO READERS

This Statement of Position presents the recommendations of the Financial Forecasts and Projections Task Force regarding reporting on financial feasibility studies. It represents the considered opinion of the task force on the best reporting practice for such engagements and has been reviewed by members of the AICPA Auditing Standards Board for consistency with existing auditing standards. AICPA members may have to justify departure from the recommendations contained in this statement if their work is challenged.

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Report on a Financial Feasibility Study

(This Statement of Position should be read and applied in conjunction with the *Guide for a Review of a Financial Forecast*.)

1. In 1980, the AICPA issued the *Guide for a Review of a Financial Forecast*. The guide defines a feasibility study as an analysis of a proposed investment or course of action. Although the guide was not intended to cover all aspects of feasibility studies, it does apply to the review of a forecast included in a feasibility study and an accountant's report thereon.

2. Preparation of a financial feasibility study generally includes such elements as the following:

- Analyzing program history, objectives, timing, and financing
- Analyzing demand
- Assisting management to identify key factors on which future financial results will depend
- Assisting management to develop assumptions that form the basis for the forecast
- Assembling the forecast (that is, performing the mechanical aspects of translating the assumptions into the forecast)
- Reviewing the financial forecast, which permits expressing conclusions on whether (a) the assumptions provide a reasonable basis for the forecast and (b) the forecast is presented in conformity with applicable presentation guidelines
- Concluding whether the forecast indicates that sufficient funds could be generated to meet operating and debt service requirements

When the financial feasibility study includes such procedures, the accountant's report on the study often describes them and his conclusions.

3. The guide provides for such an expanded report stating,

The report [on a review of a financial forecast] may also present other information and comments the accountant wishes to include such as . . . explanatory comments or other informative material.¹

The other information and comments may describe the nature of the work performed and conclusions reached with regard to other aspects of the financial feasibility study.

4. Following is a report that might be issued when an accountant chooses to expand his report on a financial feasibility study. Although the entity referred to in the report is a hospital, the form of report is applicable to other entities, such as a hotel or a stadium.

5. Although the following report format and language should not be departed from in any significant way, the language used should be tailored to fit the circumstances that are unique to a particular engagement (for example, the description of the proposed capital improvement program, paragraph *c*; the proposed financing of the program, paragraphs *b* and *d*; the specific procedures applied by the accountant, paragraph *e*; and any explanatory comments included in emphasis-of-a-matter paragraphs, paragraph *j*, which deals with a general matter, and paragraph *k*, which deals with specific matters).

Expanded Report

a. The Board of Directors
Example Hospital
Example, Texas

b. We have prepared a financial feasibility study of the Example Hospital's plans to expand and renovate its facilities. The study was undertaken to evaluate the ability of the Example Hospital (the Hospital) to meet the Hospital's operating expenses, working capital needs, and other financial requirements, including the debt service requirements associated with the proposed \$25,000,000 [legal title of bonds] issue, at an assumed average annual interest rate of 10.0 percent, during the five years ending December 31, 19X6.

c. The proposed capital improvements program (the Program) consists of a new two-level addition which is to provide fifty additional medical-

¹ AICPA, *Guide for a Review of a Financial Forecast* (New York: 1980) p. 22.

surgical beds, increasing the complement to 275 beds. In addition, various administrative and support service areas in the present facilities are to be remodeled. The Hospital administration anticipates that construction is to begin June 30, 19X2, and to be completed by December 31, 19X3.

- d. The estimated total cost of the Program is approximately \$30,000,000. It is assumed that the \$25,000,000 of revenue bonds that the Example Hospital Finance Authority proposes to issue would be the primary source of funds for the Program. The responsibility for payment of debt service on the bonds is solely that of the Hospital. Other necessary funds to finance the Program are assumed to be provided from Hospital funds, from a local fund drive, and from interest earned on funds held by the bond trustee during the construction period.
- e. Our procedures included analysis of
- Program history, objectives, timing, and financing.
 - The future demand for the Hospital's services, including consideration of
 - Economic and demographic characteristics of the Hospital's defined service area.
 - Locations, capacities, and competitive information pertaining to other existing and planned area hospitals.
 - Physician support for the Hospital and its programs.
 - Historical utilization levels.
 - Planning agency applications and approvals.
 - Construction and equipment costs, debt service requirements, and estimated financing costs.
 - Staffing patterns and other operating considerations.
 - Third-party reimbursement policy and history.
 - Revenue/expense/volume relationships.
- f. We also participated in gathering other information, assisted management in identifying and formulating its assumptions, and assembled the accompanying financial forecast based upon those assumptions.
- g. The accompanying financial forecast for the annual periods ending December 31, 19X2 through 19X6 is based upon assumptions that were provided by or reviewed with and approved by management. The financial forecast includes
- Balance sheets.
 - Statements of revenues and expenses.
 - Statements of changes in financial position.
 - Statements of changes in fund balance.

- h.* The financial forecast presents management's estimate of the most probable financial position, results of operations, and changes in financial position and fund balance for the forecast periods. Accordingly, the forecast reflects its judgment, based on present circumstances, of the most likely set of conditions and its most likely course of action.
- i.* We have made a review of the financial forecast in accordance with applicable guidelines for a review of a financial forecast established by the American Institute of Certified Public Accountants. Our review included those procedures we considered necessary to evaluate both the assumptions used by management and the preparation and presentation of the forecast.
- j.* Legislation and regulations at all levels of government have affected and may continue to affect revenues and expenses of hospitals. The financial forecast is based upon legislation and regulations currently in effect. If future legislation or regulations related to hospital operations are enacted, such legislation or regulations could have a material effect on future operations.
- k.* The interest rate, principal payments, Program costs, and other financing assumptions are described in the section entitled "Summary of Significant Forecast Assumptions and Rationale." If actual interest rates, principal payments, and funding requirements are different from those assumed, the amount of the bond issue and debt service requirements would need to be adjusted accordingly from those indicated in the forecast. If such interest rates, principal payments, and funding requirements are lower than those assumed, then such adjustments would not adversely affect the forecast.
- l.* Our conclusions are presented below:

 - We believe that the accompanying financial forecast is presented in conformity with applicable guidelines for presentation of a financial forecast established by the American Institute of Certified Public Accountants.
 - We believe that the underlying assumptions provide a reasonable basis for management's forecast. However, some assumptions inevitably will not materialize and unanticipated events and circumstances may occur; therefore, the actual results achieved during the forecast periods will vary from the forecast, and the variations may be material.
 - The accompanying financial forecast indicates that sufficient funds could be generated to meet the Hospital's operating expenses, working capital needs, and other financial requirements, including the debt service requirements associated with the proposed \$25,000,000 bond issue, during the forecast periods. However, the achievement of any financial forecast is dependent upon future events, the occurrence of which cannot be assured.

m. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

n. (Date)

Effective Date

6. The provisions of this statement shall be effective for accountants' expanded reports on financial feasibility studies dated on or after November 30, 1982.

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