



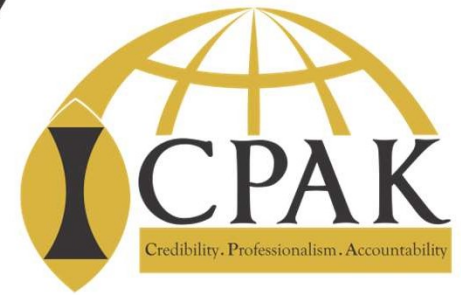
INAUGURAL EXTERNAL AUDIT PRACTITIONERS CONFERENCE

**Independence and Governance Issues:
A critical Focus on Practitioners and Possible
way-out Regarding Going Concern
Considerations**

By: FCPA Georgina Malombe

15th December 2020

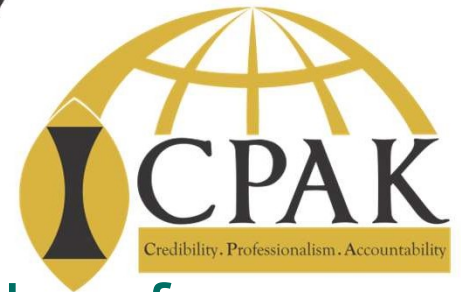
Agenda



- 1 Introduction-Leading through crisis
- 2 Independence & Governance
- 3 Emerging independence & Governance Issues
- 4 Going Concern Considerations
- 5 Auditors Opinion
- 6 Conclusion

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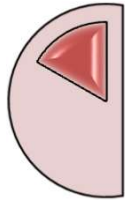
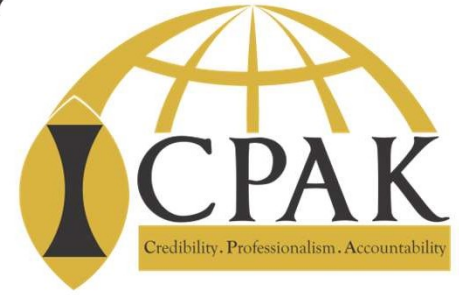
Leading Through Crisis



- ☐ Great change leaders focus on people & processes.
- ☐ Organizations evolve overtime.
- ☐ Stability and change must coexist
- ☐ Without doing things differently, no company is likely to succeed , or last(going concern).
- ☐ **What lessons have we learnt from Covid-19 ?**

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Leading People Through Change



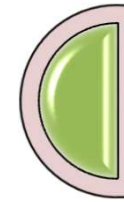
Support

Remove Barriers like
sense of loss. Provide
resources and be
available



Sway

Map out critical
change agents
and stakeholders
.

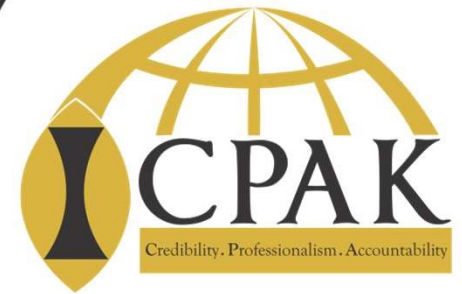


Learn

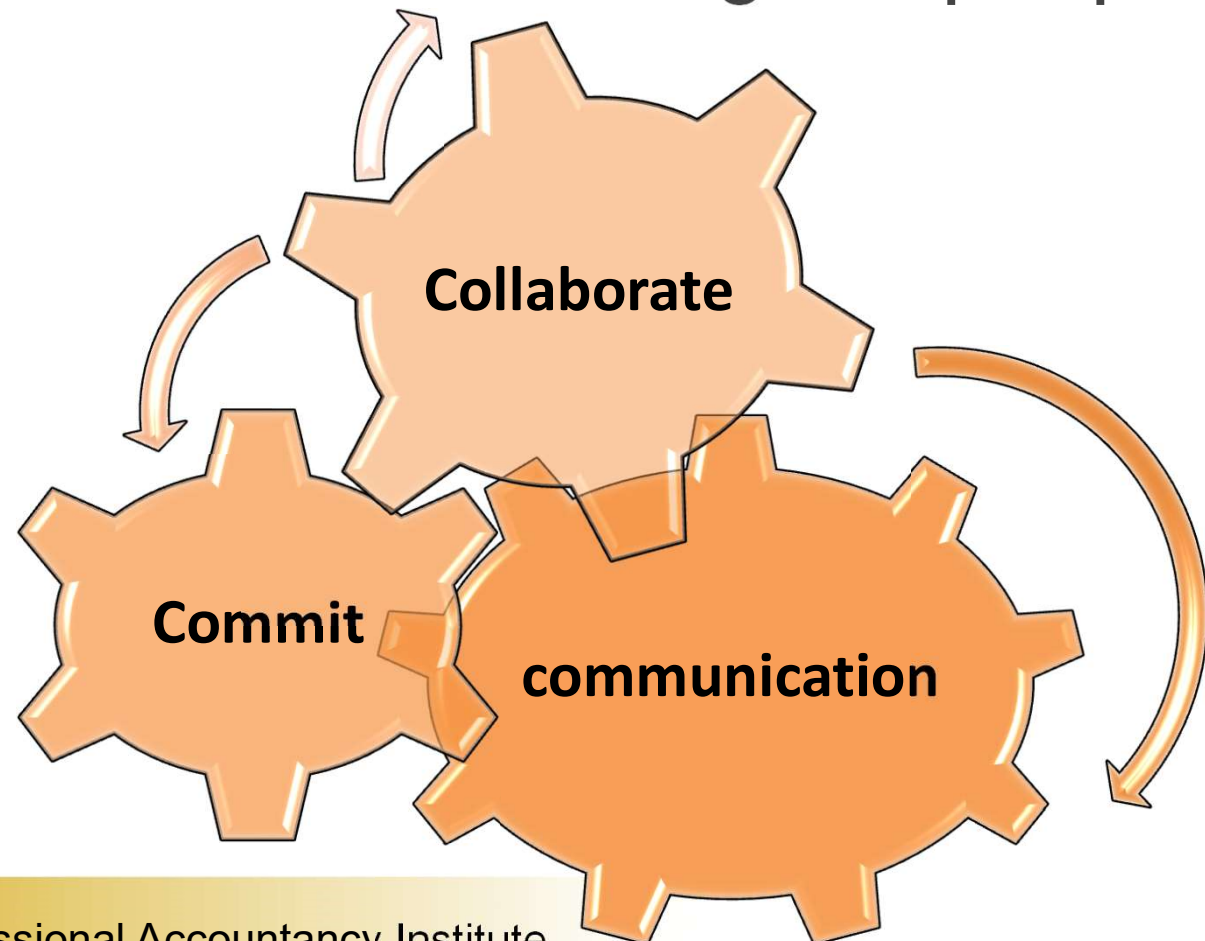
You don't have
answers to all
questions, learn
and re-learn

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3 C's of Change

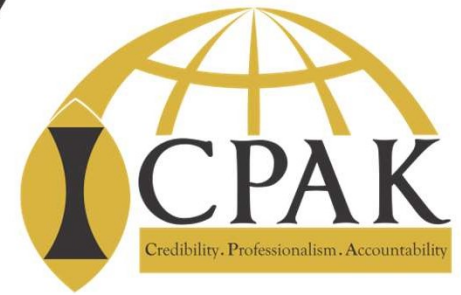


Leading the process, and leading the people.



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Independence & Governance



Auditors Independence:

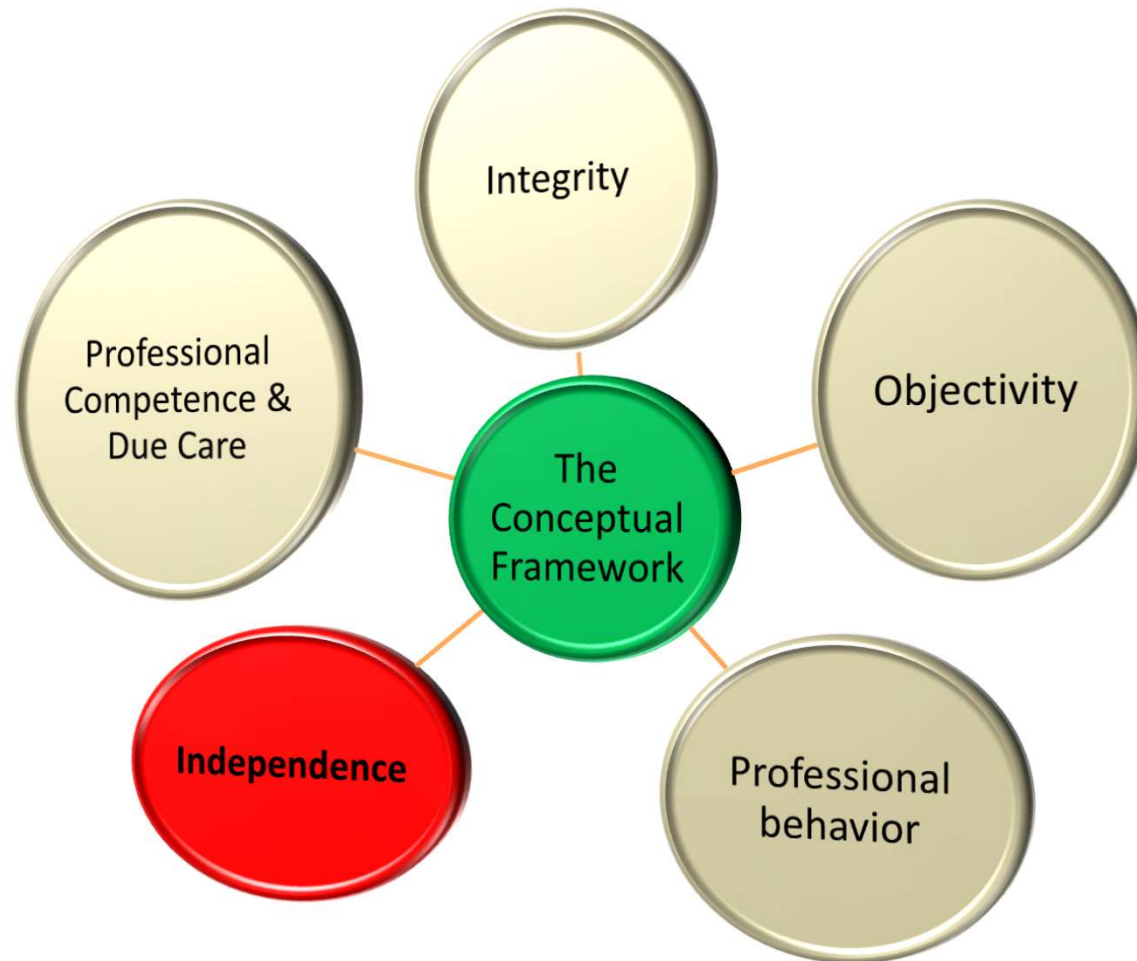
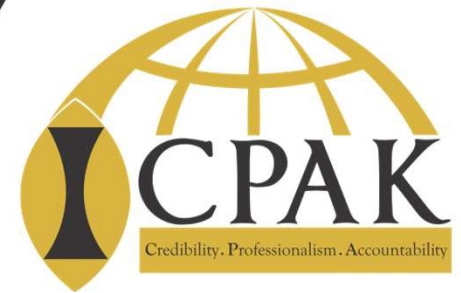
❑ An auditor independence is “freedom from those factors that compromise, or can reasonably be expected to compromise, an auditor’s ability to make unbiased audit decisions”.

‘independence in mind’ and ‘independence in appearance’

❑ Threats to auditors independence: Self-Review, self-interest, advocacy, familiarity (trust) and intimidation.

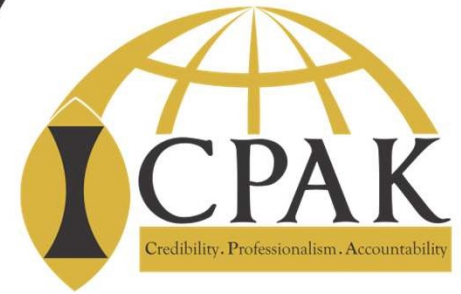
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International Code of Ethics for Professional Accountants

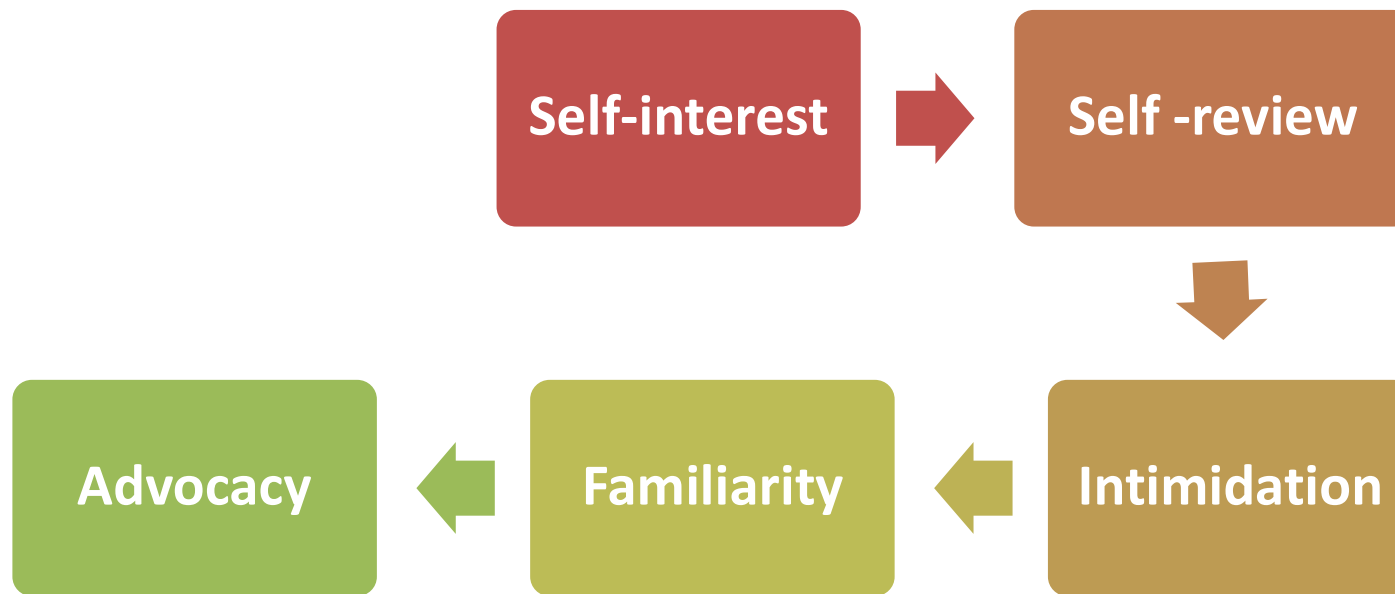


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International Code of Ethics for Professional Accountants

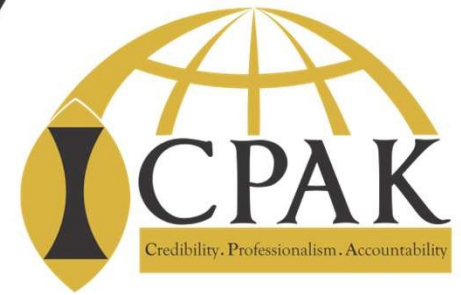


- **Threats to Auditors Independence**

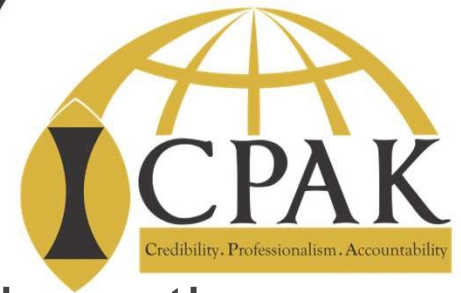


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Governance Framework



Governance

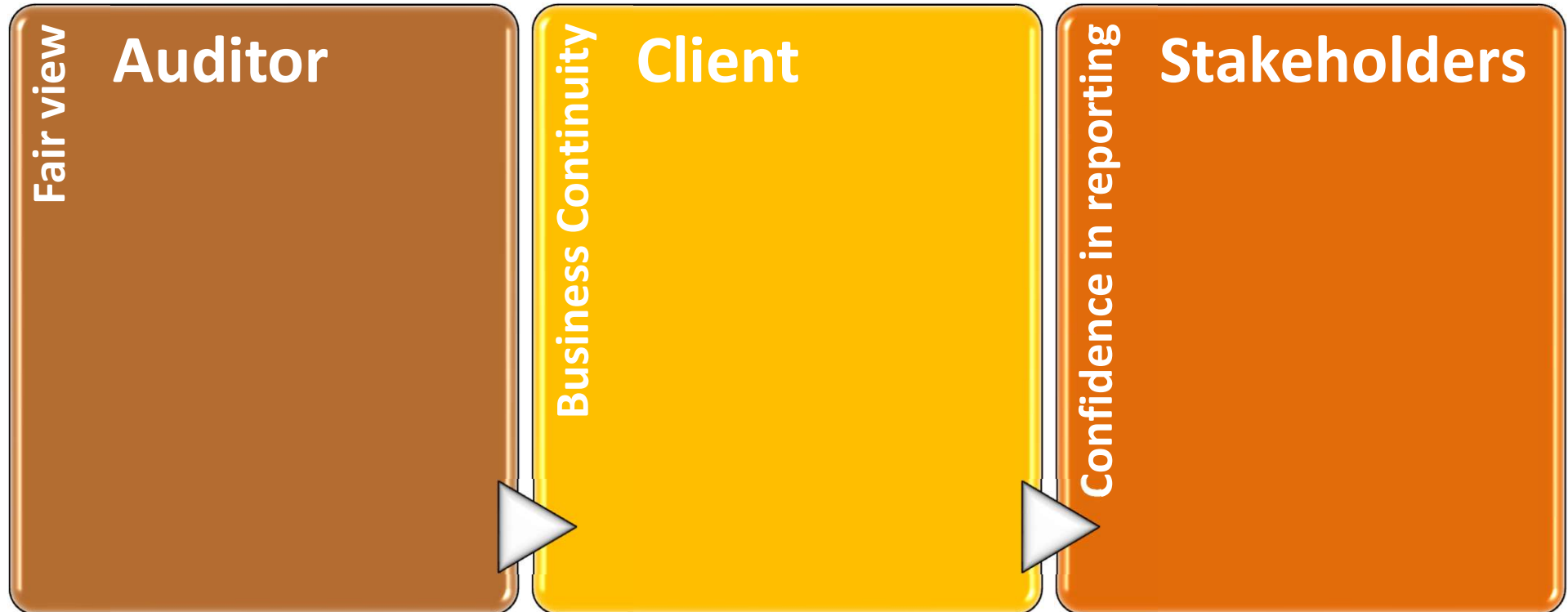
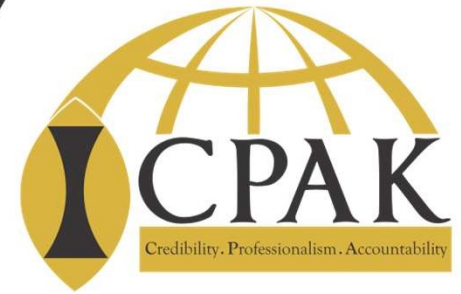


Governance refers to the structures, systems, and practices an organization has in place to:

- assign decision-making authorities, define how decisions are to be made, and establish the organization's strategic direction; **(Oversight)**.
- oversee the delivery of its services; the implementation of its policies, plans, programs, and projects; and the monitoring and mitigation of its key risks; and **(Management)**.
- report on its performance in achieving intended results and use performance information to drive ongoing improvements and corrective actions. **(All stakeholders)**.

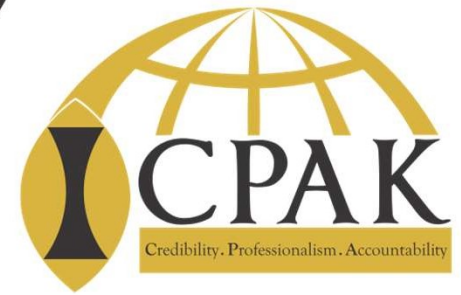
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Independence & Governance



External audit is an attest function carried out by an unbiased and independent person, aimed at providing comfort to users of audited financial statements of organisations, that those statements can be relied upon.

Emerging Governance Issues



- Stakeholder engagement-Staying up to date
- Change of policy frameworks – communication, meetings, employee engagements
- Robust risk assessments and review of risk appetites
- Emerging fraud trends
- Redefining and redesigning processes

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Going Concern Considerations (ISA 570)

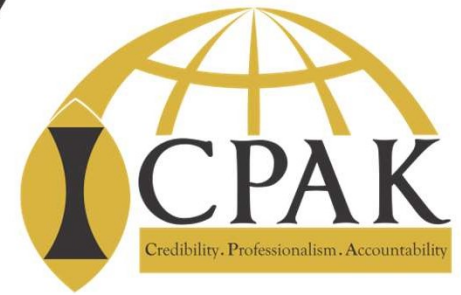


- ❑ Going Concern is the assumption that an entity will remain in business for the foreseeable future (not less than 12 months).
- ❑ *This means the entity will not be forced to halt operations and liquidate its assets in the near term at what may be very low fire-sale prices.*
- ❑ **Critical Question:** What is the auditor's responsibilities in the audit of financial statements relating to going concern and the implications for the auditor's report.?

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How Have Organizations Reacted?

COVID-19 Crisis & Going Concern



- SMEs & MSMEs closed businesses/ changed operations
- Retrenchments
- Pay cuts/ unpaid leave
- Restructuring
- Use of technology
- Profit warning/ cautionary statements

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How Have Organizations Reacted?

Profit warning/ cautionary statements



2020

- StanChart
- Nation Media
- Britam Holdings
- KPLC
- Kenya Orchards
- Kenya Airways
- Etc etc

2019

- Kenya Airways
- NSE
- CIC Group
- Standard Group
- Kenya Orchards
- EA Portland Cement
- Unga Group
- Etc etc

CMA Guidelines on profit warning: Anticipated drop in profits by 25%
What about SMEs and MSMEs?

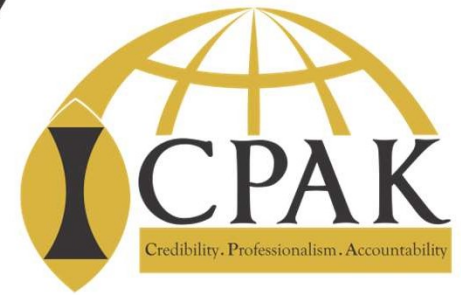
Objectives of the Auditor on Going Concern.



1. To obtain **sufficient appropriate audit evidence** regarding, and conclude on, the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements;
2. To conclude, based on the audit evidence obtained, whether a **material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern**; and,
3. To report in accordance with this ISA and other applicable ISAs.

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Risk Assessment Procedures and Related Activities



Consider whether **events** or **conditions** exist that may **cast significant doubt** on the entity's ability to continue as a going concern.

- a) If such an assessment has been performed by the management, discuss **management's plans to address them**;
- b) If such an assessment has not yet been performed, discuss the **basis for the intended** use of the going concern basis of accounting, and inquire whether events or conditions exist that, may cast significant doubt on the entity's ability to continue as a going concern

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Additional Audit Procedures When Events or Conditions Are Identified



- ❑ Request management to make its assessment.
- ❑ Evaluate management's plans for future actions to see if they are likely to improve the situation
- ❑ Request written representations from management and, those charged with governance
 - Banks
 - Suppliers
 - Key customers

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Additional Audit Procedures When Events or Conditions Are Identified



- ❑ Where the entity has prepared a cash flow forecast,
 - 1) Evaluating the reliability of the underlying data generated to prepare the forecast;
 - 2) Determining whether there is adequate support for the assumptions underlying the forecast.

Additional Audit Procedures: Considerations for Smaller Entities



Unique Observations

- ☐ Lack detailed financial analysis
- ☐ Business owners know the business in-out.
- ☐ Inability to withstand adverse conditions.
- ☐ Able to respond quickly to exploit opportunities
- ☐ Lack reserves to sustain operations

Risks

1. Banks and other lenders may cease to support the entity
2. Possible loss of a principal supplier, major customer, key employee, or the right to operate under a license, franchise or other legal agreement.
3. Inability to maintain critical human capital
4. Abrupt closure

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Additional Audit Procedures: Considerations for Smaller Entities

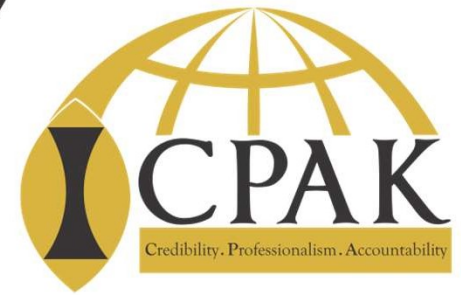


Responding to various risks for smaller entities

- ☐ Discuss the **medium** and **long-term** financing of the entity with management, provided that management's contentions can be corroborated by **sufficient documentary evidence** and are **not inconsistent** with the auditor's understanding of the entity.
- ☐ Where a small entity is largely financed by a loan from the owner-manager, it may be important that these funds are not withdrawn

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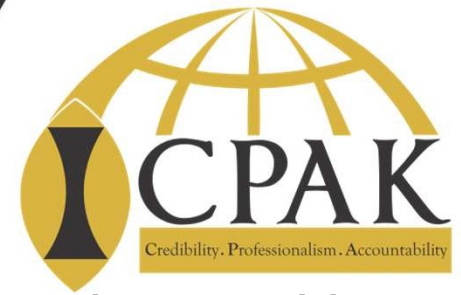
Governance Considerations



1. **Depth of analysis** • Is the analysis performed by management sufficiently detailed and is it based on a robust assessment of the operating and financial exposures arising from COVID-19 that the entity has been or may be impacted by?
2. **A range of scenarios** • Does the going concern analysis effectively combine available cash with a range of scenarios including a reasonable worst-case scenario to allow directors to conclude on the going concern assessment?
3. **Internal modelling consistency** • Where appropriate, are cashflow estimates used in the going concern analysis consistent with those used for establishing or supporting balance sheet values (e.g. impairment and deferred tax)? • Are the key assumptions underlying the cash flows supportable and reasonable?

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Governance Considerations



4. **External disclosure consistency** • Is the analysis consistent with recent market disclosure including Directors' Reports and Investor presentations?
5. **Going concern basis adoption** • Does analysis suggest that, on balance, it is reasonable to conclude that the entity has the ability to continue as a going concern?
6. **Documentation** • Is the board analysis and challenge of management's analysis supporting the assessment of the going concern basis appropriately documented as evidence of that challenge?
7. **Disclosure when material uncertainties exist** .Do disclosures detail management's plans or options available to them, either within or outside their control, to mitigate the effect of the events or conditions, the status of any plans and the interdependency of these plans or options?

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The Way Forward Going Concern Evaluation Items



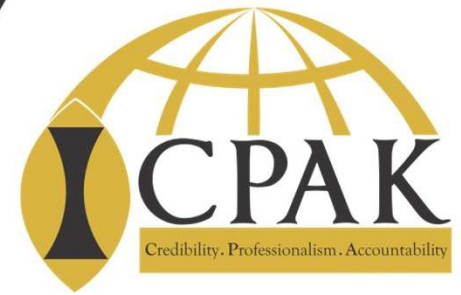
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- ☐ The auditor should cover the same period as that used by management to make its assessment.
- ☐ Evaluate robustness of disclosures in the financial statements.
- ☐ Evaluate negative trends in operating results, such as a series of losses.
- ☐ Evaluate loan defaults by company.
- ☐ Evaluate Denial of trade credit to the company by its suppliers.

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The Way Forward

Going Concern Evaluation Items



- ☐ Consider uneconomical long-term commitments to which the company is subjected to.
- ☐ Evaluate existing and future legal proceedings against the company.
- ☐ Consider change in senior management and at the board level.
- ☐ Consider relevant regulatory guidance.
- ☐ Evaluate the process management followed to make its assessment, the assumptions on which the assessment is based and management's plans for future action and whether management's plans are feasible in the circumstances.

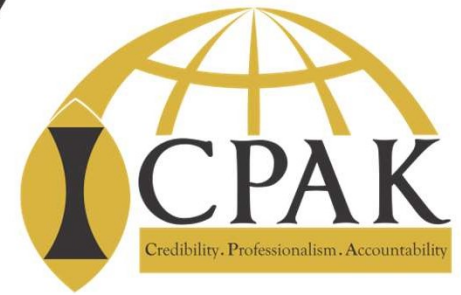
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Auditors Opinion



Material Uncertainty Related to Going Concern	<p>We draw attention to Note xx in the financial statements, which indicates that the Company incurred a net loss of xxx during the year ended December 31, 20X1 and, as of that date, the Company's current liabilities exceeded its total assets by xxx. As stated in Note xx, these events or conditions, along with other matters as set forth in Note xx, indicate that a material uncertainty exists that may cast significant doubt on the Company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.</p>
Key Audit Matters	<p>Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In addition to the matter described in the Material Uncertainty Related to Going Concern section, we have determined the matters described below to be the key audit matters to be communicated in our report.</p> <p>[Describe each key audit matter in accordance with ISA 701.]</p>

Conclusion



“The pessimist complains about the wind; the optimist expects it to change; the realist adjusts the sails.”

” William Arthur Ward”



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THANK YOU



EXAMPLES

1. Key audit matters ... In addition to the matter described in the material uncertainty related to going concern section, we have determined the matters described below to be the key audit matters to be communicated in our report.
2. Key audit matters..... Except for the matter described in the material uncertainty related to going concern section, we have determined that there are no other key audit matters to be communicated in our report.

EXAMPLES

Conclusions relating to principal risks, going concern and viability statement

1. Apart from the impact of the matters disclosed in the material uncertainty related to going concern section, we have nothing to report in respect of the following information in the annual report, in relation to which the ISAs require us to report to you whether we have anything material to add or draw attention to:
 - the disclosures in the annual report [set out on page ...] that describe the principal risks and explain how they are being managed or mitigated;
 - the directors' confirmation [set out on page ...] in the annual report that they have carried out a robust assessment of the principal risks facing the company, including those that would threaten its business model, future performance, solvency or liquidity;