

Tutorial letter 105 Evaluation, Conclusion and Reporting



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Agenda

- Subsequent events
- Going concern
- Misstatements
- Audit opinions and reports
- Reporting on other engagements
- Review engagements
- Agreed upon procedures
- Compilation engagements

Subsequent Events

ISA 560

Deals with the **auditors responsibility** relating to subsequent events in an audit of financial statements

Subsequent Events

- The financial statements **may be affected by certain events** that occur after the date of the financial statements
- These **events** include:
 - Adjusting events (Conditions existing at year-end)
 - Non-adjusting events (Conditions arising after year-end)

Subsequent Events

The auditor gives an **opinion** on the fair presentation of the annual financial statements (AFS),

i.e. Whether the AFS are free from material **misstatement** or not

Thus where Subsequent events exist, adjustment or disclosure is required in the AFS otherwise it will lead to the AFS containing **misstatement** which could affect the audit **opinion**.

Subsequent Events

The objectives of the auditor are:

1. To obtain audit evidence about whether events that require adjustment of or disclosure in the AFS are **appropriately reflected in those AFS**
2. Respond to facts which become known to the auditor after the date of the auditors report
(Refer to Para 4 of ISA 560)

Subsequent Events

Year-End Date	AFS Approval Date	Auditor Report Date	AFS Issue Date
30 June 2015	1 July 2015	10 July 2015	1 August 2015
Refer to the definition in paragraph 5.	Refer to the definition in paragraph 5.	The auditor is expected to gather audit evidence up to the date of the audit report therefore the auditor has an obligation to perform audit procedures. (Para 6-9)	The auditor has no obligation to perform audit procedures
Co. act Sec 27 Financial year-end of companies		However if situations arise after the report date but before the AFS are issued, the audit may be required to perform additional procedures. (Para 10-13)	However if situations arise after the AFS are issued, the auditor may have to ensure that reliance is not placed on the report (Para 14-17)

Subsequent Events

Events occurring between the date of the financial statements and the date of the auditors report (Para 6-9)

- Auditor has an obligation to perform audit procedures
- If as a result of the procedures performed the auditor identifies subsequent events, the auditor shall determine whether such events is appropriately reflected in those AFS

Subsequent Events

Facts which become known to the auditor after the date of the auditors report but before the date the AFS are issued (Para 10-13)

- No obligation to perform any audit procedures
- If client amends AFS, perform procedures on amendments and issue a new report

Remember to consider the circumstances in Para 12 and 13

Subsequent Events

Definitions: (Para 5 of ISA560)

- **Date of financial statements:** Date of the end of the latest period covered by the AFS
- **Date of auditor report:** Date the auditor dates the report on the AFS
- **Subsequent Events:** Events occurring between the date of the financial statements and the date of the auditors report, and facts that become known to the auditor after the date of the auditors report

Subsequent Events

Facts which become known to the auditor after the AFS have been issued (Para 14-17)

- No obligation to perform audit procedures
- If client amends AFS, perform procedures on amendments and issue a new report
- Inform those who wish to rely on the audit report of the situation.
- Refer to SAAPS 3 page 34 for an illustration of an audit report that is amended due to the AFS being amended after the initial issue thereof.

Subsequent Events

- **ISA 560:** Provides the **guidelines for the auditors responsibility regarding subsequent events** which includes the procedures the auditor can perform to identify such events. If any such events are identified, the auditor will determine if management has made the necessary changes in accordance with IAS10
- **IAS 10:** Provides the **accounting rules should subsequent events be identified**. Management should make the changes to the AFS as necessary whilst the auditor should ensure that these changes comply with the IAS and that the AFS are fairly presented

Going Concern

Going Concern Assumption: An entity is viewed as continuing in business for the foreseeable future

General purpose financial statements are prepared on a going concern basis

Assets and liabilities are recorded on the basis that the entity will be able to realize its assets and discharge its liabilities in the normal course of business
(Para 2)

Going Concern

Managements responsibility:

IAS 1 requires management to make an assessment of an entity's ability to continue as a going concern (Para 3)

The assessment involves making a judgement, at a particular point in time about inherently uncertain future outcomes of events or conditions (Para 5)

Going Concern

The objectives of the auditor are:

1. To obtain audit evidence regarding the appropriateness of managements use of the going concern assumption in preparing the AFS
2. To conclude whether a material uncertainty exists that may cast doubt on the entity's ability to continue as a going concern.
3. To determine the implications for the audit report

Going Concern

Planning Phase:

- Perform risk assessment procedures and consider whether there are **events or conditions** that may cast doubt on the entity's ability to continue as a going concern
- Determine if management already performed a preliminary assessment of the entity's ability to continue as a going concern
- 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 concern

Going Concern Indicators

Events or conditions that may cast doubt on the entity's ability to continue as a going concern (Para A2)

- **Financial** events or conditions
- **Operating** events or conditions
- **Other** events or conditions

Going Concern

Audit procedures when events or conditions are identified:

- The auditor must obtain evidence to determine whether or nor a material uncertainty exists
- Including considering mitigating factors

Para 16 and A15

Going Concern

Audit Conclusions and reporting:

The auditor will use his judgement and evidence obtained to conclude whether a material uncertainty exists relating to events or conditions that **individually** or **collectively** may cast doubt on the entity's ability to continue as a going concern. (**Para 17**)

Going Concern

Going concern assumption appropriate but a material uncertainty exists

The auditor shall determine whether the AFS:

- Adequately describe the event that may cast doubt on the entity's ability to continue as a going concern and managements plans to deal with these events
- Disclose clearly that a material uncertainty exists and therefore the entity may be unable to realize its assets or discharge its liabilities in the normal course of business

Going Concern

Going concern assumption appropriate but a material uncertainty exists:

- If adequate disclosure is made the auditor shall express an unmodified opinion including an emphasis of matter paragraph (Para 19)
- Include a separate section with the heading "**Material Uncertainty Related to Going Concern**".
- **Key Audit Matters section:** include reference to the "**Basis for Opinion**" para where the matter is stated.
- If adequate disclosure is not made, the auditor shall express a qualified or adverse opinion. (ISA 570 (revised) par 23 and par A.32: illustrative example 2)

Going Concern

Use of going concern assumption inappropriate:

If the AFS are prepared on the going concern basis, but in the auditors judgement this basis is inappropriate, the auditor shall express an adverse opinion (**ISA 570 (revised) Par 21**)

Going Concern

Management unwilling to make or extend its assessment

The auditor shall consider the implications for the audit report

Going Concern

Communication with TCWG

The auditor shall communicate with TCWG events or conditions that may cast doubt on the entity's ability to continue as a going concern.

The communication shall include:

- If events or conditions constitute a material uncertainty
- If the use of the going concern assumption is appropriate in preparation of the AFS
- The adequacy of related disclosures in the AFS

Going Concern

Factual Insolvency

- Liabilities > Assets fairly valued (S4 Co.act)
- An indicator but does not necessarily mean a going concern problems exists
- If trading under these conditions:
 - Possible reckless trading (S22)
 - Possible RI (S45 APA)
- Can be mitigated by a subordination agreement

Commercial Insolvency

- Cannot pay debts even if assets > liabilities (S4 Co.act)
- Stronger indicator for **likely** going concern problems
- The company's working capital cycle is impaired thus affecting its ability to trade

Going Concern

SAAPS 3

- Provides illustrative examples of audit reports modified by going concern issues (Page 36-43)
- Provides a decision tree for linking going concern considerations with types of audit opinions (Page85-86): **See TL105**

Going Concern

Exam Technique:

- You may be required to **evaluate** whether the use of the going concern assumption is appropriate. (You discuss both the applicable indicators as per ISA 570 (revised) and mitigating factors, and conclude)
- **Concerns** regarding the going concern principle. (You discuss just the indicators.)

Going Concern

Exam Technique:

- Further audit procedures when there is a material uncertainty relating to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. (You base your procedures on the information in the scenario and make the procedures per ISA 570 (revised) applicable.)
- Explain the impact on the auditor's report, when a company is not a going concern. (To answer this you would use the decision tree in SAAPs 3 page 85-86.)

Misstatements

ISA 450

Deals with the auditor responsibility to evaluate the effect of **identified misstatements** on the audit and of **uncorrected misstatements** if any on the financial statements

Misstatements

The objective of the auditor is to evaluate:

- The effect of identified misstatements on the audit; and
- The effect of uncorrected misstatements, if any, on the financial statements
(Para 3)

Misstatements

Definitions: (Para 4)

- **Misstatement:** A difference between a reported financial statement item and an item to be in accordance with the applicable financial reporting framework. **A misstatement arises from error or fraud**
- **Uncorrected Misstatement:** Misstatements that the auditor accumulates during an audit that is not corrected

Misstatements

Accumulation of Identified misstatements:

The auditor shall accumulate misstatements identified during the audit, other than those that are clearly trivial.(Para 5)

The auditor may determine an amount below which misstatements would be clearly trivial and if accumulated would still not have a material effect on the financial statements (Para A2)

Misstatements

Consideration of identified misstatements as the audit progresses: (Para 6-7)

- Determine if the audit strategy and plan needs to be revised
 - The nature and circumstance of misstatements indicate that other misstatements may exist
 - The aggregate of misstatements approaches materiality
- If management examines an account and corrects misstatements on the auditors request, the auditor must still perform additional procedures to determine whether misstatements remain.

Misstatements

Communication and correction of misstatements (Para 8-9)

- The auditor shall communicate all misstatements accumulated and request management to correct those misstatements
- If management refuse to correct the auditor shall:
 - Understand managements reason for not correcting
 - Evaluate if the AFS are free from material mistatement

Misstatements

Evaluating the effect of uncorrected Misstatements:

- First reassess materiality to confirm if it remains appropriate
- Then auditor determines if uncorrected misstatements are material, individually or in aggregate. The auditor shall consider:
 - The size and nature of the misstatement
 - Effect of uncorrected misstatements relating to prior periods

Misstatements

Communication with TCWG: (Para 12-13)

- Auditor shall communicate with TCWG uncorrected misstatements **and** the effect that they, individually or in aggregate have on the opinion in the auditors report. **(Including those of prior periods)**
- The auditor shall communicate each material uncorrected misstatement individually
- The auditor shall request that uncorrected misstatements be corrected

Misstatements

Documentation: (Para 15)

The auditor shall include in the audit documentation:

- Amounts below which misstatements are regarded as clearly **trivial**
- All misstatements accumulated on the audit and if corrected
- If uncorrected misstatements are material, individually or in aggregate and the basis for that conclusion

Misstatements

Types of questions that may be asked

- Discuss the effect of the **misstatements** identified on the **financial statements**.
- Discuss the effect of the **misstatements** identified on the **audit opinion / report**

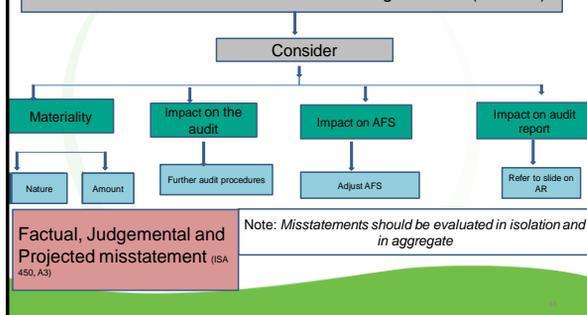
Misstatements

Exam Technique:

- When answering a question on misstatements, always determine if a materiality figure is given, if not calculate this figure.
- A misstatement can be either quantitative (Amounts) or qualitative (nature) and should be considered individually or in aggregate
- Remember that we are concerned with the net effect of differences on the AFS

Framework for answering a misstatement question

Evaluation of misstatements identified during the audit (ISA 450)



Audit Reports and Opinions

In terms of ISA 200, the **overall objectives** of the auditor are to:

- Obtain reasonable assurance about whether the AFS are **free from material misstatement**, thereby enabling the auditor to **express an opinion**; and
- To report on the AFS in accordance with the auditors findings

New and Revised Audit Report

- IRBA Board has approved for adoption, issue and prescription by Registered Auditors in South Africa the following IAASB pronouncements:
 - [ISA 700 \(Revised\), Forming an Opinion and Reporting on Financial Statements](#);
 - [ISA 701, Communicating Key Audit Matters in the Independent Auditor's Report](#);
 - [ISA 705 \(Revised\), Modifications to the Opinion in the Independent Auditor's Report](#);
 - [ISA 706 \(Revised\), Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report](#);
 - [ISA 570 \(Revised\), Going Concern](#);
 - [ISA 260 \(Revised\), Communication with Those Charged with Governance](#); and
 - [Related Conforming Amendments to other ISAs](#).

New and Revised Audit Report

- Significant changes between the old Audit Report and the New and Revised Audit Report:
 - **New requirement for listed entities to include the name of the engagement partner in the auditor's report**
 - **Ability to include the auditor's responsibility paragraph on the website of an appropriate authority**

Key Audit Matters ISA 701 (new)

- Those matters that, in the auditor's professional judgement, were of **most significance in the audit** of financial statements of the current period.
- **The auditor shall take the following into account when determining which matters are key audit matters:**
 - Matters which required *significant auditor attention* in performing the audit.
 - Areas of *higher assessed risk* of material misstatement or *significant risks* identified.
 - Matters which required *significant auditor judgement* that also involved *significant management judgement*, including *accounting estimates*.
 - *Accounting estimates* that have been identified as having *high estimation uncertainty*.
 - The effect on the audit of *significant events or transactions* that occurred during the period.
 - Based on the auditor's judgement about which *matters were of most significance* in the audit.
 - Matters that *pose challenge to the auditor* in obtaining sufficient appropriate audit evidence.
 - Areas of *complexity* and *significant management judgement* (accounting estimates) may need to *involve experts*.

NOTE: *Significant risks are often areas that require significant auditor attention.*

Audit Opinions and Reports

ISA 700 (revised)

- Deals with the auditors responsibility to form an opinion on the AFS including the form and content of the auditors report
- This ISA promotes consistency in the auditors report
- Deals with an unmodified (Unqualified) opinion (i.e. The AFS are fairly presented in all material respects)

Audit Opinions and Reports

ISA 700 (revised)

- Refer to the appendix within the ISA for examples of an auditor report
- **NB: Only Give the opinion paragraph**, not expected to write out the entire audit report.

Audit Opinions and Reports

ISA705 (revised)

- Deals with the auditors responsibility to issue an appropriate report where the auditor concludes that a modification to the opinion is necessary
- This ISA establishes 3 types of modified opinions, namely "Qualified" "Adverse" and "Disclaimer" of opinion.

Audit Opinions and Reports

ISA 705 (revised)

Qualified Audit Opinion

- Auditor concludes that **misstatements**, individually or in aggregate **are material but not pervasive**
- **Except for** the matters described in the basis for qualified opinion paragraph, the financial statements are **fairly presented**

Audit Opinions and Reports

ISA 705 (revised)

Qualified Audit Opinion

- Refer to the appendix, specifically illustration 1 and 3 for an example of a qualified audit opinion
- Take note that an additional paragraph has been included “Basis for qualified opinion” before the opinion paragraph which results in the modification to the standard audit report as seen in ISA 700

Audit Opinions and Reports

ISA 705 (revised)

Adverse Audit Opinion

- The auditor concludes that misstatements, individually or in aggregate are both **material and pervasive**.
- Thus the auditor concludes that the AFS as a whole are not fairly presented (Remember that the misstatements are **pervasive**)

Audit Opinions and Reports

ISA 705 (revised)

Adverse Audit Opinion

- Refer to the appendix, specifically illustration 2 for an example of an adverse audit opinion
- Again take note that an additional paragraph has been included “Basis for Adverse opinion” before the opinion paragraph which results in the modification to the standard audit report

Audit Opinions and Reports

ISA 705 (revised)

Disclaimer Audit Opinion

- The auditor shall disclaim an opinion when the auditor is **unable to obtain audit evidence or where multiple uncertainties exist** it is not possible to form an opinion.
- NB: Misstatements are both **material and pervasive**.
- A disclaimer ultimately means that the auditor **expresses no opinion on the financial statements**

Audit Opinions and Reports

ISA 705 (revised)

Disclaimer Audit Opinion

- Refer to the appendix, specifically illustration 4 and 5 for an example of a disclaimer audit opinion
- Again take note that an additional paragraph has been included “Basis for Disclaimer opinion” before the opinion paragraph which results in the modification to the standard audit report

Audit Opinions and Reports

ISA 706 (revised)

- Deals with additional communication in the auditors report when the auditor considers it necessary such as:
 - Emphasis of matter paragraph
 - Other matters paragraph
- This ISA deals with a **modification to the auditors report but not a modification to the auditors opinion** as in ISA 705

Audit Opinions and Reports

ISA 706 (revised)

Emphasis of matter paragraph:

- Is included below the opinion paragraph
- Used to **draw users attention** to a **matter disclosed or presented in the AFS** that in the auditors judgement is fundamental to a users understanding.
- Only emphasis information disclosed in the AFS

Audit Opinions and Reports

ISA 706 (revised)

Emphasis of matter paragraph

- Must indicate that the audit opinion is not modified in respect of the matter emphasized
- Refer to appendix 3 for an example of an audit report with an emphasis of matter paragraph included

Audit Opinions and Reports

ISA 706 (revised)

Other matter paragraph:

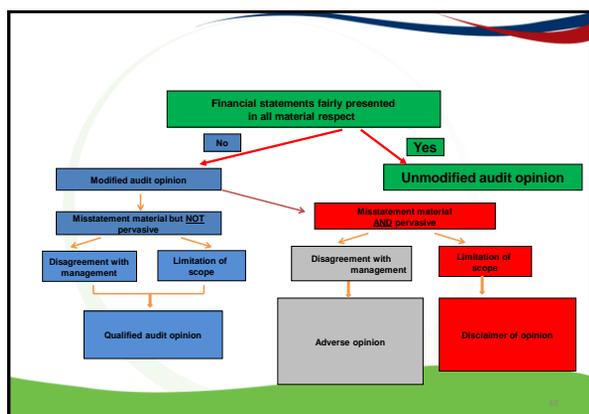
- Is included below the opinion and emphasis of matter paragraph if included
- It **emphasizes information not required to be disclosed in the AFS**, but in the auditors judgement is relevant to a users understanding of the audit

Audit Opinions and Reports

ISA 706 (revised)

Other matter paragraph:

- Normally disclose a reportable irregularity if reported to IRBA under this paragraph



Reporting on other engagements

- An auditor is often requested to report on other types of engagements, however this discussion will be limited to the following engagements:
- Review Engagements (ISRE2400 and ISRE 2410)
- Agreed upon procedure engagements
- Compilation

Reporting on other engagements

Review Engagements:

- Deals with the practitioners responsibilities when engaged to perform a review of historical financial statements when the practitioner **is not the auditor**.
- The practitioners objective in a review is to obtain **limited assurance** about whether the AFS as a whole is free from material misstatement.

Reporting on other engagements

Review Engagements:

- The auditor primarily performs **inquiry** and **analytical procedures** to obtain audit evidence
- Limited assurance is expressed as follows:
“ Nothing has come to our attention that causes us to believe that the financial statements are not fairly presented”

Reporting on other engagements

Review Engagements:

- The auditor provides limited assurance as opposed to reasonable assurance
- We provide limited assurance because we perform limited procedures
- Remember that the companies act requires some companies to be independently reviewed which will be done in accordance with this ISA
- Refer to ISRE 2400, Appendix 2 for examples of a review report

Reporting on other engagements

Limited assurance	Reasonable assurance (ISA 700)
<ul style="list-style-type: none"> • Procedures are limited • Assurance expressed as a negative “ Nothing came to our attention” • Engaged to review the AFS 	<ul style="list-style-type: none"> • Procedures are not Limited • Assurance expressed as a positive” In our opinion” • Engaged to audit the AFS

Reporting on other engagements

Agreed upon procedures ISRS 4400

The objective of an agreed-upon procedures engagement is for the auditor to carry out procedures of an audit nature to which the **auditor and the entity and any appropriate third parties have agreed** and to **report on factual findings**

Reporting on other engagements

Agreed upon procedures:

- The auditor provides a **factual findings report**
- **No** assurance is expressed
- Thus users must assess the report themselves and draw their own conclusions from the auditors work

Reporting on other engagements

Agreed upon procedures:

- The **report is restricted only to those parties that have agreed to the procedures.**
- The agreed upon procedures that the auditor performs may include any of the procedures as discussed in ISA 500
- The auditors right of **access to information is limited** in order to fulfill the engagement requirements.

Reporting on other engagements

Agreed upon procedures

- Where additional procedures are required, this must first be agreed upon by all parties.
- Refer to **ISRS 4400 Appendix 2 for an example** of a factual findings report

Compilation Engagement

ISRS 4410

Deals with the practitioners responsibilities when engaged to **assist management with the preparation and presentation of historical financial information** without obtaining any assurance on that information

Management retains responsibility for the financial information and the basis on which it is prepared and presented

Compilation Engagement

- No testing is conducted and no assurance is given in the report
- Ordinarily includes the preparation of financial statements
- May also include the collection, classification and summarization of other financial information
- Refer to **ISRS 4410 appendix 2** for an example of a compilation report.