BUSINESS RESCUE

IMPACT OF BUSINESS RESCUE TO THE AUDIT PROCESS

PRESENTER: SONÉ KOCK

BUSINESS RESCUE AUDIT IMPACT

Responsibility as Auditor

- The Business Rescue process brings about some practical considerations around the audit procedures, but it does not change the responsibility of the auditor.

- The auditor is appointed by the shareholders or business rescue practitioner to express an opinion on whether the consolidated and separate financial statements of the company is a fair reflection of the financial position as at the reporting period date and for the period then ended.

BUSINESS RESCUE AUDIT IMPACT

Appointment of an Auditor

2 scenarios

- Current auditors of a company that goes into business rescue; or
- The company goes into business rescue and the position of auditor is vacant and the appointment of an auditor is made by the business rescue practitioner.

- **Client reacceptance / continuance considerations:**
  - Risk of the engagement is higher than normal and potentially as part of the firm's process, approval from the Risk Committee needs to be obtained to continue or re-accept the engagement;
  - Assessment of staff requirements to the engagement from a senior staffing level is required as it would entail a lot more senior involvement to the audit both from engagement partner and manager to composition of the audit team;
  - Involvement of audit and IFRS technical teams with considerations around the impact to the audit opinion and the correct accounting treatment of items;
  - Potential external audit experts or management experts to assess the recoverable amounts of assets and liabilities;
  - Appointment of an EQCR to the engagement if not a public interest entity;
  - Independence considerations; and
  - Agreement of the audit fee with the Business Rescue Practitioner and formally engaging through an engagement letter.

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Specific Considerations around the Risk Assessment

The good thing is that the audit process remains unchanged!

- **The first step is planning and risk assessment:**
  - Although the Business Rescue Practitioner is in control of the company and its activities, he or she is supported by the board of directors and management. From a day-to-day practical perspective in executing the audit the CFO and finance team will remain responsible to provide you as the auditor with the relevant information required. This will all be in consultation with the BRP.

- **The overall pervasive financial statement risk increases when a company is in business rescue.**

- **What this means is a lot more involvement is required from senior staff on the engagement - i.e. engagement partner involvement in directing the staff to ensure that focus is on the right areas and that relevant information is obtained.**
  - Client staff might have left due to restructuring of the company or possible retrenchments.
  - Client staff morale is extremely low and makes it challenging to get the relevant information.
  - Internal control environment has changed due to the roles and responsibilities of staff that has been changed.

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Specific Considerations around the Risk Assessment (Continued)

Planning and risk assessment (continued)

- Obtain a copy of the business rescue plan. Arrange a meeting with the business rescue practitioner and understand the details around the plan, has the plan been approved and the progress made so far in execution of the plan. Understand whether there are any changes anticipated to the plan.

- A key consideration is the date of the approval of the plan compared to the reporting period end date of the financial statements. This is important to consider whether the business rescue is a subsequent event, which is a non- adjusting subsequent event and could have an impact on how certain items are accounted for.

- The statement of financial position becomes a critical component of the audit with most significant risks included to the balance sheet.

- Remember – you as auditor are still responsible to report on the full set of financial statements that includes the statement of comprehensive income.

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Specific Considerations around the Risk Assessment (Continued)

Risk assessment (continued)

- Classification of assets and liabilities – current vs non-current;
- Assessment of the carrying value of assets – specifically around the value in use vs fair value less costs to sell;
- Goodwill and intangibles – what is the plan with the business and potential restructuring – Nature of these intangibles and do they still have value?
- Plant and equipment – consideration of assets that are idle – potential suspension of depreciation, carrying values;
- Inventory – fire sale of certain items – assessment of valuation at the lower of cost or net realisable value;
- Trade and other receivables / intercompany loans – ECL models, increase in credit risk with lifetime credit losses; and
- Right of use assets – possible impairments as a result of lease cancellations.

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Specific Considerations around the Risk Assessment (Continued)

Risk assessment (continued)

Completeness of liabilities is a significant risk.

- As part of the business rescue process creditors would have submitted their claims. This opens a can of worms and claims seem to come out of the woodwork in this process. The business rescue practitioner is key in the process of assessing whether these claims are valid liabilities or not and the auditor will work closely with the business rescue practitioner to assess the validity, accuracy and completeness of liabilities.

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Specific Considerations around the Risk Assessment (Continued)

Risk assessment (continued)

Completeness of liabilities – some areas of consideration:

- Covenant breaches – before or after business rescue process has commenced and has the lender condoned the breaches.
- Completeness of provisions re employee liabilities – retrenchments etc.
- Accrual in relation to the business rescue practitioner fees in terms of the approved engagement letter as part of the business rescue plan.
- Termination penalties in relation to cancellation of leases.

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Specific Considerations around the Risk Assessment (Continued)

Risk assessment (continued)

Other considerations:

Reportable irregularities and NOCLAR

Some examples seen in practice:

- Withholding of payment of VAT to the Receiver of Revenue;
- Deductions from staff remuneration with respect to PAYE, pension and provident fund and not being paid over to the Receiver of Revenue or the fund;
- Financial statements not completed and submitted within six months of the year-end.

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Specific Considerations around the Risk Assessment (Continued)

Risk assessment (continued)

Impact to the audit opinion

- SAAPS 3 – Going concern decision tree.
- Not automatic qualification, adverse or disclaimer.
- If relevant disclosures are made with respect to material uncertainties to the financial statements and auditor can obtain relevant appropriate audit evidence - then most likely to be unmodified with emphasis of matter.

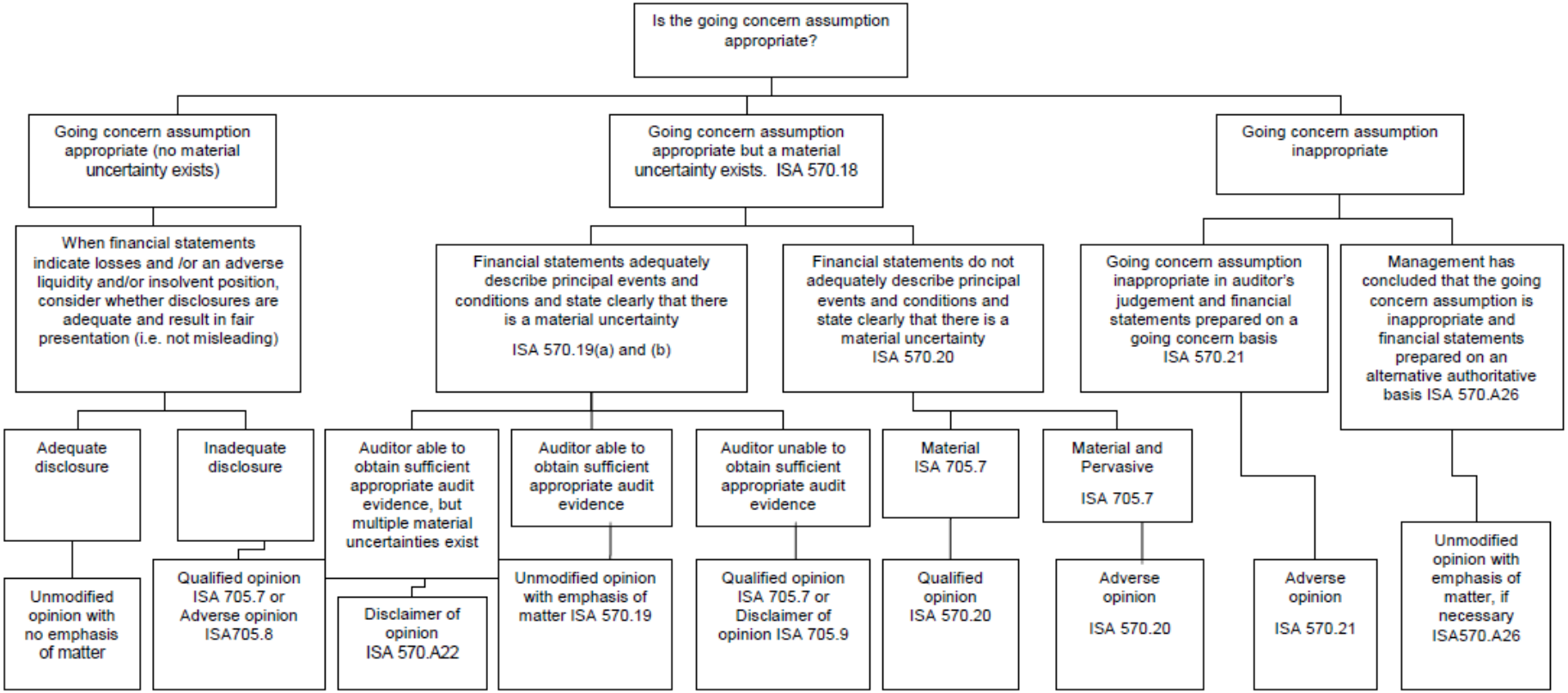
Practical matters:

- Business rescue practitioner approve the financial statements.
- Behind the name of the company it states COMPANY NAME (IN BUSINESS RESCUE).

SAAPS 3 (Illustrative Reports)

Appendix I

Going Concern Decision Tree



Going concern assumption: An entity is ordinarily viewed as continuing in business for the foreseeable future with neither the intention, nor the necessity of liquidation, ceasing trading, or seeking protection from creditors pursuant to law or regulations. Accordingly assets and liabilities are recorded on the basis that the entity will be able to realise its assets and settle its liabilities in the normal course of business (Glossary of Terms).

Material uncertainty: Exists when the magnitude of its potential impact is such that, in the auditor's judgement, clear disclosure of the nature and implications of the uncertainty is necessary for the presentation of the financial statements not to be misleading (ISA 570.17).

Q&A