

The Impact of COVID-19 on the Auditor's Report: Going Concern

This newsletter does not constitute an authoritative pronouncement from the IRBA, nor does it amend or override the International Standards on Auditing, South African Auditing Practice Statements or South African Guides.

This newsletter addresses some matters the auditor may consider with regard to the auditor's reporting responsibilities in the auditor's report that reflects the impact of COVID-19 on the audit of financial statements. This includes going concern and other reporting responsibilities. It is relevant to all registered auditors and their personnel and may also be used to communicate reporting issues and responsibilities to the preparers and users of financial statements.

The newsletter consists of two parts:

- I. Reporting considerations for the auditor; and
- II. Illustrative examples of paragraphs the auditor may adapt and include in the auditor's report.

Other COVID-19 guidance for auditors

Auditors are referred to the [IRBA website](#) where a repository of local and international guidance on the implications of COVID-19 in relation to audits of financial statements has been created.

The IRBA newsletter on the [Implications of the COVID-19 Outbreak on Audits and Auditors](#), which was issued on 20 March 2020, is also included in this repository.

The IRBA may issue further guidance, when necessary, as the situation develops.

Background

- Auditors are referred to the South African Auditing Practice Statement ([SAAPS 3 \(Revised May 2019\), Illustrative Reports](#), (SAAPS 3 (Revised May 2019))), that provides practical guidance to registered auditors who report on financial statements both for compliance with the International Standards on Auditing (ISAs) and the International Standards on Review Engagements, as applicable; and for the legal and regulatory requirements applicable to auditors and auditor reporting in South Africa, as related to the content and format of the auditor's report. The auditor is required to comply with SAAPS 3 (Revised May 2019) as an authoritative auditing pronouncement¹.
- Reading this newsletter is not a substitute for reading and applying the ISAs and SAAPS 3 (Revised May 2019).
- The auditor should be aware of and consider laws and regulations issued by regulators as it relates to reporting responsibilities of the auditor on the audit of financial statements. For example, section 252(1)(aa) of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) creates a responsibility for the auditor to report under certain circumstances to the Prudential Authority and others.

¹ Section 1 of the Auditing Profession Act 2005 (No. 26 of 2005) (the Act), definition of "auditing pronouncements".

- The auditor should be aware of and consider guidance that has been issued by any relevant regulator.
- In terms of Section 44 of the Auditing Profession Act, 2005 (No 26 of 2005), a notification that results from a reportable irregularity is included in the Report on Other Legal or Regulatory Requirements section of the auditor's report. The auditor should be alert to circumstances created by COVID-19 that may give rise to a reportable irregularity.
- The financial year-end date of the entity will have a bearing on the considerations to be made by the auditor in planning, executing, concluding and reporting on the engagement.
- This newsletter has been developed with the information available at the date of publication. As the impact of COVID-19 on the financial statements of entities evolve, auditors will be required to exercise their professional judgment in applying this newsletter.
- The auditor exercises professional judgment in determining whether or not a material uncertainty related to going concern exists and to report thereon or whether an Emphasis of Matter paragraph should be included in the auditor's report.
- For the illustrative examples, other wording may be more appropriate in the circumstances of individual engagements, in which case the wording in the illustrative examples of paragraphs may be adapted accordingly.
- The guidance in this newsletter is not meant to be exhaustive.

Scope

- **This newsletter does not deal with the auditor's considerations and circumstances when the auditor concludes that a modification to the auditor's opinion on the financial statements is necessary for any reason.**
- The firm is required to establish policies and procedures designed to provide it with reasonable assurance that appropriate consultation takes place on difficult or contentious matters². These matters may include those that relate to the auditor's reporting responsibilities in the auditor's report that reflects the impact of COVID-19 on the audit of financial statements.
- This newsletter applies to both the audits of listed and non-listed entities (whether companies or other types of entities).
- This newsletter may also be relevant to audits conducted in the public sector.
- Although this newsletter is written in the context of an audit of financial statements, it can be used, adapted as necessary, for independent review engagements.

² International Quality Control Standard (ISQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*, paragraph 34(a).

I. REPORTING CONSIDERATIONS FOR THE AUDITOR

The International Standards on Auditing

COVID-19 and the associated government and other responses by those affected will negatively impact the South African economy, the economic outlook of our country and its businesses. This requires that auditors, in applying their professional scepticism and exercising their professional judgment, consider how these negative effects may influence their reporting responsibilities in the auditor's report.

The ISAs prescribe how such developments may influence the auditor's reporting responsibilities in the auditor's report. In particular, the following ISAs are of relevance to this newsletter:

- ISA 570 (Revised), *Going Concern*;
- ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*; and
- ISA 706 (Revised), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*.

Management's assessment of the entity's ability to continue as a going concern and the auditor's evaluation thereof

The going concern assessment made by management is a fundamental part of the audit that may be significantly affected by COVID-19.

When performing risk assessment procedures as required by ISA 315 (Revised)³, the auditor is required to consider whether events or conditions exist that may cast significant doubt on the entity's ability to continue as a going concern. In so doing, the auditor is required to determine whether management has already performed a preliminary assessment of the entity's ability to continue as a going concern, and:

- If such an assessment has been performed, the auditor is required to discuss the assessment with management and determine whether management has identified events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern and, if so, management's plans to address them; or
- If such an assessment has not yet been performed, the auditor is required to discuss with management the basis for the intended use of the going concern basis of accounting, and inquire of management whether events or conditions exist that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern⁴.

The auditor is required to evaluate management's assessment of the entity's ability to continue as a going concern⁵; and that should cover at least 12 months from the date of the financial statements as defined in ISA 560⁶ ⁷. The auditor is also required to inquire of management as to its knowledge of events or conditions beyond the period of management's assessment that may

³ ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph 5.

⁴ ISA 570 (Revised), paragraph 10.

⁵ ISA 570 (Revised), paragraph 12.

⁶ ISA 560, *Subsequent Events*, paragraph 5(a).

⁷ ISA 570 (Revised), paragraph 13.

cast significant doubt on the entity's ability to continue as a going concern⁸.

The auditor shall remain alert throughout the audit for evidence of events or conditions that may cast doubt on the entity's ability to continue as a going concern⁹. Therefore, if, **for example**, before 15 March 2020 (the date when the President declared COVID-19 a national disaster), management had already completed its going concern assessment and the auditor had already performed the evaluation thereof (but not finalised the audit), the auditor will need to request management to reassess the entity's ability to continue as a going concern, and the auditor will then be required to reperform the evaluation thereof. In addition, as circumstances change, management and the auditor may need to respond appropriately to those changes. Due to COVID-19, we expect that the auditor's evaluation of the appropriateness of management's going concern assessment will be more extensive. We remind auditors that this will require audit evidence that is sufficient and appropriate in the circumstances and that the assessment of going concern will continue to be performed through to the point of signing the auditor's report. The effects of COVID-19 should be considered for any evaluation of management's going concern assessment after 15 March 2020, and for earlier dates if relevant to the entity.

The auditor is required to evaluate whether sufficient appropriate audit evidence has been obtained regarding, and is required to conclude on, the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements¹⁰.

If sufficient appropriate audit evidence has not been obtained, then the requirements of ISA 705 (Revised)¹¹ and specifically the effect on the auditor's report are required to be considered.

Material uncertainty

Based on the audit evidence obtained, the auditor is required to conclude whether, in the auditor's judgment, a material uncertainty exists which relate to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern. A material uncertainty exists when the magnitude of its potential impact and likelihood of occurrence is such that, in the auditor's judgment, appropriate disclosure of the nature and implications of the uncertainty is necessary for the:

- Fair presentation of the financial statements (in terms of a fair presentation financial reporting framework); or
- Financial statements not to be misleading (in terms of a compliance framework)¹².

There is considerable uncertainty about the economy and consequent future earnings, solvency and cash flows of many entities for the foreseeable future. It will be difficult for preparers to make a meaningful base case economic forecast, or a plausible downside economic scenario. In this highly uncertain environment, going concern assessments will be more difficult for entities to make, and more entities may need to report a material uncertainty related to going concern.

The auditor is required to apply professional scepticism where management and those charged with governance have determined that the current circumstances are not reasonably expected to have any material financial impact on the entity, and that no material uncertainties related to going

⁸ ISA 570 (Revised), paragraph 15.

⁹ ISA 570 (Revised), paragraph 11.

¹⁰ ISA 570 (Revised), paragraph 17.

¹¹ ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*.

¹² ISA 570 (Revised), paragraph 18.

concern exist for the entity.

Given the current uncertainty and volatility, we expect that more auditors may need to refer to material uncertainties regarding going concern in their auditor's reports, in accordance with ISA 570 (Revised). Where they do so, the reporting should draw attention to management's disclosures ("We draw attention to Note xxx in the financial statements, which indicates that ..."), the available facts and circumstances, and its impact on the financial statements. **Auditors should not report on material uncertainties using generic or boilerplate language.**

Under these circumstances, when the auditor concludes that management's use of the going concern basis of accounting is appropriate, but a material uncertainty exists, the auditor is required to determine whether the financial statements:

- Adequately disclose the principal events or conditions that may cast significant doubt on the entity's ability to continue as a going concern and management's plans to deal with these events or conditions; and
- Disclose clearly that there is a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern and, therefore, that it may be unable to realise its assets and discharge its liabilities in the normal course of business¹³.

If adequate disclosure about the material uncertainty is made in the financial statements, the auditor is required to express an unmodified opinion. In addition, the auditor's report is required to include a separate section under the heading "Material Uncertainty Related to Going Concern" to:

- Draw attention to the note in the financial statements that discloses specific matters; and
- State that these events or conditions indicate that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern, and that the auditor's opinion is not modified in respect of the matter¹⁴.

If adequate disclosure about the material uncertainty is not made in the financial statements, the auditor is required to:

- Express a qualified opinion or adverse opinion, as appropriate, in accordance with ISA 705 (Revised); and
- In the Basis for Qualified (Adverse) Opinion section of the auditor's report, state that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the financial statements do not adequately disclose this matter¹⁵.

Key Audit Matters

If management and those charged with governance have determined that no material uncertainties exist related to the going concern for the entity (while also making the necessary disclosures of their going concern assessment and assumptions made in the preparation of the financial statements), the effects of COVID-19 on the audit of the financial statements may meet the definition of a key audit matter(s), which is those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period.

¹³ ISA 570 (Revised), paragraph 19.

¹⁴ ISA 570 (Revised), paragraph 22.

¹⁵ ISA 570 (Revised), paragraph 23.

Key audit matters are selected from matters communicated with those charged with governance¹⁶.

The auditor is required to communicate key audit matters in the auditor's report in accordance with ISA 701 for audits of complete sets of general purpose financial statements of listed entities¹⁷. When the auditor is otherwise required by law or regulation, or decides to communicate key audit matters in the auditor's report, the auditor is also required to do so in accordance with ISA 701¹⁸.

In reporting a key audit matter, the auditor does not use boilerplate language. Instead, the auditor reports in a manner that informs users of the auditor's report and the financial statements, to support those users' effective decision-making. This will require a careful case-by-case consideration of the applicable facts and circumstances. Reporting might also provide context for users about the circumstances in which the audit has been carried out, and the impact of those circumstances on the way the auditor has concluded on significant judgments.

ISA 701 provides requirements and guidance on how to determine a key audit matter¹⁹ and how to communicate it²⁰. It is important to note that communicating a key audit matter is not a substitute for expressing a modified opinion²¹.

A matter giving rise to a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA 570 (Revised), is by its nature a key audit matter. However, in such circumstances, this matter is not to be described in the Key Audit Matters section of the auditor's report. Rather, the auditor is required to include a reference to the Material Uncertainty Related to Going Concern section(s) in the Key Audit Matters section²².

Where the auditor has determined that a key audit matter(s) also exists for matters other than related to going concern, it would be appropriate to also consider and reflect the COVID-19 impact in each separate key audit matter(s) in terms of ISA 701, where relevant.

Emphasis of Matter

Even if the effects of COVID-19 do not lead to a material uncertainty that may cast significant doubt on the entity's ability to continue as a going concern, an entity may still include disclosure of the effects thereof in the financial statements.

As a result, the effects of COVID-19 on the audit of the financial statements may meet the definition of an Emphasis of Matter. The reason for this is that an Emphasis of Matter paragraph is a paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgment, is of such importance that it is fundamental to users' understanding of the financial statements²³. ISA 706 (Revised) includes as one of the examples of a circumstance where the auditor may consider it necessary to include an Emphasis of Matter paragraph, a significant subsequent event that occurs between the date of

¹⁶ ISA 701, paragraph 8.

¹⁷ ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraph 30.

¹⁸ ISA 700 (Revised), paragraph 31.

¹⁹ ISA 701, paragraphs 9-10.

²⁰ ISA 701, paragraphs 11-16.

²¹ ISA 701, paragraph 12.

²² ISA 701, paragraph 15(b).

²³ ISA 706 (Revised), paragraph 7(a).

the financial statements and the date of the auditor's report²⁴.

However, the auditor is reminded that widespread use of Emphasis of Matter paragraphs may diminish the effectiveness of the auditor's communication about such matters²⁵ and should only be included when the matter is of such importance that it is fundamental to users' understanding of the financial statements.

As a reminder, if the auditor is required to modify the opinion in accordance with ISA 705 (Revised), as a result of the matter, or the auditor determines the matter to be a key audit matter to be communicated in the auditor's report, then an Emphasis of Matter is not reported²⁶.

An Emphasis of Matter paragraph is also not a substitute for reporting in accordance with ISA 570 (Revised) when a material uncertainty exists related to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern.

When the auditor includes an Emphasis of Matter paragraph in the auditor's report, the auditor is required to:

- Include the paragraph within a separate section of the auditor's report, with an appropriate heading that includes the term "Emphasis of Matter";
- Include in the paragraph a clear reference to the matter being emphasised and to where relevant disclosures that fully describe the matter can be found in the financial statements. The paragraph is required to refer only to information presented or disclosed in the financial statements; and
- Indicate that the auditor's opinion is not modified in respect of the matter emphasised²⁷.

Other Matter

An Other Matter paragraph is a paragraph included in the auditor's report that refers to a matter other than those presented or disclosed in the financial statements that, in the auditor's judgment, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report²⁸. The effects of COVID-19 on the audit of the financial statements will not usually meet the definition of an Other Matter. Accordingly, no illustration of an Other Matter paragraph is provided in this newsletter.

²⁴ ISA 706 (Revised), paragraph A5.

²⁵ ISA 706 (Revised), paragraph A6.

²⁶ ISA 706 (Revised), paragraph 8.

²⁷ ISA 706 (Revised), paragraph 9.

²⁸ ISA 706 (Revised), paragraph 7(b).

II. ILLUSTRATIVE EXAMPLES OF PARAGRAPHS THE AUDITOR MAY ADAPT AND INCLUDE IN THE AUDITOR'S REPORT

This newsletter does not deal with the auditor's considerations when the auditor concludes that a modification to the auditor's opinion on the financial statements is necessary, for any reason.

Auditors should not report on material uncertainties or Emphasis of Matters using generic or boilerplate language. As such, other wording may be more appropriate in the circumstances of individual engagements, in which case the wording in the illustrative examples of paragraphs should be adapted accordingly.

(a) Material uncertainty related to going concern

Illustration 1

The impact of the material uncertainty related to COVID-19 on ABC Proprietary Limited's ability to continue as a going concern

We draw attention to Note xxx in the financial statements, which indicates that ABC Proprietary Limited incurred a net loss of Rxxx during the year ended 30 June 20X1; and as of that date, ABC Proprietary Limited's current liabilities exceeded its total assets by Rxxx. As stated in Note xxx, COVID-19 affects ABC Proprietary Limited and this may result in certain material uncertainties for the future financial position, performance and cashflows of ABC Proprietary Limited. [Describe the indicators and circumstances relevant to the entity]. These events or conditions indicate that a material uncertainty exists that may cast significant doubt on ABC Proprietary Limited's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

Illustration 2

The impact of the material uncertainty related to COVID-19 on ABC Proprietary Limited's ability to continue as a going concern

We draw attention to Note xxx in the financial statements, which indicates how COVID-19 has affected ABC Proprietary Limited to date, and results in certain material uncertainties related to the future financial position, performance and cash flows of ABC Proprietary Limited. These events or conditions indicate that a material uncertainty exists that may cast significant doubt on ABC Proprietary Limited's ability to continue as a going concern. [Describe the indicators and circumstances relevant to the entity]. Our opinion is not modified in respect of this matter.

(b) Emphasis of Matter

Emphasis of Matter – Subsequent event: The impact of the uncertainty of COVID-19

We draw attention to Note xxx in the financial statements, which deals with subsequent events and specifically the possible effects of the future implications of COVID-19 on ABC Proprietary Limited's future prospects, performance and cashflows. Management have also described how they plan to deal with these events and circumstances. Our opinion is not modified in respect of this matter.

Bernard Peter Agulhas
Chief Executive Officer

About the IRBA

The IRBA is a public protection statutory body established to protect the financial interests of the public by ensuring registered auditors and their firms deliver services of the highest quality. It upholds audit firm independence to ensure that audit quality is such that it enhances the accuracy and credibility of financial performance reporting. In this way, the IRBA has an important role to play in building the reputation of South Africa as an investment market for both local and global investors and driving economic growth for the country.

The IRBA also registers suitably qualified accountants as auditors, who must adhere to the highest ethics standards, and promotes the auditing profession through the effective regulation of assurance conducted in accordance with internationally recognised standards and processes.