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Auditing, Reporting & Compliance

NEWS

Remote Auditing Challenges and How to Overcome Them

and other information from the ARC segment

Newsletter
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Editorial

Dear GGI friends and colleagues

Welcome to this new edition of the GGI Auditing, Reporting & Compliance Practice Group newsletter. I am very delighted to thank the contributors to this newsletter for their articles in these unprecedented times.

The coronavirus pandemic has impacted all of our lives and, from a professional perspective, the financial situation of our clients. Audit procedures have to be reassessed when meeting in person becomes challenging and sometimes even impossible. As a result, the coronavirus pandemic is one of the major topics covered in several highly interesting articles; for example, how do we set audit risk, going concern, or determine potential need for impairment of assets? This goes along with governments providing varying financial and fiscal support to companies within different countries. In this context, many of our GGI member firms are involved in helping clients through these troubled times.

Beyond that, the German government, as well as the accounting and auditing world, has been shocked by the fraudulent activities surrounding the insolvent Wirecard AG, formerly listed in the German DAX 30, the leading index of the German stock market. The public trust in auditors and overseeing institutions has been negatively impacted. The investigation is still under way, but the question is, how can this happen to a member of our profession? It is very likely that the German profession will be more intensely regulated in the upcoming years. This coincides with new ethics rules issued in the UK surrounding scandals of the Big Four.

On a personal note, I hope you find yourself in good health and that you can lead your personal practices safely through these challenging times. I will be more

than delighted to meet you again during one of the next conferences or in one of the upcoming webinars.

All the best to you and your families.

Kindest regards,

Boris Michels
Global Chairperson of the GGI Auditing, Reporting & Compliance Practice Group

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Remote Auditing Challenges and How to Overcome Them

By Paul Speidel

Gathering sufficient audit evidence in a remote audit environment is requiring auditors to be creative and to implement new techniques. Physical examinations, inspections, and observations are still required by auditing standards. Also, the auditor is still required to develop an understanding of the controls pertaining to the major transaction cycles and accounting processes, perform fraud interviews, make physical inventory observations, and perform other tasks traditionally done in person.

Audit insight previously obtained by looking over a client's shoulder as they perform a task, or reading facial expressions and body language when responding to inquiries, are more challenging in a remote environment. The COVID-19 pandemic has affected most clients, both financially and in how they conduct their businesses. These changes must be addressed when assessing audit risks in planning the audit.

Performing an audit remotely will require increased and new uses of technology. Technology often used for meetings such as Webex, Zoom, etc, may be used in performing audit procedures. Use of live-streaming video and drones may be necessary for physical inventory observations.

Determining the technological tools currently in use by both the auditor and the client, or that can easily be obtained and implemented, is necessary to effectively plan and perform the audit. Technology solutions for the following must be considered:

- Auditor access to the client's accounting system;
- How to transfer documents between the client and the auditor;
- Conducting meetings where seeing each other is important;
- How to perform walk-throughs of the significant transactions cycles;
- How to observe inventory.

When assessing audit risk, the documentation of the auditor's understanding of the client's major accounting transaction cycles and the related internal control processes and systems are more challenging in a remote environment. Factors to consider include:

- Did the client's office close?
- Were or are some of the client's staff working remotely?
- Have the processes or procedures changed either temporarily or permanently?
- Have tasks been temporarily reassigned?
- What is the effect of any changes in the processes and procedures on internal controls?

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Paul Speidel brings over 35 years of experience in public accounting, working with companies in various industries. He manages client relationships and attest engagements, performs pre-issuance financial statement reviews, and participates in the firm's internal inspection and peer reviews.

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- Were there different processes for periods of time when the office was closed or when certain staff were working remotely?

If there were different processes in place throughout the audit period, the auditor should document their understanding of the controls for each major transaction cycle for each portion of the year. Based on their understanding of the processes and procedures, audit risks should be considered for each period and process, and potentially, audit procedures developed that are different or expanded for portions of the year.

Professional standards require a physical observation of a client's inventory; however, the standards do not require a physical presence or prohibit performing the observation remotely. To perform an inventory observation remotely, use of client personnel using video streaming is an option. One client staff can video stream while another performs test counts, with the video feed being observed by the auditor. The auditor can direct the client staff where to direct the video feed and instruct the client staff to open containers to view the contents as deemed necessary. For larger inventories or outdoor inventories, drones can be used to provide a video feed.

Addressing potential inventory obsolescence is particularly challenging when auditing remotely. Consider viewing a video feed of the client walking through each aisle of the warehouse. Any items that look to be slow moving should be considered for further testing.

Performing audits remotely requires careful consideration of how changes in the environment, and changes specific to each client, will impact the audit approach and procedures. Increased and creative use of technology to overcome these challenges is necessary to continue to perform quality auditing.

Post-Wirecard:

Wirecard Stands as a Major Global Business, Supervision, and Audit Failure

By Helmut Havenith

Supervisors and auditors agree on one point: fraud. As usual in the matter, the whipping post is ready and candidates to be tied there are abundant. Undeniably, there was something wrong with Wirecard's business and financial statements.

Probably both should remember that the existence of fraud or of fraudulent elements does not warrant an acquittal for sure.

The Supervisors debate the proper definition and allocation of areas of responsibility, the adequacy of means, staff, and authority, and the appropriate degree of initiative in an investigation process. The debate has a good chance of being spiced up by politics. For the time being, the writing on the wall concludes the need for reform – surprisingly, before we even know what went wrong.

The Auditors remain quiet, giving full cooperation and no reference to fraud. Audit professionals would have liked to learn from them on the latest developments in the profession: materiality levels, risk assessments and fraud risk assessments, understanding and testing of ICS, audit evidence.

The next reform to reinstate the credit of the profession is already written on the wall

In early July, the UK Big Four committed, after other failures, to implement, by 2024, the segregation between audit and advisory activities. Plans must be presented by the concerned by October; it is interesting to read that EY has said that the first proposals do not go far enough.

UK supervisors intend to strengthen the mid-sizers. Germany argues reforms.

The landscape has changed

Post-Enron reforms stayed “below expectations”. The European reform was particularly watered down after tremendous lobbying by the Big Four. Smaller firms stood behind their larger fellows, seeing an opportunity to join the “big” club. All others enjoyed somehow the limited impact.

Professional quality control shifted from self-regulation to public administration. Intensity and sanctions varied by country.

The debate on network versus association is ongoing. The underlying criteria are subject to interpretation. Slight changes in the definition criteria or their interpretation threaten today’s associations qualifying as networks. The impact: cost of clarifying the status; independence conflicts in substance or in appearance; cost of conflict identification; cost of insurance; loss of business; loss of members. Current networks now fully understand those costs.

COVID-19 uncertainties flood us with calls for laws, regulations, controls, state intervention, restrictions to entrepreneurship, and individual freedom. Measures that would have provoked revolutions a year ago are current money today. Activism rules.

Opportunities or first to overcome threats?

This time, smaller firms cannot accommodate sitting in the third row behind Big Four and mid-sizers.

The Big Four have their well-oiled marketing machines in place for the debates to come. Some Chinese walls in ownership are long anticipated. They will agree in defending their market position and share. They will strive to further increase costs for mid-sizers aiming at their clientele.

Mid-sizers now all understand the challenges to face and the cost involved in being a network. A less homogeneous group, the higher ranked have an interest in keeping their competition limited and distant.

For us, there are no friends within the network firms. They would appreciate associations becoming networks or submitted to additional obligations.

Before dreaming about new clients and additional work, we need to make sure to have our lobbying in place: a formal one as an association, at all decision and influencing levels, early and with a strong voice; an informal one by all of us, clarifying to clients and business partners that one size does not fit them all and that the additional costs of such reforms will end up in their income statement.

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After 20 years with Big Four companies, **Helmut Havenith** set up his own audit company in the multicultural and multilingual Luxembourg some 10 years ago. With the help of his team, he is dedicated to the audit of groups, private equity, securitisation companies, and other commercial and industrial companies.

Audit Central

Revised Ethical Standard Issued in UK

By Katherine Rose

A revised Ethical Standard (ES) has been released for periods beginning March 2020, that hopes to restore public confidence in audit. Some of the changes only affect the audit of public interest entities (PIEs), but many impact the audit of all entities and are of importance to all who carry out audit work.

The changes to the ES are designed to address concerns regarding the independence of auditors and conflicts of interest that arise. To achieve this the **“objective, reasonable and informed third party”** test, a core element of the ES, is redefined to make it more effective. The test now focusses on the perspective of stakeholders who are the ultimate beneficiaries of the audit process. When considering whether the principles of the ES have been met, reference is made to the perspective of a third party, which is informed about the roles and responsibilities of an auditor, those charged with governance, and the entity’s management, **but is not themselves an audit practitioner.** This will require auditors to have a greater understanding of an entity’s key stakeholders and their expectations as to how auditor independence should be ensured.

The existing approach of having more stringent requirements for the audit of PIEs remains, but the ES now extends these constraints to **other entities where there is significant public interest** to stakeholders, such as private entities with more than 2,000 employees.

Auditor independence may be impaired when non-audit services are provided to an audit client. This is addressed by a change of approach for the audit of PIEs and other entities of public interest, with the introduction of a **new list of permitted services** that can be provided to an audit client, all of which are related to the audit itself or are required by law.

Further changes restrict all auditors from providing internal audit and recruitment services and rule out work under contingent fee arrangements. For some firms this is significant to the services they can now offer.

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Katherine Rose is responsible for quality control, compliance, and technical matters at Citroen Wells. She also manages a portfolio of audit clients, with 15 years’ experience working with businesses across many industries, focussing on international groups and consolidations under UK GAAP and IFRS.

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Audit Risks in a COVID-19 Environment

By Tom Parry

As auditors plan audits of clients with 2020 fiscal year-ends, they will need to consider how the clients have been affected by the pandemic. The US Auditing Standards Board has identified four areas that may present heightened risks for auditors:

Internal control

Client controls may have changed during the pandemic to accommodate remote workforces, requiring the auditor to conduct evaluations of controls in place both before and after the pandemic commenced.

While an auditor may have historically placed reliance on the effectiveness of a given control, such an approach may no longer be possible, requiring the auditor to revise the nature, timing, and extent of substantive testing.

Fraud risk

COVID-19 also presents a "perfect storm" for fraud risk: incentives or pressure, opportunity, and rationalisation.

There may be pressures to make fraudulent journal entries to sustain the appearance of an entity's viability to lenders, or to misappropriate assets if personal financial situations have worsened.

Opportunities could arise from breakdowns in internal controls, allowing for fraudulent financial reporting or misappropriation of assets.

Employees could rationalise these fraudulent activities, thinking, "I'm only changing the numbers to help the company survive", or "I'll pay this back as soon as things return to normal".

Noncompliance with laws and regulations

The risk of noncompliance may be heightened as a result of many small businesses finding it necessary to participate in various forms of federal economic stimulus funding. Regulations put in place to ensure proper use of the funding can be onerous, and the complexities of these regulations and short time frame to submit applications, may have led to a heightened risk of inadvertent noncompliance.

Accounting estimates

Auditors will need to identify audit areas that would have a heightened risk, such as the allowance for doubtful accounts or impairment of goodwill or intangible assets.

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Tom Parry oversees quality control at Navolio & Tallman. He is the immediate past chair of the AICPA Peer Review Board, member of the CA Peer Review and Accounting Principles and Auditing Standards Committees and serves on the Quality Control task force of the US Auditing Standards Board. He also provides peer review and quality control services for other firms.

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Georgia Passed a New Law Regulating the Accounting, Reporting, & Auditing of Enterprises

By Giorgi Kutchashvili

Wondering how developing countries succeed? Then this article is for you. In 2014, Georgia signed an Association Agreement with the European Union, under which it undertook to gradually bring the accounting and auditing sector closer to EU norms and standards. As a result, in 2016, Georgia passed a new law according the enterprises

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Giorgi Kutchashvili is a head of the Financial Audit Department in TMC LLC. He heads up a team of auditors and supervises audit matters. He also participates in audit engagements as an audit manager. In addition, Giorgi leads the training in financial and tax issues in the TMC training club.

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accounting, reports preparation/publication and auditing. The basic idea of the law is that the financial statements of enterprises should be transparent and public.

According to the law, enterprises were divided into categories and the respective requirements were defined for each category. The category is assigned according to three criteria: the value of the assets, the annual income, and the number of employees. High-end enterprises are required to conduct accounting and financial reporting in accordance with International Financial Reporting Standards (IFRS). Relatively low-end enterprises are required to conduct accounting and financial reporting in accordance with International Financial Reporting Standards for Small and Medium Entities (IFRS for SMEs).

They have the right to use IFRS. However, under the new law, high-end entities are required to provide audits of their own financial statements. The new law also applies to audit firms; in the audit process, the auditor/audit firm is required to comply with International Audit Standards (ISA) and follow the IESBA Code of Professional Accountants (IESBA) established by the International Federation of Accountants (IFAC).

In the end, it should be noted that the new law is a big step forward in the development of the country, as it promotes the formation of financial culture and the production of financial records in accordance with international standards.

It also helps companies to attract investors, as they will be able to easily obtain financial information prepared according to international standards, and make an adequate decision based on this information.

Insights from the 2020 ACFE Global Study on Occupational Fraud

The Anatomy of Fraud

By Smadar Rinat

The Association of Certified Fraud Examiners (ACFE) released the "Report to the Nations: 2020 Global Study on Occupational Fraud and Abuse", covering cases investigated by certified fraud examiners around the globe. Impacted organisations included private, public, government, and not-for-profit entities. Findings of the Report are summarised below.

While asset misappropriation was found to occur more frequently than other frauds, it resulted in the lowest median loss. In contrast, financial statement fraud occurred less frequently but resulted in the greatest loss. Corruption crimes fell in the middle in terms of frequency and financial cost.

Detection was one of the most important keys to fraud prevention.

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Smadar Rinat is a Principal in the international and audit and accounting departments of Prager Metis CPAs, a Member of Prager Metis International Group. Smadar has over 25 years of experience in the accounting industry. She specialises in providing audit, review, compilation, and accounting services.

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Frauds were mostly uncovered by tips from employees. Organisations with hotlines detected fraud sooner and suffered lower losses.

The offender's level of authority tended to correlate with the magnitude and length of the crime, while the financial damage was correlated to the perpetrator's length of employment with the entity.

While committing fraud, perpetrators often exhibited red flags. The most common were living beyond means; financial difficulties; unusually close association with a vendor/customer; control issues/ unwillingness to share duties.

Lack of internal controls contributed to almost one-third of frauds. The presence of anti-fraud controls resulted in lower losses and faster detection. It is important to note that annual financial statements audits are not designed to detect fraud. An organisation's management is responsible for the design, implementation, and maintenance of internal controls to prevent and detect fraud.

The coronavirus pandemic has introduced many challenges, including changes in business volume and activities, and shifting of a large percentage of the workforce to remote work. This new environment requires organisations to re-evaluate internal controls, policies, procedures, and fraud risks.

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Tax and Fiscal Policy in Response to the Economic Crisis in France after the Lockdown

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Carole Hong Tran

Carole Hong Tran is a Partner with FIDAG, French Chartered Accountant, and ACCA member, with considerable expertise in statutory audit and due diligence operations.

FIDAG

By Carole Hong Tran

In a post-crisis environment, businesses are increasingly exposed to solvency risks, in addition to liquidity risks, as the crisis continues. Through many immediate decisions, the French government is trying to limit the adverse impacts on the economy and to help businesses stay afloat. Maintaining business cashflow has been a core goal of the fiscal policy measures which have included:

- Extending deadlines for tax filing for three months;
- Deferral of tax payments for three months and, in the most difficult situations, direct tax

rebates can be decided in the framework for an individualised examination of applications;

- A fast-track procedure for corporate tax claims refundable in 2020 is being implemented;
- Through the solidarity fund financed by the government and the regions, an aid up to EUR 1,500 is granted for very small enterprises, the self-employed, professionals, and the most affected micro-entrepreneurs who have no more than 10 employees, an annual turnover of less than EUR 1 million, and an annual taxable profit of less than EUR 60,000, particularly affected by the economic consequences of COVID-19;
- Mobilisation of EUR 300 billion from the government to guarantee cash lines of credit banks that businesses may need. Indeed, until 31 December 2020, companies of all sizes and legal forms may apply to a state-guaranteed loan from their regular bank to support their cashflow.
- Support from the government and the Banque de France to negotiate with its bank a rescheduling of bank loans;
- Maintaining employment in companies through the simplified and reinforced short-time work schemes and wage subsidies;
- A support plan for French exporting companies.

In the meantime, the path to exiting the crisis may be long. The French government will need to explore all options for tax policy reform to restore its public finances, both in terms of revenue levels and of the tax structure. The debate for next year's finance bills is starting with intense work programs in the coming days.

Going Concern Considerations in a COVID World

By Jeffrey A. Ford

Assessing an entity's ability to continue as a going concern can be challenging even in the best of times. Assessing this in the midst of the COVID pandemic may present additional uncertainties. Nevertheless, auditors and management are required to assess if substantial doubt exists regarding a company's ability to continue as a going concern for at least twelve months past issuance of financial statements.

Impairment Versus Distress

A company or certain assets may experience a decline in value below carrying value for many reasons,

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including pandemic conditions. This impairment does not necessarily indicate substantial doubt regarding going concern. Distress, indicated by difficulties in paying obligations, maintaining production, or generating revenues, may signal this substantial doubt.

Assessing Substantial Doubt

Many of the risks evaluated for going concern have been amplified by the economic fallout of the COVID pandemic, particularly in estimating whether the risks are temporary and the viability of management's mitigation plans. Are revenue and demand declines temporary? Have margins eroded? Is there disruption in the supply chain or availability of labour? Is the company able to raise capital? Are there government relief programs that can help? Are there debt covenant violations or defaults? Can the debt be restructured? The answers to these questions may be indeterminable at this time.

What if Uncertainty Persists?

If uncertainty persists, a company effectively has two choices with regard to its financial statements. First, the statements may be modified to reflect a going concern uncertainty. Most would prefer to avoid this path. Alternatively, companies may hold issuance of their financial statements until the uncertainties can be alleviated. Audit standards provide specific guidance in addressing protracted delays in issuance. This may be a superior option for many during the COVID crisis.

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Impairment of Assets under COVID-19

Mind the GAAP

By Tanvi Gupta

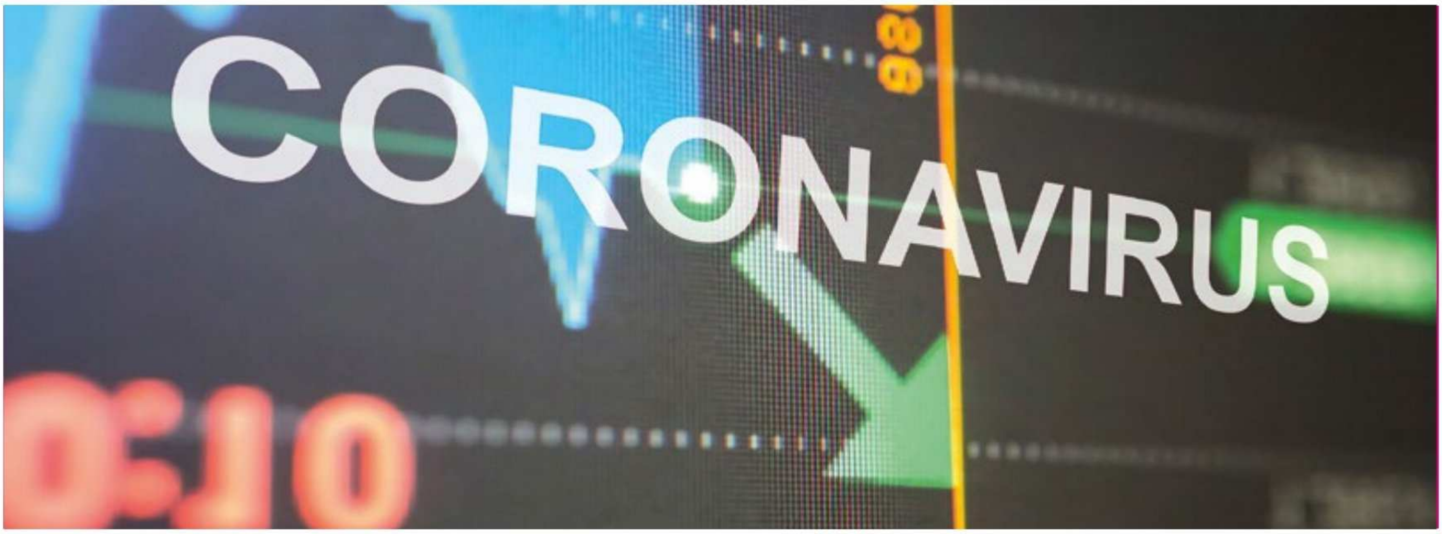
We are living through one of the most challenging times in recent history with the COVID-19 pandemic impacting businesses globally and causing turbulence of an unimaginable scale. The resultant effect, worldwide, has led to many entities experiencing significant shifts in demand and supply curves and decline in their market capitalisation. Given the forceful impact of the pandemic, entities need to address whether a triggering event necessitating testing for impairment of its assets has arisen for financial reporting.

Is the pandemic a triggering event for impairment?

The current economic environment may prompt the need for entities to conduct an impairment assessment of its assets. Although the standards focus on the recoverability amounts of assets, thereby taking a long-term view, the entities may be required to make a careful evaluation of macroeconomic factors and their impact.

Need to revisit cashflow projections

Entities would need to review and



adjust their cashflow projections (CFPs) in the light of likely effects of the pandemic. While there is a negative impact in the near- and medium-term cashflows, cashflows in the long run might have a limited or negligible impact.

Given the extreme uncertainty and volatility, developing a scenario-based approach for CFPs might be appropriate. A rigorous stress testing of all variables and assumptions may provide a better clarity of results in every scenario.

Impact of the pandemic on discount rates

Risk-free rates used in asset valuations may be very low, due to reduction in interest rates by regulators, resulting in very anomalous asset valuations. Therefore, adding a company/sector specific risk premium to capture the unsystematic risk becomes critical.

Challenges in estimating the fair value

Given the highly volatile public markets, the challenge arises as to whether the stock price truly reflects the fair value of a particular business/asset. Entities cannot altogether ignore the prices prevailing orderly transactions in active markets.

However, factors like making volatility comparisons of different periods and adjusting them in the light of expected market conditions, and estimations using various moving averages, merit consideration.

Conclusion

The economic impact of the crisis globally is still unknown. The impairment assessment would need to be made taking a long-term view and considering all impacts. There are no definite answers. Every aspect would need a thorough evaluation supported by concrete analysis and documentation.

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Tanvi Gupta is a Chartered Accountant and specialises in audit and assurance, wherein she is engaged in serving large multinational clients by performing the attest function. Serving clients from national and international companies and having worked in every existing kind of GAAP, she offers pragmatic solutions to her clients.

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Accounting-Audit New Opportunities Amid COVID-19 Crisis

By Seres Baum

The COVID-19 pandemic has transformed the ways and behaviours of people all around the world. The social distancing measures that were implemented to prevent the contagion of the disease, or to modify the timeline of the contagion curve, enhanced some trends that did not seem so obvious.

Some of these tendencies have had major impacts on business models and job opportunities offered by professionals of basically all economic segments, including consulting and auditing.
The organisational plans being put in place to contain and to reply to the outbreak are expected to be in place for a certain period. Consulting and assurance providers should be prepared to adjust to this period in a sustainable way.

Standards of execution of work, previously carried out or validated in person, began to be changed to be satisfied remotely. Notwithstanding, the wholeness commitment regarding the initially planned quantity and/or quality, associated to the deliverables, began to be accepted according to the argument-variable "what is possible?". As organisations adjust to dealing with the preliminary impact of COVID-19, consulting and auditing functions have an important role to play to continue providing critical advice and assurance, helping management and the boards on the unstable risks and controls landscape.

Along with the commitment to keep assisting clients, there are some new opportunities arising from the "new normal". These prospects include:

- Advising about and monitoring new controls avoiding frauds risks and management overrides;
- Understanding the client's need of capital and helping them access government credit/incentive assistance;
- Compliance of outsourced service providers (remote work) specially related to intangible assets such as know-how and industrial secrets;
- Tracking third-party remote access avoiding threat and cyberattack in the client's structure;
- Covers and validity of existing insurance covers for the "new model" of business.

As COVID-19 continues, new business opportunities are showing up for those professionals who adapt to survive when sailing in troubled waters.

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