

*Auditing in
Covid-19 -
Global
pandemic*



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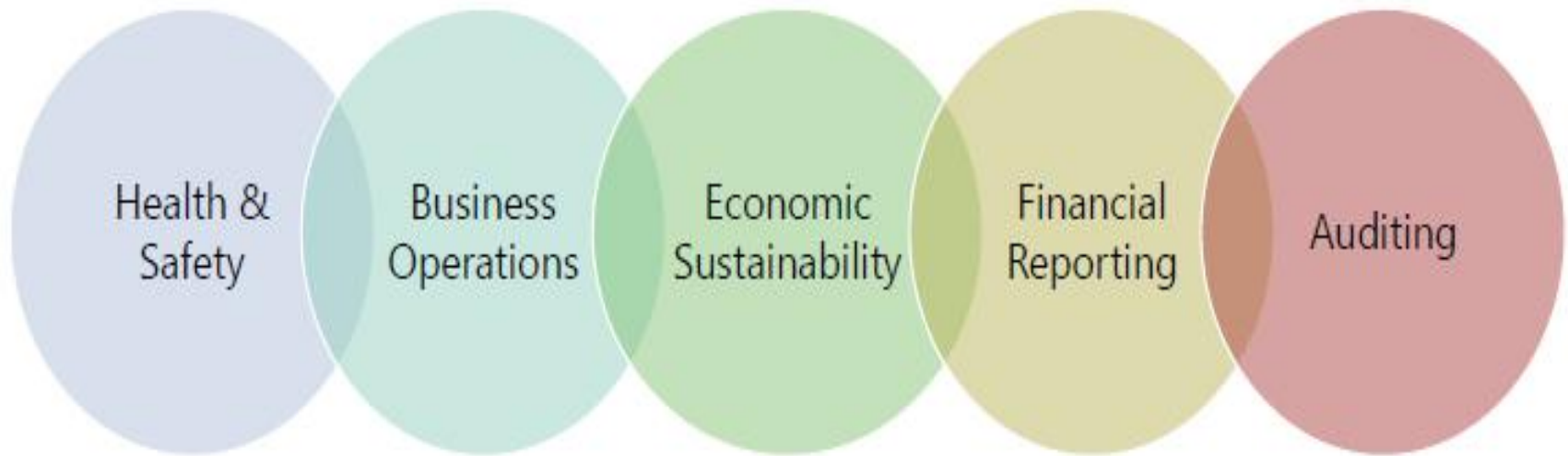
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Overall Conclusions

Overview



Covid-19 - Global pandemic



The impact of COVID-19 is **pervasive**

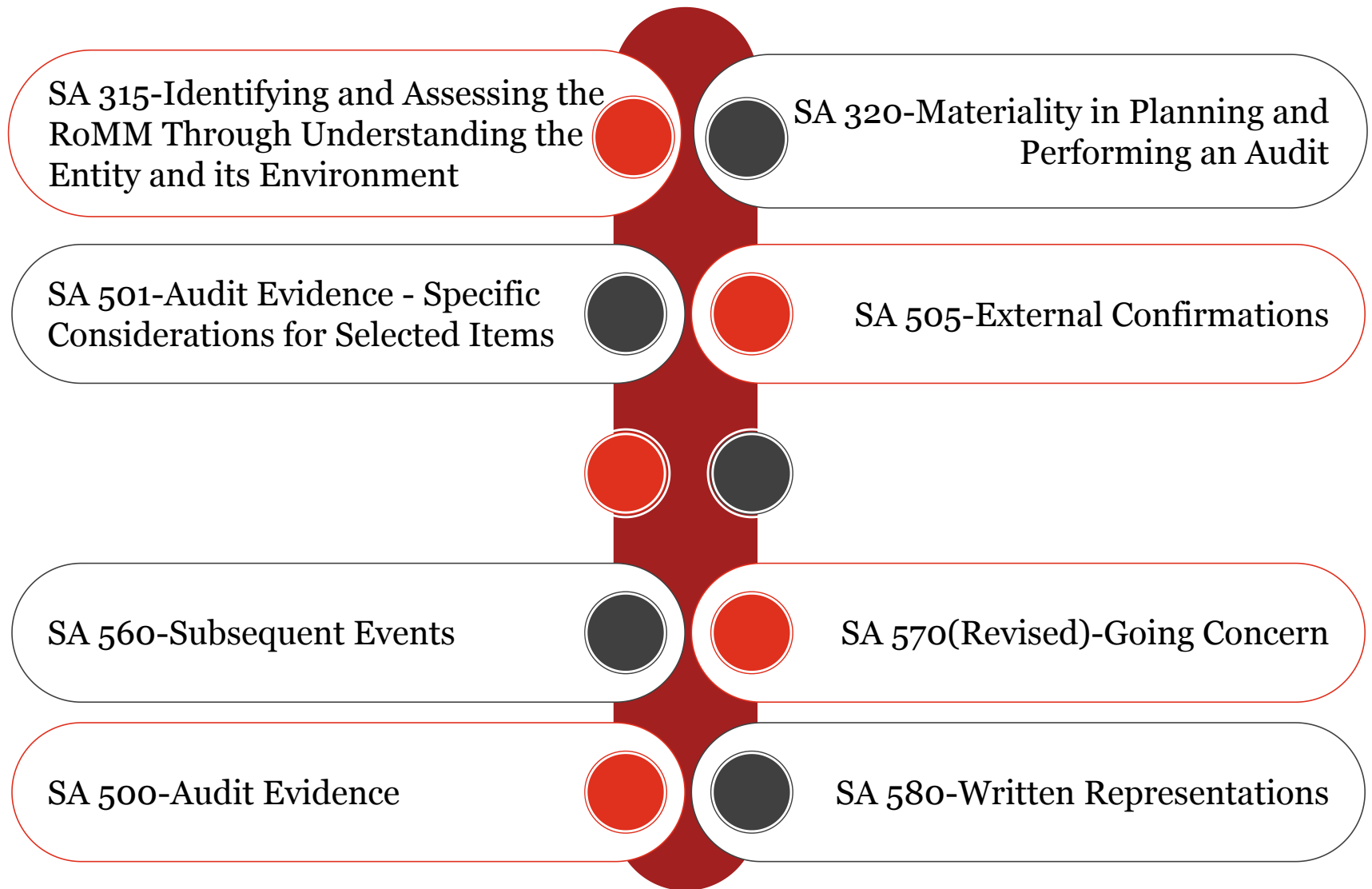
Covid-19 - Global pandemic - Background

- ❑ The global pandemic COVID-19 has already had a ***significant impact on global trade and economy*** with consequential impact on global and Indian financial markets.
- ❑ The ***uncertainty*** arises primarily from interruptions in production, supply chain disruptions, unavailability of personnel, closure of facilities / offices, decline in demand, liquidity crisis, business continuity issues, etc.
- ❑ This may also have accounting, disclosure, internal control and auditing implications for many entities and ICAI has also issued detailed guidance.
- ❑ These underlying situations, however, must not undermine the ***delivery of high quality audits***. To enable the auditors to perform audits ***additional time*** may be required and ***alternate audit procedures*** may need to be performed in order to obtain sufficient appropriate audit evidence.
- ❑ Auditors must ***carefully evaluate unique circumstances*** prevailing in their audits and assess risk accordingly when applying the concepts in their audits.

Impact on Standard of Auditing



Standard of Auditing Impact due to COVID-19



Standard of Auditing Impact due to COVID-19

SA 700(Revised)-Forming an Opinion and Reporting on Financial Statements



SA 705(Revised)-Modifications to the Opinion in the Independent Auditor's Report



SA 706(Revised)-Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report



SA 701-Communicating Key Audit Matters in the Independent Auditor's Report



SA 720(Revised)-The Auditor's Responsibility In Relation To Other Information In Documents Containing Audited Financial Statements



SA 540-Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures



Identifying and Assessing the RoMM Through Understanding the Entity and its Environment

- ❑ SA 315 provides a basis for designing and implementing responses to the assessed risks of material misstatement.

- ❑ The auditor should consider the following matters when obtaining understanding of the entity and its environment, in light of its objectives, strategies and other business risks under COVID-19:
 - Impact on entities which operates in ***multiple geographies***
 - Impact on those entities whose ***vendors/ bankers/ suppliers/ service providers*** are in geographies that are exposed.
 - Potentially have accounting implications for all entities with ***exposure to broader economic downturn*** and decline in financial markets.

Identifying and Assessing the RoMM Through Understanding the Entity and its Environment

- ❑ Auditor needs to evaluate additional risk in following areas :
 - Operational disruption resulting in any changes to the business model arising from significant ***drop in demand, reduced customer base, disruption in supply chain, employee's absence or work from home, geographical implications*** of group operations, public lock down etc.
 - Contractual ***non-compliance*** resulting in contractual breaches, additional security requirements or stressed asset valuations.
 - ***Liquidity and working capital*** issues given the reduced/ impaired ability to service debt or replenish working capital requirements due to possible lower cash flows.
 - Asset valuations – ***downward asset valuations*** may trigger legal and compliance issues or lead to liquidity challenge.

- ❑ The auditor should also ***discuss with TCWG and management*** whether the impact has been incorporated into their risk assessment processes and how they have identified and assessed the significance of the emerging business risks. The auditor should also consider if disclosures are required in the financial statements about the key assumptions made in reaching this conclusion.

- ❑ If the auditor has revised the risk assessment as a result, audit ***materiality*** may also need to be revised as the audit progresses.

Auditing Accounting Estimates

- ❑ SA 540 deals with the auditor's responsibilities regarding accounting estimates, including fair value accounting estimates, and related disclosures in an audit of financial statements.
- ❑ Significant assumptions including ***projected cash flows***, used in these accounting estimates may be affected by the impact of COVID-19.
- ❑ Examples where significant accounting estimates used by management are:
 - ***Impairment*** of Goodwill, Property Plant and Equipment, Intangible Assets and Valuation & impairment of receivables, loans and advances
 - Valuation of defined benefit plans and obligations – due to significant changes in employee strength or ***de-valuation*** of underlying plan assets
 - Stock compensation performance conditions and obligations.
 - Contractual ***penalties***
 - Employment termination benefits
 - Insurance recoveries related to business interruptions
 - Onerous contract provisions
 - Allowance for ***expected credit losses***

Auditing Accounting Estimates

- ❑ The auditor should use procedures as prescribed by SA 540, to check whether:
 - the accounting estimates, including fair value accounting estimates, in the financial statements, whether recognised or disclosed, are ***reasonable***; and
 - related disclosures in the financial statements are ***adequate***.

- ❑ The above procedures include how management has assessed the ***effect of estimation uncertainty*** or the risk assessment and audit evidence supporting these accounting estimates and related disclosures that may be affected by the impact of COVID-19 on the business of the entity and the economic environment.

Audit Evidence - Specific Considerations for Selected Items

- ❑ Auditor need to obtain sufficient appropriate audit evidence in accordance with SA 330, SA 501 and other relevant SAs, with respect to certain aspects of
 - Existence and condition of inventory;
 - Completeness of litigation and claims involving the entity;
 - Obtaining external confirmations; and
 - Using work of an expert

- ❑ Due to government-imposed shutdowns or due to unavailability of the client personnel, it ***may not be practicable*** for most of the business entities to ***conduct physical verification of inventory*** as on the date of the financial statements i.e. 31st March, 2020.

- ❑ The auditor must plan procedures depending on the underlying circumstances wherein the ***inventory count date*** could be advanced prior to the year- end or deferred to a date after the year-end.

- ❑ In some cases, ***alternative audit procedures***, for example inspection of documentation of subsequent sale of specific inventory items acquired or purchased prior to the physical inventory counting, may provide sufficient appropriate audit evidence about existence and condition of inventory.

Using the Work of Another Auditor in Consolidated Financial Statements

- ❑ SA 600 deals with situations where the ***principal auditor***, reporting on the financial information of an entity, uses the work of another auditor with respect to the financial information of one or more components included in the financial information of the entity.
- ❑ Paragraph 49 of Guidance Note on Audit of Consolidated Financial Statements states to consider requirement under SA 600 in a case where the ***parent's auditor is not the auditor of all the components*** included in the consolidated financial statements.
- ❑ The principal auditor should perform procedures to obtain sufficient appropriate audit evidence, that the work of the other auditor is adequate for the principal auditor's purposes.
- ❑ While doing so, the ***principal auditor should consider*** how the ***impact of COVID-19*** including travel bans, temporary suspension of business operations, government mandated leaves, etc., may affect risk assessments, materiality and the ability to obtain sufficient appropriate audit evidence in respect of components.
- ❑ If principal auditor is unable to obtain adequate information or reporting from the component auditors, the principal auditor ***should express a qualified opinion or disclaimer of opinion*** because there is a limitation on the scope of audit.

Using the Work of Another Auditor

- ❑ The ***alternative means or methods*** to obtain sufficient appropriate audit evidence by the principal auditor from component auditor are as follows:
 - Can data be shared cross-border, to allow for principal auditor for review? Could files be loaded into a ***cloud-based portal*** and a login provided to the principal auditor? Local laws may restrict cross-border data sharing. If in doubt, advice should be sought on any local legal restrictions.
 - Can video calls and/or ***screen sharing software*** be used to discuss the work with the component auditor?
 - Can the component auditor be asked to complete a ***detailed questionnaire*** or clearance on the work they have performed?
 - Consider the outcome of any prior visits, including visits during planning or at an interim stage
 - What work of component auditor was previously reviewed?
 - Consider the past work of the component auditor – have there been significant errors or issues, or has work been performed to a high standard?
 - Can a more detailed memorandum be provided to the component auditor on what work should be done for purpose of group reporting?
 - What work can be done centrally by the Principal auditor's team?
 - If finance systems are integrated, data may be accessible for review by Principal Auditor. Management may be able to provide information directly to the Principal auditor to allow for testing.

- ❑ Each individual engagement will need to be assessed on a case by case basis to determine what may be appropriate.

Subsequent Events

- ❑ SA 560 deals with the auditor's responsibilities relating to subsequent events in an audit of financial statements

- ❑ The auditor shall take into account the auditor's risk assessment in determining the nature and extent of such audit procedures, which shall include the following:
 - Obtaining an ***understanding*** of any ***procedures management has established*** to ensure that subsequent events are identified.
 - ***Inquiring of management*** and, where appropriate, those charged with governance as to whether any subsequent events have occurred which might affect the financial statements.
 - ***Reading minutes***, if any, of the meetings, of the entity's owners, management and those charged with governance, that have been held after the date of the financial statements and inquiring about matters discussed at any such meetings for which minutes are not yet available.
 - Reading the entity's latest subsequent interim financial statements, if any.

- ❑ When, as a result of the procedures performed, the auditor identifies events that require adjustment of, or disclosure in, the financial statements, the auditor shall determine whether each such event is ***appropriately reflected*** in those financial statements.

Subsequent Events

- ❑ Events occurring after the reporting period are categorized into two viz.
 - ***Adjusting events*** i.e. those require adjustments to the amounts recognised in its financial statements for the reporting period; and
 - ***Non-adjusting events*** i.e. those do not require adjustments to the amounts recognised in its financial statements for the reporting period.

- ❑ In certain cases, ***Management judgement*** may be required to categories the events into one of the above categories. However, adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to ***conditions existing*** at the balance sheet date. Disclosure should be made in the report of the approving authority of those events occurring after the balance sheet date that represent material changes and commitments affecting the financial position of the enterprise.

- ❑ Entities must ***disclose significant recognition and measurement uncertainties*** that might have been created by the outbreak of the COVID -19 in measuring various assets and liabilities. They should also disclose how they have dealt with the impact of COVID -19 on the financial position and financial performance of the entity.

Written Representations

- ❑ SA 580 deals with the auditor's responsibility to obtain written representations from management and, where appropriate, those charged with governance.
- ❑ Auditors need to assess whether any ***specific representations*** may be required to be obtained from the Management in relation to Managements' assessment of impact from the ongoing outbreak of COVID-19 on the financial statements for the year ending March 31, 2020 as well as for the reasonable foreseeable future.

Going Concern

- ❑ SA 570 deals with the auditor's responsibilities in the audit of financial statements relating to going concern and the implications for the auditor's report.
- ❑ There could be ***several situations*** arising from the ongoing COVID-19 outbreak that could have an impact on the ***assumption*** relating to going concern. For some entities, the impact could be severe and may leave management with no realistic alternative but to ***liquidate or cease operations***. There could also be entities which may have to scale down their operations while impact may not be significant for other entities.
- ❑ COVID-19 is resulting in ***significant operational disruption*** and presents an existential threat for many businesses. Entities and audit teams need to ***consider the implications*** on the assessment on going concern and viability in the financial report and whether these circumstances will result in ***prolonged operational disruption*** which will significantly erode the financial position of the entity.
- ❑ In the current scenario, while making Going concern assessment, ***management*** would generally be expected to ***prepare detailed forecasts*** which, will require regular updation till the financial statements are authorized for issue. These forecasts should capture potential scenarios and management's plans.
- ❑ Management should consider the impact of COVID-19 on customers, suppliers and employees. Management should also consider whether the insurance policies taken by the entity cover the losses arising from the COVID -19.

Going Concern

- ❑ The auditor will only be able to form a conclusion relating to going concern once management has made its own assessment. The auditor should ***inquire of management and TCWG*** as to what information is available about the future, and determine whether this has been appropriately considered as part of management's assessment.

- ❑ This should, for example, include a ***detailed and robust review of up to date forecasts, cash flows, sensitivity analyses*** and reviews of COVID-19 contingency plans and impact assessments conducted by the management.

- ❑ Given the level of uncertainty and speed of increasing impact of COVID-19, audit teams need to ***critically consider the current position at the point of sign off as part of the subsequent events review*** right up to the point of signing the auditor's report, and may need further evidence and information by management, including updating financial models.

- ❑ If the entity is disclosing in their subsequent events disclosures that an estimate of impact cannot be made due to the evolving situation, this ***may result in a material uncertainty on going concern*** within the audit report.

Audit Report implication

- ❑ For entities that are significantly affected by the COVID-19 situation, there are a number of ways that the auditor's report might be affected, as one or more of the following may be required in accordance with the reporting SAs:
 - Modifications to the auditor's opinion due to material misstatements or an inability to obtain sufficient appropriate audit evidence (**SA 705**)
 - Inclusion of a going concern material uncertainty section (**SA 570**)
 - Inclusion of key audit matters (**SA 701**)
 - Addition of an emphasis of matter paragraph (**SA 706**)

- ❑ When the entity has been materially affected and auditor has concluded that the ***accounting is not appropriate*** and/or the ***disclosures*** management has made in the financial statements are ***not adequate or appropriate*** in the circumstances, SA 705, requires us to issue a qualified or adverse opinion, as appropriate in the circumstances depending on the materiality and pervasiveness of the impact, due to a disagreement with management that is material to the financial statements.

- ❑ A modification to the audit opinion (qualification or disclaimer of opinion, as appropriate in the circumstances) is also necessary if we are ***unable to obtain sufficient appropriate audit evidence*** to conclude that the financial statements as a whole are free from material misstatement.

Audit Report implication

- ❑ The effects of COVID-19 and governments' actions taken in order to curb the spread are significant. For many entities, these actions will result in events or conditions that ***may cast significant doubt on the entity's ability to continue as a going concern***. When such events or conditions are identified, the auditor should seek sufficient appropriate audit evidence to determine whether or not a material uncertainty exists.

- ❑ In the current circumstances, audit work addressing the effect of the COVID-19 on the entity may frequently be a ***matter that required significant auditor attention in audits*** and auditor may decide that it is a "***matter of most significance in the audit of the financial statements***" of the current period, in accordance with SA 701. For example, it may have involved significant auditor judgement because it relates to areas in the financial statements that involved significant management judgement, such as impairment of non-financial or financial assets, fair values or revenue recognition.

- ❑ The auditor should evaluate whether the impact of the disruption caused because of COVID-19 to the operations of the entity, consequential impact on the financial statements would be a key audit matter and if determined so, the auditor would need to ***report the same*** along with ***how the matter was addressed*** in the audit.

Other Information In Documents Containing Audited Financial Statements

- ❑ Entities would need to provide additional disclosure as part of the financial statements/ annual report w.r.t. the following areas:-
 - ***Risk assessment*** – Entities may elaborate on existing reported risks w.r.t. calamities or add new ones relating to COVID-19.
 - ***Management discussion and analysis*** – Entities may include management’s discussion and analysis of any material current and potential future impact on their operations, financial condition and liquidity arising out of the entity’s exposure to COVID-19 risks.
 - ***Notes to the financial statements*** – Specific disclosures under the subsequent events accounting standards and any other specific account specific disclosures.
- ❑ The auditor is required to read any other information disclosed in the annual report and consider whether the same is ***consistent with the financial statements*** and the auditor's knowledge obtained in the audit.

The Auditor's Responsibilities Relating to Fraud in An Audit of Financial Statements

- ❑ SA 240 deals with the auditor's responsibilities relating to fraud in an audit of financial statements. Specifically, it expands on how SA 315 and SA 330 are to be applied in relation to risks of material misstatement due to fraud.
- ❑ The impact of COVID-19 on businesses could be very significant and could put ***pressures on management to meet performance targets*** or market expectations. This raises the risk of the likelihood of fraud in the financial statements to a higher level which requires the auditor to exercise a much higher degree of ***skepticism*** and carry out extended audit procedures to eliminate the possibility of fraud or material error in the financial statements.

Internal Control Consideration



Internal Control Considerations

- ❑ In case of companies, where the auditors have to issue a Report on the Internal Financial Controls over Financial reporting, because of the impact of COVID-19, there could be additional considerations that need to be considered as below:
 - Companies may need to implement ***new internal controls*** or modify existing internal controls over financial reporting.
 - Evaluate whether ***any of the controls is not operating*** effectively on account of absence of concerned person due to illness/quarantine/working from home/isolation/travel inaccessibility.
 - Identify alternate controls.
 - Company's ability to close financial reporting process in time.
 - Company's ability to design and implement controls related to selection and application of Generally Accepted Accounting Principles (GAAP) for accounting

Internal Control Considerations

Internal financial reporting - Opinion

Identify the new risks involved in this scenario (remote access to server, zoom security, etc.)

Alternate procedures over the operating effectiveness of controls during the lock-down period

Risk of fraud, errors,
misstatement

Internal controls designed and implemented to consider the impact of Covid-19

Extensive documentation for the design and effective implementation of the controls

Overall Conclusion



Overall Conclusions

- ❑ The ***role of auditors*** at times like this is under ***increased scrutiny*** as the auditors have a public interest obligation to complete the audit work in accordance with professional standards and ethics requirements.

- ❑ Under the current circumstances, auditors must recognize that the manner in which they conducted the audits in the past may ***need significant modification*** to address the challenges and uncertainties arising out of the impact of COVID-19.

- ❑ Auditors should ***exercise a very high degree of skepticism*** and be prepared to call out where the Company's narrative that the Board presents is not specific enough and does not "tell the whole story" of the various scenarios and level of uncertainty specific to the Company's operations. Irrespective of the challenges and uncertainties, there ***should not be any dilution or non-compliance with the auditing standards*** in carrying out the audits.

Any Questions



Questions

- Whether we are required to perform additional audit procedures in case if we are not able to attend physical inventory count ?
- Whether we can rely on Scanned evidences in current scenario ?
- Whether impact of Covide-19 is mandatorily required to be reported as KAM under SA 701?
- Whether any additional procedures are required to perform when confirmation responses are received by email or facsimile ? As in the current scenario when we are not able to send/receive hard copy confirmations?
- Whether alternative means of accessing workpapers of Component (Subsidiary) can be implemented ?
- Whether Current conditions change our responsibilities for obtaining sufficient appropriate audit evidence under the SAs or other relevant auditing standards?

Thank you