

Webinar Series – Practical Audit Quality Considerations for Auditing in the Pandemic Environment July 2020

International Federation of Accountants®

Webinar 3: Auditor Reporting in the Pandemic Environment & Looking Ahead

Summary of Key Takeaways

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Introduction

The focus on auditor’s reports has increased in the current environment as investors and other users of financial statements seek greater transparency from entities around the impacts of Covid-19 in the financial statements, as well as greater transparency into the audit. Covid-19 may result in a rise in modifications to the auditor’s opinion, or have other implications on the auditor’s report, such as inclusion of material uncertainties relating to going concern, use of emphasis of matter paragraphs, and for listed entities, implications for key audit matters (KAMs)/critical audit matters (CAMs).

In the final of a three-part webinar series, IFAC convened a panel of audit experts to share their perspectives and practical insights on auditor reporting in the pandemic environment. The panel also reflected more generally on lessons learned over the last few months.

This document provides a summary of key takeaways from the discussion. The full recording of the session can be accessed [here](#).

Going Concern

The global economic implications of the COVID-19 pandemic have increased the likelihood that events or conditions exist that may cast significant doubt on an entity’s ability to continue as a going concern. Depending on the specific facts and circumstances of each entity, management’s assessment of going concern could be more complex and increased disclosures around going concern may be needed in the financial statements. As a result, the auditor may need to perform additional audit procedures to conclude whether management’s assessment and related disclosures are reasonable.

Challenges	Practical considerations
<p>It may be more challenging for management to assess the entity’s ability to continue as a going concern. Forward looking assumptions such as revenue projections or future cash flow may be difficult to make, and models and forecasts may be subject to drastic (yet plausible) assumptions and significant uncertainties. All these factors may make it more difficult for the auditor to audit management’s going concern assessment.</p>	<p>Effective two-way communication between the auditor and audit entity is crucial, particularly as facts and circumstances can quickly change. Management needs to prepare a robust going concern assessment. Whether an entity uses highly complex models or less complex spreadsheets, it is likely that existing models or approaches will need updating to factor in significant uncertainties and multiple scenarios. Auditing management’s going concern assessment will require the auditor to apply their professional skepticism to management’s judgments and assumptions. Considerations for the auditor may include whether:</p> <ul style="list-style-type: none">• Additional audit procedures may be required, such as increased sensitivity analysis, robust stress testing of scenarios (including reverse stress testing - considering what it would take for the entity to fail), recalculation of future cash flows and other forecasts, and inspection of key contracts.• There is a higher risk of computational error. More work may be needed around reviewing changes to models and formulas, and testing whether changing inputs result in expected outputs being calculated.• Management’s assessment covers an appropriate period (typically at least the first twelve months after the balance sheet date, or after the date the financial statements will be signed, but

Challenges	Practical considerations
	<p>the timeframe might need to be extended depending on the circumstances).</p> <ul style="list-style-type: none"> • Management has included adequate, transparent, and entity-specific disclosures in the financial statements on the level of uncertainties and events or conditions that affect going concern. • A consistent approach has been applied across all companies in a group, and wherever possible, going concern assessments have been completed at the same time. • There are any implications for the auditor’s report. (Potential implications for the auditor’s report relating to going concern are summarized in the IAASB Staff Audit Practice Alert: Auditor Reporting in the Current Evolving Environment Due to Covid-19) <p>Timely documentation of the auditor’s thought processes and rationale for their judgments and conclusions on the reasonableness of management’s assessment is important. This will help the auditor to stand back and consider – Does it make sense? Is there enough evidence to support the conclusion? It may also help with any internal firm processes or consultations for reviewing and benchmarking auditors’ going concern assessments.</p>
<p>For further guidance on going concern, see the IAASB Staff Audit Practice Alert: Going Concern. This includes examples of events or conditions that may exist as a result of the COVID-19 pandemic, sets out further example audit procedures, and outlines potential implications for the auditor’s report.</p>	

Auditor Reports

Challenges	Practical considerations
<p>Covid-19 may amplify conditions that give rise to a modification to the auditor’s opinion.</p>	<p>➔ Where modifications may be necessary, it is very important for the auditor to engage with management and those charged with governance as early as possible. Modifications to the auditor’s opinion are required where the auditor concludes that:</p> <ul style="list-style-type: none"> • There is a material misstatement of the financial statements, for example inadequate or inappropriate disclosure of the effects of the current circumstances, including insufficient description of relevant risks, estimates and judgments applied by the entity. • They are not able to obtain sufficient appropriate audit evidence, for example because of severe restrictions to accounting records that cannot be overcome by alternative remote procedures. <p>Types of modifications to the auditor’s opinion are set out in <i>ISA 705 (Revised)</i>.</p>

Challenges	Practical considerations
<p>Covid-19 may impact the identification of key audit matters (KAMs) for listed entities.</p> <p><i>[Or for entities listed on the US SEC, critical audit matters (CAMs)]</i></p>	<p>Both KAMs and CAMs are selected from matters communicated to those charged with governance (TCWG), or the audit committee, but:</p> <ul style="list-style-type: none"> • KAMs are those matters that, in the auditor's professional judgment, were of the most significance in the audit of the financial statements. A matter giving rise to a material uncertainty related to going concern is by its nature a KAM. However, in such circumstances these matters are not described in the KAM section of the auditor's report, but instead, the auditor reports in accordance with ISA 570 (Revised) on going concern. See IAASB Staff Alert on auditor reporting for further guidance. • CAMs are any matter arising from the audit of the financial statements that relates to accounts or disclosures that are material to the financial statements and involved especially challenging, subjective, or complex auditor judgment. Whilst the Covid-19 crisis may not itself be a CAM, it may be a principal consideration in the auditor's determination as to whether one or more CAMs exist. The PCAOB standards do not prescribe that substantial doubt about going concern is always a CAM, and auditors will need to apply their judgment to the specific circumstances. See PCAOB staff guidance on CAMs for further considerations. <p>For both KAMs and CAMs, the auditor should evaluate whether matters reported to TCWG are a KAM or CAM, and clearly document judgments made. KAMs are a requirement for audits of listed entities but can be used voluntarily in other audits.</p>
<p>Auditor judgment is needed in deciding when it is appropriate to use an emphasis of matter (EOM) paragraph. It is important that they are not overused.</p>	<p>Emphasis of matter paragraphs should only be included where the auditor wants to draw users' attention to a matter, they believe is of fundamental importance to the users' understanding of the financial statements. An example could be where there is not a material uncertainty related to going concern and management has disclosed useful information about how they came to that conclusion, the judgments made, mitigating factors etc, but in various places throughout the financial statements. In the same situation where disclosures are all in one place, the auditor may decide that an emphasis of matter paragraph is not necessary.</p>
<p>For further guidance on auditor reporting, see the IAASB Staff Audit Practice Alert: Auditor Reporting in the Current Evolving Environment Due to Covid-19.</p>	

Looking Ahead

Reflecting on changes experienced over the last 6 months, considerations going forward include:

- How to maintain people wellness through prolonged periods of remote working.

- How to ensure effective training of more junior staff, which can be particularly difficult for areas such as professional skepticism, which is usually learnt through practical experience and face to face interactions with clients.
- The logistics of delivering an audit with greater reliance on technology and remote access to client documentation.
- Whether changes to an entity's control environment that enabled a shift to remote operations were temporary with the view that processes and controls would revert back once staff return to the office, or whether changes will become more permanent and if so, whether more robust review processes need to be established and documented.

For further guidance on [Audit](#) and [Financial Reporting](#) considerations due to COVID-19, please refer to IFAC's dedicated webpages on both topics:



For further COVID-19 related guidance on audit and ethics from the standard-setting boards, please refer to their webpages:

IAASB: [Guidance for Auditors During the Coronavirus Pandemic](#)

IESBA: [COVID-19: Ethics & Independence Considerations](#)

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