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Willie Botha
Technical Director
International Auditing and Assurance Standards Board
529 Fifth Avenue
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Dear Sir,

RESPONSE TO INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD'S (IAASB) EXPOSURE DRAFT (ED) ON PROPOSED INTERNATIONAL STANDARD ON AUDITING (ISA) 570 (REVISED 202X) GOING CONCERN

The Institute of Singapore Chartered Accountants (ISCA) appreciates the opportunity to comment on the above ED issued by the IAASB in April 2023.

To solicit meaningful feedback for the topic, ISCA undertook the following initiatives to seek views from key stakeholders:

(i) Conducted a one-month public consultation to seek feedback from its members;

(ii) Solicited feedback on the ED from members of the ISCA Auditing and Assurance Standards Committee;

(iii) Organised two focus groups to engage audit practitioners to obtain their views on the ED. The participants were from large international firms and small and medium-sized practices; and

(iv) Reached out to other selected stakeholders such as users and management/preparers of financial statements to hear their views on areas where the revised auditing requirements could affect them.

Ongoing uncertainties in the macro-economic environment and recent developments in the corporate reporting landscape such as corporate failures of prominent companies like Wirecard and Silicon Valley Bank, necessitate a revisit of the extant standard in the public interest. However, it is essential to recognise that auditors are not, and should not be, the sole guardian of public interest. Fostering a robust and trustworthy corporate reporting ecosystem requires the collective effort of various stakeholders, particularly management and directors.

While audit reports can be referred to by users to give an indication of an entity's ability to continue as a going concern, the survival of a business is dependent on the actions of its management and directors. As such, new and enhanced requirements imposed on auditors need to be balanced vis-à-vis the responsibilities borne by management and directors who drive the operations and strategy of the business. We have highlighted this as part of our response to Question 13.

We share our specific comments to selected questions in the ED as follows:

> Question 1
>
> Do you agree that the proposals in ED-570 are responsive to the public interest, considering the qualitative standard-setting characteristics and project objectives that support the public interest as set out in **Appendix 1**?

While we understand that the proposed revisions are meant to support the public interest, certain new or enhanced requirements should not be implemented without an accompanying expansion of the reporting responsibilities of management and directors over going concern, as elaborated under the responses to Questions 7, 9 and 13.

> Question 2
>
> Do you believe that the proposals in ED-570, considered collectively, will enhance and strengthen the auditor's judgments and work relating to going concern in an audit of financial statements, including enhancing transparency through communicating and reporting about the auditor's responsibilities and work?

We believe that the proposals collectively might strengthen the auditor's judgments and work relating to going concern. However, we hear concerns that certain new or enhanced requirements present challenges in practical implementation and may be too onerous on the auditors should auditor reporting requirements be expanded in a manner that would put the auditor in the position of disclosing information about the entity's viability that is not included in the financial statements, as elaborated under our responses to Questions 8, 9 and 13.

> Question 3
>
> Do you believe the proposed standard is scalable to entities of different sizes and complexities, recognizing that general purpose financial statements are prepared using the going concern basis of accounting and that going concern matters are relevant to all entities?

We believe that the proposed standard is scalable. The examples of the type of procedures that can be tailored to suit entities of different nature and circumstances are useful.

However, the applicability of the requirements under Question 8 to encompass all circumstances (and by extension, all entities) compromises scalability as it adopts a standardised approach for all instead of a risk-based approach. To enhance scalability in this regard, an approach may be to confine the requirements to financial statements of entities where going concern is more pertinent to users, such as public interest entities or entities with external borrowings etc.

Scalability can be further enhanced in the area of communication with TCWG as elaborated under our response to Question 11.

> Question 4
>
> Do the requirements and application material of ED-570 appropriately reinforce the auditor's application of professional skepticism in relation to going concern?

The requirements appropriately reinforce the auditor's application of professional skepticism through its linkage to other relevant standards such as ISA 315 (Revised 2019) and ISA 540 (Revised).

Question 5
Do you support the definition of Material Uncertainty (Related to Going Concern)? In particular, do you support the application material to the definition clarifying the phrase "may cast significant doubt"?

The definition of Material Uncertainty (Related to Going Concern) ("MUGC") included in the ED is based on paragraph 18 of the extant standard. While we support the inclusion of a definition to drive consistent interpretation, it would be useful for the definition to take into account the proposed changes under paragraph A5 of the ED, in particular, the clarification that events and conditions are identified on a gross basis, before considering remedial actions in determining whether there is a MUGC. Specific reference could be made in the definition to the consideration of management's plans and their ability to mitigate the effects of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern.

Application material under paragraph A5

The application material clarifies that the phrase "may cast significant doubt" is used in circumstances when the individual or collective magnitude of identified events or conditions is such that the entity will be unable to meet its obligations and continue its operations for the foreseeable future unless management takes remedial actions to mitigate the effects of these events or conditions.

(a) We disagree with the use of the word "will" here, as the auditor may be unable to make a definitive conclusion in this respect. We suggest replacing the word "will" with "may".

(b) We find the explanation that "may cast significant doubt" is used in circumstances before consideration of remedial actions to be useful. The example given provides guidance that remedial actions are outside the ordinary course of business, for example, early liquidation of assets or seeking additional funding beyond normal re-financing arrangements.

(c) We suggest for additional guidance to be included on the application of the concepts of "feasibility" of management's plans and whether they "mitigate" the effects of events and conditions, for example, where there are multiple possible scenarios / outcomes.

Question 6
Does ED-570 appropriately build on the foundational requirements in ISA 315 (Revised 2019) in addressing risk assessment procedures and related activities, to support a more robust identification by the auditor of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern?

Given that going concern is driven by factors such as business model, market conditions, ability to obtain financing etc, the risk assessment process is critical in the identification of events or conditions that lead to MUGC. Hence, the stronger linkage to ISA 315 (Revised 2019), which strengthens risk assessment procedures, is a good development.

However, this may imply a shift in perceived responsibility – the auditor evaluates management's assessment of the entity's ability to continue as a going concern, with management having responsibility to identify and assess events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. Placing an obligation on the auditor to, effectively, form a view on the existence of events or conditions independently from management may be viewed as a reasonable expectation of an independent audit, but may create additional legal exposure for auditors.

Furthermore, in the absence of a formal process for conducting the going concern assessment by management, identifying going concern indicators may prove challenging for auditors when management does not furnish the necessary information. This is especially so since management possesses intimate knowledge of the entity's operations and industry developments.

<u>Question 7</u>

Do you support the change in the commencement date of the twelve-month period of management's assessment of going concern, from the date of the financial statements (in extant ISA 570 (Revised)) to the date of approval of the financial statements (as proposed in paragraph 21 of ED-570)? When responding consider the flexibility provided in paragraphs 22 and A43–A44 of ED-570 in circumstances where management is unwilling to make or extend its assessment. If you are not supportive of the proposal(s), what alternative(s) would you suggest (please describe why you believe such alternative(s) would be more appropriate and practicable)?

We agree that the date of approval of the financial statements is more appropriate as the commencement date of the going concern assessment. However, for this to be effectively implemented, we believe that the areas below will need to be addressed.

Misalignment to accounting standards

In assessing going concern, paragraph 26 of the International Accounting Standard (IAS) 1 *Presentation of Financial Statements* only requires management to take into account information at least but not limited to twelve months from the end of the reporting period.

The misalignment in requirements between paragraph 26 of IAS 1 and paragraph 21 of the ED could create an unintended, but undesirable, impression that the auditor has a greater responsibility over going concern than management. If the commencement date of the assessment is changed in the auditing standard, the IAASB should coordinate with the International Accounting Standards Board (IASB) to revise IAS 1 as well.

A potential significant challenge faced by auditors arising from such misalignment is that they would face difficulties in requesting management to extend the assessment period since it is not mandated under the IAS 1. This would be particularly challenging where the financial statements are issued after an extended period of time, for instance, where audit reports are issued more than a year after the financial year end This may lead to a limitation on the scope of the audit. Auditors commonly conduct the assessment by reviewing the approved budget or cash flow projection, which typically covers twelve months from the financial year end. The period beyond that would not have been approved by the board of directors and hence will be subjected to a higher degree of uncertainty. It would be useful for the application material to clarify the extent of work required for this additional period due to the change in commencement date, drawing reference to the principles of ISA 560 *Subsequent Events*.

Question 8

Do you support the enhanced approach in ED-570 that requires the auditor to design and perform audit procedures to evaluate management's assessment of going concern in all circumstances and irrespective of whether events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern?

We do not support the enhanced approach, as it would be inconsistent with the fundamental principle of a risk-based audit approach.

Enhanced approach inconsistent with the concept of risk assessment

The requirement for the auditor to design and perform procedures in all circumstances is inconsistent with the concept of performing risk assessment, where the extent of audit work performed should commensurate with the risks assessed.

Such a requirement can lead to substantial increase in costs for entities with low risk of going concern. Drawing reference to IAS 36 *Impairment of Assets*, an entity first identifies indications of impairment before proceeding with an impairment assessment, rather than performing the assessment outright. Similarly, entities with low risk of going concern typically do not require a very robust going concern assessment to be performed by management and subsequently reviewed by the auditor.

To avoid excessive audit work performed, in the case of an entity with a low risk of going concern because of huge profits and strong operating cash flows, the standard should provide more clarity on the extent of work required. For example, whether limited procedures such as inquiries with management would be sufficient.

Consideration of mitigating factors

We would like to clarify if the requirements under paragraphs 16–19 apply before the consideration of mitigating factors under paragraphs 26–27. In our view, it may be too conservative and premature to proceed with a full-scale testing without considering mitigating factors.

Reinforcing management and directors' responsibilities over going concern

For the auditors to be able to carry out the evaluation under all circumstances, management must correspondingly prepare the going concern assessment under all circumstances. Hence, the importance of performing and documenting such assessment needs to be reinforced to management and directors. In addition, incorporating going concern assessment as part of internal controls over financial reporting would be beneficial for entities from a risk management perspective. This could be reinforced through communication with those charged with governance.

Question 9

Does ED-570 appropriately incorporate the concepts introduced from ISA 540 (Revised) for the auditor's evaluation of the method, assumptions, and data used in management's assessment of going concern?

The ED appropriately incorporates the concepts from ISA 540 (Revised) and the stronger linkage is a good development. However, similar to our response for Question 8, it may not be practical to proceed directly with the evaluation without first considering going concern indicators and mitigating factors.

Gap between accounting and auditing standards

This is another instance where there is a gap between the requirements of the accounting and auditing standards. In order for the auditor to perform audit procedures to evaluate management's assessment of going concern in all circumstances, including the methods, assumptions and data used, it is essential for the accounting standards to mandate that management prepares such assessment using proper method, assumptions and data in all circumstances.

Since accounting standards do not establish prescriptive requirements with respect to management assessment, we recommend that the standard be focused on the robust challenging of management's significant assumptions and judgements, regarding whether these are reasonable and supportable, as well as considering the relevance and reliability of the underlying information used in the assessment.

Question 10 Do you support the enhanced requirements and application material, as part of evaluating management's plans for future actions, for the auditor to evaluate whether management has the intent and ability to carry out specific courses of action, as well as to evaluate the intent and ability of third parties or related parties, including the entity's owner-manager, to maintain or provide the necessary financial support?

We are supportive of the enhanced requirements. Based on our understanding, in practice, auditors are already evaluating the intent and ability as part of their evaluation of management's plans. Hence, it is good for the standard to formalise the requirements and include related application material.

Guidance on when to assess legality and enforceability of commitments

Paragraph A52 of the ED states that written confirmation to provide evidence about the intent of third party or related party financial support providers may include, when applicable, the legality and enforceability of the commitments. It would be useful for the standard to provide guidance on situations that require the auditor to assess legality and enforceability, as these aspects are not typically covered in standard audit procedures.

For instance, in cases where the financial support provider is a related party, such as a parent company with strong financials and has historically been providing financial support when needed, it may not be necessary to assess legality and enforceability. Rather, the auditor should consider the business rationale for the related party to provide such support. In contrast, when the financial support provider is an individual and the entity in question faces a high going concern risk, enforceability of the commitment becomes more critical.

Question 11 Will the enhanced requirements and application material to communicate with TCWG encourage early transparent dialogue among the auditor, management and TCWG, and result in enhanced two-way communication with TCWG about matters related to going concern?

We are supportive of the enhanced requirements. In practice, these requirements are already carried out in most audits of listed companies, where there is formal oversight of the entity by TCWG.

However, for other types of entities, such as smaller private entities or subsidiaries or branches of multinational corporations that are non-complex and lower risk, TCWG oversight may not be as formal. Scalability could be enhanced in the area of communication with TCWG for such entities.

<u>Question 12</u> Do you support the new requirement and application material for the auditor to report to an appropriate authority outside of the entity where law, regulation or relevant ethical requirements require or establish responsibilities for such reporting?

This new requirement is also consistent with a requirement in ISA 250 (Revised) to report to appropriate external authorities identified or suspected non-compliance with laws or regulations though it would be more applicable for jurisdictions where laws and regulations require the auditor to report on going concern issues to external authorities.

In Singapore, listed companies are required to announce their financial statements on a quarterly basis if their auditors have stated that a material uncertainty relating to going concern exists in their latest financial statements. As there are no specific reporting requirements for auditors, this new requirement is not applicable to our jurisdiction.

We note that this requirement is applicable to all entities. However, this requirement may be more relevant to regulated entities due to their higher risk profile and public interest characteristics. Hence, IAASB may wish to consider confining the scope to regulated entities.

<u>Question 13</u> This question relates to the implications for the auditor's report **for audits of financial statements of all entities**, i.e., to communicate in a separate section in the auditor's report, under the heading "Going Concern" or "Material Uncertainty Related to Going Concern", explicit statements about the auditor's conclusions on the appropriateness of management's use of the going concern basis of accounting and on whether a material uncertainty has been identified. Do you support the requirements and application material that facilitate enhanced transparency about the auditor's responsibilities and work relating to going concern, and do they provide useful information for intended users of the audited financial statements? Do the proposals enable greater consistency and comparability across auditor's reports globally?

While some users of financial statements are supportive of the inclusion of explicit statements by the auditors, the proposed approach to include explicit statements by the auditors may not be the best way to communicate matters related to going concern. We highlight the issues below.

Explicit statements wrongly perceived as piecemeal opinion

One of the fundamental principles of audit is that the auditor only expresses a single audit opinion on the financial statements as a whole. The auditor does not give multiple audit opinions. However, when such explicit statements are included, they may be wrongly perceived as a separate opinion issued on going concern, which is not what an auditor would ordinarily report. This would further widen the audit expectation gap.

Since going concern is an underlying concept in the preparation of financial statements, some carry the view that the absence of additional disclosures by the auditor should already be sufficient to indicate that the auditor is satisfied with management's use of the going concern basis of accounting.

Lack of expansion of management and directors' responsibilities

It is important to recognise that a robust corporate reporting eco-system is a collective responsibility shared among its multiple stakeholders and should not be overly dependent on auditors. Any proposed change must reflect this.

With this in mind, any expansion in the auditor's disclosure on going concern should be preceded by an expansion in the reporting responsibilities for directors and management. This is because the survival of an entity is primarily dependent on the actions of its directors and management. Otherwise, it would appear that the auditor has a greater role and responsibility than directors and management in this respect.

Currently, the requirement under IAS 1 is for management to disclose if significant judgement has been made in determining that there is no material uncertainty related to going concern. For easy call situations, management is not required to provide further disclosures on going concern. If auditors are required to make explicit statements in the absence of management disclosures, it would appear that the reporting requirements are unbalanced.

Explicit statements may be viewed as assertions on going concern

The inclusion of such explicit statements may be viewed as the auditor affirming that no MUGC exists. However, a going concern assessment is forward-looking and subject to inherent limitations because the conditions existing at the time of the assessment may change unpredictably and drastically in the future, potentially giving rise to going concern issues at a later point in time. Hence, there are concerns raised that it would be onerous for the auditor to include such explicit statements in the auditor's report. In the event of corporate failures arising from circumstances not within the entity's control, there are concerns over legal consequences that may result from the inclusion of such statements. If explicit statements are to be added, additional explanatory wording relating to the auditor's inherent limitations to predict future effects of events or conditions is needed to avoid any misunderstanding by users.

Another concern is the possibility of financial statement users placing excessive reliance on the binary conclusions presented in the explicit statements, without thoroughly reading the accompanying information and related disclosures. This can lead to users overlooking important "warning signals" embedded in the auditor's report or financial statements. As a result, the expectation gap on the auditor's reporting responsibilities in relation to going concern will be further widened.
In our view, enhancing the level of disclosures by management on going concern would provide greater value to users, as elaborated in the next section.

Enhancing the level of disclosures by management

Instead of binary statements from the auditor about the existence or non-existence of MUGC, providing more comprehensive disclosures on going concern in the financial statements from management's perspective, especially for "close call' situations, will be more value adding and relevant to users.

Additional information that would be useful to users of financial statements include:

(i) Sufficiency of working capital to satisfy the entity's present cash flow needs;
(ii) Assumptions used in the entity's assessment of its ability to operate as a going concern;
(iii) Sensitivity analysis on the entity's financials;
(iv) Plans put in place with regard to how the entity intends to fulfil its short-term obligations in the next twelve months; and
(v) Whether the entity has renegotiated its facilities and/or been granted extension of time to meet its debt obligations. If so, disclose whether the entity has fulfilled or is able to meet its debt obligations.

In this regard, the IAASB should consider working closely with the IASB on key relevant disclosures. We believe that this will result in better communication to financial statement users on the risks associated with an entity's ability to continue as a going concern and the complexity of such assessments.

Guidance on when Emphasis of Matter should be utilised

Currently, the auditor can provide further transparency in the auditor's report through an Emphasis of Matter paragraph in accordance with ISA 706 (Revised) to draw attention to going concern disclosures in the auditor's report. With the proposed new disclosures in the auditor's report, it would be helpful for the standard to clarify whether, when and how an emphasis of matter in relation to MUGC should be utilised.

Question 14 This question relates to the additional implications for the auditor's report **for audits of financial statements of listed entities**, i.e., to also describe how the auditor evaluated management's assessment of going concern when events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern (both when no material uncertainty exists or when a material uncertainty exists). Do you support the requirements and application material that facilitate further enhanced transparency about the auditor's responsibilities and work relating to going concern? Should this be extended to also apply to audits of financial statements of entities other than listed entities?

We are supportive of the new requirements, which would standardise the auditor's communication in a "close call" situation.

To provide more transparency to users of financial statements, the IAASB should consider working with the IASB on key relevant disclosures as elaborated in the response to Question 13 under *Enhancing the level of disclosures by management*. The auditors would then be able to further supplement such disclosures by describing the procedures performed over those disclosures.

Question 17(b) Effective Date—Given the need for national due process and translation, as applicable, and the need to coordinate effective dates with the fraud project, the IAASB believes that an appropriate effective date for the standard would be for financial reporting periods beginning approximately 18 months after approval of the final standard. Earlier application would be

permitted and encouraged. The IAASB welcomes comments on whether this would provide a sufficient period to support effective implementation of the ISA.

We note that the exposure draft of revised ISA 240 is expected to be issued by December 2023. If there are proposed updates to the auditor's report in ED-ISA 240 as well, the effective dates of both standards should be aligned so that changes to the auditor's report can be implemented concurrently.

Should you require any further clarification, please feel free to contact Mr Terence Lam at terence.lam@isca.org.sg or Ms Wang Zhumei at zhumei.wang@isca.org.sg.

Yours faithfully,

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