AUDIT IN AN UNCERTAIN ENVIRONMENT

1.   INTRODUCTION

To improve the chances of survival, especially during turbulent times, the ability to quickly adapt to change is one of the most necessary traits. The importance of adaptability has become more evident over the past 18 months, as the auditing profession, along with the rest of the country, has had to contend with a global pandemic and the consequences of social unrest. In fact, adaptability has become the buzzword that now denotes the need for innovation and an evolving mindset, with individuals and businesses having to navigate the new reality brought on by COVID-19.

Arguably, as the landscape has unexpectedly changed, other buzzwords such as "disruption" and "unprecedented" have become the driving force behind finding ways to adapt and survive in this environment. For instance, reliance on technology has grown exponentially, with auditors having to adapt and execute audits remotely. Further, auditors have had to assess changing risks around going concern, fraud, dealing with government grants and changes in control environments. In turn, these challenges have put a spotlight on the impact of the pandemic on ethical behaviour, auditor independence, risk management and audit quality.

Despite all these challenges, the overall adaptability that auditors have shown needs to be recognised. The profession has continued to support the functioning of the capital markets; protected the interests of shareholders and the public; and played a meaningful role in rebuilding the reputation of the profession. Auditors need to capitalise on this by making sure that the lessons learnt, as further discussed here, are effectively incorporated into the strategic plans that will help take the profession forward.

2.   IMPACT ON ETHICS AND INDEPENDENCE

The pandemic has put pressure on professionals and also created new ethical challenges. COVID-19 has become a real-world stress test for ethical cultures, as leaders, managers, employees, and other stakeholders have to adapt to the changes, and also find ways to predict and mitigate the related consequences.

Some of these challenges can be summarised as follows:

- Safeguards may no longer be available (for example, the manager or partner designated for a review might no longer be around due to illness or death).

- Pressure to achieve pre-pandemic financial results/targets.

- Changes in the IT control environment, resulting in new threats.

- Acting with sufficient expertise.

- Individual stress from health, fear or anxiety about the unknown could detract from the mindset that is expected to exercise professional judgement and professional scepticism.

- Changing regulatory requirements could potentially increase the level of threats to compliance with the fundamental principles of professional competence and due care, and professional behaviour.

- Heightened risks of fraud, with an increase in scams and cybercrimes.

2.1 How to Address the Challenges

The current environment calls for auditors to be alert to any behaviour that might, or be perceived to, compromise audit quality and the reliance that the public places on audit reports. This means auditors need to focus on engendering greater levels of trust and sound ethical behaviour in how they carry out their responsibilities. The following are important reminders:

- There is a greater need to foster an organisational culture that promotes ethical conduct, personal responsibility and accountability, in addition to having leaders who are role models. By consistently adhering to a Code of Ethics, auditors are well-positioned to encourage and promote an ethics-based culture within their organisations and firms. (The International Auditing and Assurance Standards Board's new Quality Management Standards that will become effective in 2022 also reinforce the importance of firm culture.)

- As the IRBA Code amendments relating to the *Role and Mindset Expected of Registered Auditors* (effective as of 31 December 2021) note, the promotion of ethical values that align firm culture with the fundamental principles will support the effective application of the conceptual framework.

> **Role and mindset requirements, inter alia, require auditors to apply an inquiring mind. This involves:**
>
> ➢ **Considering the source, relevance and sufficiency of information.**
>
> ➢ **Considering the nature, scope and output of the professional activity or service.**
>
> ➢ **Being open to the need for further investigation, and not just accepting information at face value. This includes recognising personal biases that affect professional judgement, so they do not unduly influence sound decision-making.**

- Organisations also need to have effective policies in place, to encourage and protect those who report illegal or unethical behaviour (actual or suspected).

- One of the most challenging aspects of the current environment is the pace at which information/facts and circumstances change. To continue to make good ethical decisions, auditors need to keep up with these changes, so they can have an impact, especially when it comes to auditor independence. This might involve:

  o Understanding whether new threats have been created, or the level of a previously identified threat has changed.

  o Determining whether a previously planned safeguard will no longer be available or be capable of addressing a threat.

- Re-evaluating the appropriateness of providing a service to an audit client. For example, it might be that with changes in client personnel, the provision of certain activities by the auditor might either involve assuming a management responsibility or create a threat to independence that cannot be eliminated or reduced by applying safeguards.
- Determining whether there are new matters that warrant communicating with those charged with governance or external parties (e.g., regulators or audit oversight bodies).

- The duty to act, if one becomes aware of any non-compliance with laws and regulations (NOCLAR) needs to be re-emphasised. Auditors need to apply judgement and know when to have discussions with management, as there is always a need to take action if a NOCLAR has been identified.

- It should not be presumed that auditors' ethics training, knowledge of a Code of Ethics and being in a role that requires a lifelong practice of making ethical judgments and taking ethical actions in the public interest will make them more inclined to make sound ethical decisions. Rather, it is important to remember that:
  - A well-defined Code of Ethics and organisational values that are rooted in ethics will provide the right foundations to teach ethics, as is the case with other professional skills.
  - Acting ethically goes beyond just compliance; it is a mindset that involves being intentional, committed and having the strength of character to consistently do the right thing.
  - Encouraging ethical values that are ingrained into management processes, performance evaluation and the reward criteria.

3. AUDIT QUALITY AND RISK MANAGEMENT

Audit risks resulting from the challenges experienced, due to the current environment, are making it necessary for auditors to take extraordinary measures to ensure that they continue to diligently deliver on their duties. Lessons learnt from other global stakeholders that previously experienced consequences of disastrous situations, such as the Ebola pandemic, are also proving to be vital in helping to develop effective strategies to respond to COVID-19 disruptions.

At the same time, it has become evident that such events can easily lead to an increase in the risk of fraud and corrupt practices. Locally, for instance, significant deficiencies have been reported in the State's procurement and contract management processes that are related to the funds made available to relieve social and economic pressures resulting from the pandemic. Emergency measures have had to be put in place and processes have been changed – and all that has heightened the risk of fraud, among others.

Disaster and Disruption = Increased Risk of Fraud

Opportunity:
1. The mere fact that there was suddenly so much money made available increased the opportunity for fraud.
2. So did factors such as:
   a. Operating with skeleton staff.
   b. Relaxed rules to allow for emergency procurement procedures.
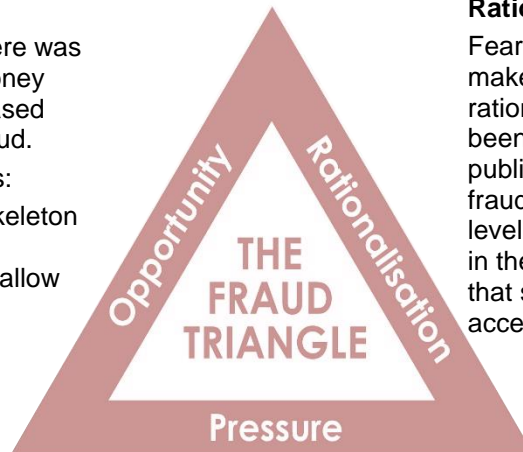
Rationalization:
Fear, uncertainty, and instability make it easier for people to rationalize wrongdoing. This has been exacerbated by the well-publicised cases of suspected fraud and corruption at top levels which could have resulted in the perception at lower levels that such behaviour is acceptable.

THE FRAUD TRIANGLE

Opportunity

Rationalisation

Pressure

Pressure:
1. The pandemic has put pressure on government, with high public expectations for the state to meet everyone's needs, to provide public funding and manage healthcare needs.
2. There was also pressure for quick decision-making even if all the systems and controls were not ready.

In this environment, it is necessary to question how audit quality has been affected. While it might still be too early to gauge whether there has been a noticeable change in trend in audit quality, certain observations show that some of the pre-pandemic issues are still ongoing.

For instance, client factors that may increase audit risk during these times include:

- Systems and processes that are not agile enough;

- Poor control environments;

- Weak fraud risk management procedures/controls; and

- Lapses in ethical decision-making by the people/leaders in the organisation (and these could speak more broadly to a "weak culture").

Areas of audit weakness that have been identified through the IRBA inspections pre-pandemic, and that continue to persist as the pandemic seems to be slowing down, include:

- Financial statement disclosure deficiencies, including the verification of additional financial statements disclosures because of the pandemic;

- Auditor judgements (audit of estimates in accordance with ISA 540), including the impact of the pandemic on impairment assessments, IFRS 9, going concern assumptions and cash flow;

- Revenue (completeness);

- Consideration of subsequent events (adjusting vs non-adjusting);

- The accuracy of cash flow statements and classifications;

- ISA 501 "… the auditor shall attend a physical stock count, unless not practicable …";

- Laws and regulations (NOCLAR, Reportable Irregularities);
- Firm: Engagement Performance (System of Quality Control and EQCR); and
- Firm: Client acceptance and continuance, as several entities and firms are under financial pressure to boost revenue streams. While the provision of non-assurance and other services to clients may be permissible, it is important to approach independence assessments with more than just a compliance mindset, considering any perceived threats to independence.

(For more details, refer to the [2020 IRBA Public Inspections Report](#)).

On the other hand, there are other more successful responses that have been noted, and examples include the following:

- A review of financial statements performed by the appropriate level of staff, to identify deficiencies in disclosures.
- From the perspective of revenue, having a thorough understanding of the entity and its information systems is more likely to ensure that audit procedures are not deficient in this area.
- An appropriate level of professional competence and due care is more likely to ensure that teams have appropriate audit evidence on file to support an accurate cash flow statement and accurate classifications within the cash flow statement.
- Organisations that invest in the training and development of their employees are better at spotting errors.
- Being wary of generic information, such as inflationary increase assumptions, in work papers. Also, impairment assessment models should consider the environment that we are in.
- Incorporating mandatory consultation policies to effectively respond to higher risk areas. In the current environment, for example, this could include consulting internally on COVID-19 related risks, such as going concern and stock counts.
- The involvement of forensic auditors.

4.   PEOPLE AND WORKING REMOTELY

Everyone will agree that it has been a transformational time for many industries worldwide, as lockdowns have been threatening people's lives and livelihoods. Therefore, there needs to be an acute awareness of the impact that the current environment and events have had on clients, audits as well as firms and their people.

In this challenging environment, remote work practices have become the norm. While remote work is not new, the pandemic has presented an opportunity for almost everyone to explore its viability – and it should be acknowledged that there have been certain benefits to its implementation.

It is then important to evaluate how people are coping in this environment, as well as how firms are responding, as their most valuable assets have been directly affected. Like any asset, people need to be in the best possible condition to produce excellent results. It is therefore necessary that firms acknowledge the impact on their people of the fear and anxiety

caused by the pandemic. Also, it is important to appreciate and accommodate personal challenges, to enable firms to effectively respond to these challenges, without compromising on audit quality.

This also means being aware of the mindset of people, as it is a critical aspect of wellbeing that can also have a direct influence on whether audits are performed diligently, with the right level of professional scepticism and quality that Auditing Standards and the public demand of auditors.

In terms of workforce support:

- Conduct surveys, to understand staff vulnerabilities, concerns and needs.

- Firm leaders should aim to be approachable and open about sharing vulnerabilities.

- Empower people, so they can invest in themselves, futureproofing what they do as professionals.

- One-on-one check-ins and mental awareness initiatives are key.

- Develop practical guidance on how to work in a remote environment, e.g., keeping cameras on during meetings to enhance interpersonal interactions.

Regarding firm support:

- Ensure and be comfortable that available technology will support the remote work environment.

POINTERS FOR MANAGING AUDIT TRAINEES

➢ **Be aware that the development of interpersonal skills might suffer during this time. Therefore, put measures in place to supplement the development of these skills.**

➢ **Virtual boardrooms are key in creating an understanding of how to interact with clients in a virtual environment.**

➢ **How to remain skeptical and challenge management in this virtual environment are different skills.**

➢ **Implement a shadowing of team members, to help trainees develop a better understanding of clients.**

➢ **Implement a buddy system to prevent trainees from feeling isolated and not knowing who to approach for help.**

- Take the opportunity to effectively utilise technology, to enhance the quality, insights and efficiency of audits.

- Develop relevant guidance and practical solutions (e.g., for stock counts and the review of documents).

- Have a resource support structure to deal with practical challenges.

- Have a quality support structure, highlighting areas of increased risks and putting risk management measures in place to effectively address risks such as additional consultation requirements.

- Foster a firm culture that supports ethical decision-making and how to effectively respond to and resolve ethical dilemmas.

- Take a holistic approach to people management and develop an understanding of their physical, emotional and mental wellbeing, as well as their aspirations and purpose.

- Leadership strategies around retention and transformation remain absolute priorities, to ensure the sustainability and evolution of the profession.

All this then means that leaders need to understand where their people and firms are in terms of navigating this new reality. This will also help support firms as they capitalise on the opportunities that have been created during this period, which include the following:

- Virtual meeting interactions are more meaningful, and attendees arrive better prepared; as a result, extra value is being gained from meetings.

- There is a stronger focus on risk and an enhanced understanding of client businesses.

- Even increased turnaround times for the completion of audits can and should be viewed in a positive light, from the perspective of the auditor taking the time to complete the audit with professional competence and due care.

Meanwhile, one of the surprising general observations over this period is that remote work has not necessarily led to a decline in productivity levels. Rather, there has been a noticeable improvement in productivity for some organisations, partly due to a lack of clear barriers between work and home life because people are constantly online. It should, however, be noted that while this might be seen as a positive for productivity, it may not bode well for people's wellbeing. As such, strategies need to be put in place to ensure that this remote work or hybrid environment does not have negative effects on people, as this could also be seen to be contributing to the attrition rate in the profession.

Another reason why productivity seems to have not suffered, as might have been expected, is that people have been willing to step in when colleagues are unavailable as result of sickness, deaths in the family and other personal challenges. However, there needs to be a recognition of people's efforts and an awareness that working under these pressured conditions cannot be sustained. Therefore, strategies that address the work/home life balance need to put in place, balancing the wellbeing of people and their fulfilment of professional duties in a sustainable way.

In the short term, recognising that people are tired, reminding them to regularly switch off and giving them time to wind down over holidays, for instance, will go a long way in alleviating short-term pressures.

5.   A GLANCE INTO THE FUTURE

If ever there was a time to reinforce ethical behaviour in the auditing profession, it is now. With the pandemic having made it necessary, in many ways, to either short-circuit well-established procedures or hasten decision-making processes, a void has been created for non-ethical behaviour to flourish. However, this is also the time for introspection and re-evaluation, to ensure that deficiencies are addressed for a better fit-for-purpose profession.

With regard to firms and their people the profession needs to develop strategies that will include helping it to adjust to a hybrid work environment and ensure that it future-proofs its skills-set. Also, leadership, retention and transformation must be top focus areas, to ensure the sustainability and evolution of the profession.

The profession must design measures on how to reconnect with its people and clients safely and responsibly, especially new clients that will be gained through the implementation of the Mandatory Audit Firm Rotation rule, which becomes effective in 2023.

It is worth acknowledging that putting quality measures in place (digital tools, training, support, consultation, etc.) could be costly for firms, especially in an environment where there are

margin pressures and clients that are operating under difficult economic conditions. However, auditors cannot compromise on quality because it is of the utmost importance for the profession; so, investments in training and technology, for instance, have to be made.

All stakeholders have a role to play in rebuilding the profession as well as ensuring accountability. That then means a collective and continued focus to take the profession beyond the pandemic is crucial.