

## COVID-19 Pandemic: FAQs and related guidance when carrying out audits based on Sri Lanka Auditing Standard for the Audits of Non – Specified Business Enterprises

The 2019 novel Coronavirus infection ('coronavirus') or 'COVID-19' outbreak poses a serious public health threat and a global economic downturn. The emergence and spread of the coronavirus have also resulted in many businesses, including auditors restricting travel of their staff members to client organizations due to both government regulations and health reasons. At the time of formulating this Frequently Asked Questions (FAQs) and related guidance, the requirements of social distancing have brought about significant limitations on the ability of the audit practitioners to perform traditional audit procedures as a result of the lock-down mandated by the authorities. Under normal circumstances, the inability to carry out required audit procedures may have created a scope limitation on the performance of the audit of non- Specified Business Enterprises (non-SBEs). This FAQ and related guidance address complexities and uncertainties that the auditors of non- SBEs are facing as a result of the coronavirus pandemic and provide practical guidance on how to deal with the challenges that are being encountered in performing such audits, thereby attempting to mitigate the limitations that may have otherwise created a scope limitation.

This publication on FAQs and related guidance is only applicable when carrying out audits in accordance with the Sri Lanka Auditing Standard (SLAuS) for the Audits of Non SBEs issued in 2018.

The following is a non-exhaustive list of FAQs and related guidance which auditors should consider when carrying out audit engagements of non-SBEs in the current circumstances. This publication is intended to help auditors to deal with the emerging situation as described above and should not be considered as enduring or providing long-term solutions as this will not be applicable when normal circumstances resume.

Matter	Guidance
<p><b>1. Does an auditor have to re-assess the risk of material misstatement of the non-SBE audit due to the COVID-19 pandemic?</b></p>	<p>With the coronavirus outbreak, an auditor in most instances will need to reassess the nature and level of risks of material misstatement on an audit of a non-SBE, as the information on which the initial risk assessment was based may have either changed or new circumstances previously not considered have occurred.</p> <p>Some new circumstances that may have arisen due to the pandemic can be:</p> <ul style="list-style-type: none"> <li>(a) the design and effectiveness of management's control may have changed because of social distancing, and at times could heighten the risk of fraud;</li> <li>(b) the owner-manager of key individuals responsible for executing critical controls may be unable to perform the work for an extended period, causing a lapse of a critical control</li> <li>(c) auditor not being able to observe a critical control in operation during the period under review, or inability to carrying our planned audit procedures because of social distancing;</li> <li>(d) the authenticity of evidence obtained while practicing social distancing, and evidence gathered in non-traditional methods.</li> </ul> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• If the auditor is yet to commence the year-end audit procedures, consider if there are any new risks that were not assessed during the planning phase.</li> </ul>

Matter	Guidance
	<ul style="list-style-type: none"> <li>• Consider if the level of risk associated with account balances, classes of transactions or disclosures at the planning stage need to be re-evaluated, perhaps to the extent that they now become a significant risk. If so, determine what additional audit procedures may be required to address any new significant risks.</li> <li>• Determine the risk arising from deviation of usual internal controls of the entity due to COVID-19 pandemic.</li> <li>• Determine if management has put in place reliable and adequate controls to monitor and address issues arising from the COVID-19 pandemic.</li> <li>• Determine if any changes in the nature and level of risk require alternative audit responses to such risks (e.g. Inability to attend client locations to perform tests of controls, increasing sample sizes when performing tests of details etc.)</li> <li>• Determine what audit evidence can be obtained remotely using virtual and electronic methods.</li> <li>• Determine if more focus on substantive testing will provide sufficient and appropriate audit evidence for the matters under significant risks.</li> </ul>
<p><b>2. Does an auditor need to update audit engagement letter as a result of the COVID-19 outbreak?</b></p>	<p>Paragraph 1.5.3 of Chapter 01 - <i>Objectives, General Principles and Responsibilities Governing an Audit of Financial Statements</i> requires the general areas of the written agreement. However, the auditor should assess whether circumstances require the terms of the audit engagement to be revised and whether there is a need to remind the entity of the existing terms of the audit engagement.</p> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• Auditor shall review the existing terms of engagement to evaluate if any changes to the audit engagement letter are required as a result of COVID-19. This may include the usual methods of audit evidence gathering which may be difficult or no longer possible to be met as a result of the COVID-19 outbreak. For example, COVID-19 restrictions on movement may result in difficulties for management to carry out physical verification of inventory while the auditor is present, or to provide certain printed hard-copy information.</li> <li>• Where such restrictions are identified, the auditor shall discuss the same with management, and determine how the information and access required for the audit will be gained in the current environment. This may require revision of the engagement terms, which needs to be communicated to the client.</li> </ul>
<p><b>3. Is the auditor required to be alert of any frauds that happen as a result of COVID-19?</b></p>	<p>An auditor need to maintain professional skepticism and be alert on how the fraud risk may vary or increase as a result of COVID-19. There may be situations where the risk of fraud has increased as the control environment may be operating differently than as usual. For instance, segregation of duties and relaxation of security controls at an entity based on changes to working conditions caused by the COVID-19 restrictions, may increase fraud risk. In general, an auditor is required to exercise professional skepticism to determine whether there are</p>

Matter	Guidance
	<p>material misstatements if any in the areas of overstatement of assets and understatement in the liabilities.</p> <p>The requirements in para 1.8.2 of Chapter 1 will suffice for the auditor to discharge his/her responsibility under Sri Lanka Auditing Standard (SLAuS) for the Audits of Non – SBEs issued in 2018.</p>
<p><b>4. How is the materiality affected due to COVID-19 pandemic?</b></p>	<p>Depending on the significance of the impact on non-SBE, the need arises to determine an appropriate materiality.</p> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• Consider if the financial performance of the non-SBE is so low due to the impact of COVID-19.</li> <li>• If the revenue and profit before tax as a basis for materiality is not suitable, determine the materiality based on the net assets or total assets of the non-SBE.</li> </ul>
<p><b>5. What are the additional areas to communicate with those Charged with Governance when a non-SBE audit is affected by COVID-19 pandemic?</b></p>	<p>Due to the social distancing and use of non-traditional methods of gathering audit evidence, the auditor may obtain audit evidence mostly from inquiry-based audit procedures. In addition, the auditor may use technology (such as conference calls or video conferencing) to gather audit evidence in place of traditional examination of printed hard copy.</p> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• If possible, use video conferencing to enable auditors to see the person they are interviewing when obtaining audit evidence through inquiry.</li> <li>• Capture the screen-shots with time of the meeting while the virtual meeting is in progress.</li> <li>• Interview others within the entity as appropriate, to determine whether the evidence obtained through inquiry procedures are valid, and to corroborate discussions with management.</li> <li>• Document the minutes of the meetings held via electronic mode in working papers and agree with parties present. The response to inquiries of the auditor shall be clearly noted referring to who said, what and when.</li> <li>• Obtain agreement to the minutes noted in writing from the management.</li> <li>• When discussions with management are carried out via emails, it is appropriate to build the history of the conversations of all email discussions into one or few emails which can be printed and kept as a part of the audit working papers.</li> </ul>
<p><b>6. What alternative procedures can be carried out when an auditor cannot attend the physical verification of inventory due to social distancing</b></p>	<p>Due to circumstances associated with the COVID-19 pandemic, the auditor may be unable to attend a physical verification of inventory, and accordingly alternative procedures shall be considered.</p> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• Inspect documentation of the subsequent sale of specific inventory items purchased prior to the planned physical inventory counting date.</li> </ul>

Matter	Guidance
<p><b>and other restrictions?</b></p>	<ul style="list-style-type: none"> <li>• Observe physical inventory counts on a date subsequent to the date it was carried out by the client and perform procedures to 'roll-back' inventory balances.</li> <li>• If the client has performed cycle-counts during the year with the presence of the internal auditor or any personnel who is not directly responsible for the custody of inventory, review the client's cycle-count procedures and records.</li> <li>• Utilize technology (such as viewing counts via a video link) to assess the existence and condition of inventory. When using technology, the auditor should use professional skepticism and common sense as suggested below: <ul style="list-style-type: none"> <li>- Prior to the count obtain the floor and location plan of the store and compare the actual images against the floor plan.</li> <li>- If practical, obtain the exact GPS coordinates of the location where inventory is held via Google Maps, and comparing the live feed GPS coordinates while the count is taking place.</li> <li>- Ask the inventory counter to virtually walk through different parts of the location and observe the live feed.</li> <li>- Capture screenshots or video while the stocktaking is underway and include them in the working papers.</li> <li>- Note names and designations of personnel carrying out the stocktaking.</li> <li>- Request to show a few items on selected racks on a random and surprise basis when virtual verification is underway.</li> <li>- Document the results and conclusions of these alternative procedures with supporting screenshots and other relevant evidence.</li> </ul> </li> <li>• Test the accuracy of the inventory reconciliation to the general ledger at period end including test of reconciling items. If the audit risk cannot be reduced to an acceptable level by using alternative method of carrying out physical verification of inventory, this will impose a scope limitation, which has to be reflected in the audit report based on the materiality.</li> </ul>
<p><b>7. How to perform roll-back audit procedures for inventory existence, during COVID 19 – pandemic?</b></p>	<p>In current circumstances, auditor may decide to use audit evidences available after the year-end and use appropriate techniques to roll-back to assess the existence of inventory for the purpose of substantive audit procedures. The examples of audit evidences that can be obtained can vary depending on the circumstances.</p> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• Vouch a sample of purchases of inventory during the intervening period to and from perpetual records.</li> <li>• Vouch a sample of sales of inventory during the intervening period to and from perpetual records.</li> <li>• Perform substantive analytical procedures to evaluate sales, gross margin percentage, inventory turnover.</li> <li>• Test Inventory sales and purchases for proper cutoff at the period end.</li> <li>• Inquire from management of the usability of recorded inventory under current conditions and document the response.</li> </ul>

Matter	Guidance
<p><b>8. What are the other alternative procedures that an auditor can take to gather audit evidences when physical access to clients' premises is not practical?</b></p>	<p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• Explore alternative methods including technology, to the extent possible. When technology is used to gather audit evidence remotely, remember to take screen-capture of evidences and retain them as a part of working papers noting the name and date of the person who provided or remotely showed each supporting document for verification.</li> <li>• Obtain external confirmations directly from the confirming parties in electronic form after validating the e-mail address.</li> <li>• Use third party supporting documents in electronic form as audit evidence</li> <li>• Examine records or documents in electronic form.</li> <li>• Document the name and date of the person who submitted each electronic supporting document for verification.</li> </ul> <p>If the auditor is unable to obtain sufficient appropriate audit evidence prior to the signing date of the auditor's report, it is important to consider the need to modify the audit opinion.</p>
<p><b>9. What additional representations related to COVID-19 would be advisable to be obtained from the management?</b></p>	<p>An auditor shall consider whether it is necessary to obtain additional written representations to support any audit evidence relevant to COVID-19. The following are some additional areas that could be added to the management representation letter, depending on the particular circumstances of an engagement.</p> <p>Points for consideration:</p> <p>Obtain additional representations to address:</p> <ul style="list-style-type: none"> <li>• that all supporting evidences provided by the client electronic or otherwise are relevant and authentic evidences.</li> <li>• the temporary nature of the plans or intentions such as shutting down of business premises or curtailing business activities due to COVID-19 that is not expected to have permanent implications of the carrying value or classification of assets and liabilities.</li> <li>• that despite the temporary nature of business and operational effect of COVID-19, the management neither has the intention nor the need to liquidate or curtail materially the scale of its operations.</li> <li>• other specific management plans for and judgements regarding future actions.</li> <li>• the feasibility of such plans or intent in relation to the applicability of going concern assessment which at times may not be possible for the auditor to assess, given the uncertainty of current circumstances.</li> <li>• that management has disclosed any and all significant changes in processes, controls, policies and procedures that have been made or modified to address the effects of the COVID-19 pandemic.</li> <li>• that for bank loans and borrowings obtained, lenders have not informed of potential discontinuation of the terms and moratorium conditions.</li> </ul>
<p><b>10. What additional procedures can be</b></p>	<p>Auditor may consider obtaining the external confirmations via electronic methods such as emails from external parties.</p>

Matter	Guidance
<p><b>performed when the auditor decided to obtain external confirmations electronically?</b></p>	<p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• Obtain electronic confirmations after validating the sender by calling the external party and inquiring if such an email confirmation was sent.</li> <li>• Determine if the emailed confirmation has come from an official email account or domain. For example a debtor or creditor may have the official email domain address that can be validated separately. However, at times non-SBEs may usually communicate with debtors and creditors through web-based email sources such as gmail and yahoo mail. In such cases, inquire from the non-SBE and request for an appropriate evidence that such web-based emails are usual modes of communication with such parties.</li> <li>• Print and retain the attachments of email confirmations in the audit file with a note of how the authenticity of the sender was validated.</li> </ul>
<p><b>11. Is obtaining management representation letter on non-SBE's letterhead required?</b></p>	<p>Decision to accept electronic signatures, scanned images of signatures, and so on, is a matter of risk management practice and the SLAuS for the Audits of non-SBEs does not require the use of client letterhead specifically.</p> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• As a matter of best practice, it might be prudent for an auditor to obtain the letter of representation in the traditional way if circumstances provide so.</li> <li>• In cases where it is not practical, obtain a scanned image of the signed management representation sent via an email from the one of the signatories to the representation letter which is copied to the other signatories. The other signatories in turn can acknowledge agreement to the representations made as a response to that email sent by the first signatory.</li> <li>• Obtain a hardcopy of the signed letter of representation when audit report is physically signed.</li> </ul>
<p><b>12. What are the alternative procedures that can be carried out in the absence of external confirmations of debtors and creditors during COVID-19 pandemic?</b></p>	<p>The current circumstances create challenges for the auditor to obtain direct external confirmations from debtors and creditors, and alternative audit procedures may be performed.</p> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• For debtors' balances – examine specific subsequent cash receipts, dispatch documentation, and sales near the period-end. If the subsequent settlements are not present, examine related documents and evidence that indicates the goods or services have been received by the customer as at the year end.</li> <li>• For creditors' balances – examine cash payments subsequent to the year end. If the subsequent settlements are not present, examine correspondence with creditors about their inquiry regarding the payments due from the non-SBE as at the year end, and other relevant records, such as goods received notes of the non-SBE acknowledged by the personnel in charge of custody of goods or recipient of services.</li> </ul>

Matter	Guidance
<p><b>13. What audit steps are required to audit the going concern of a non-SBE?</b></p>	<p>Given the unprecedented circumstances, it is difficult for the non-SBEs to assess its ability to continue business for the foreseeable future, given the significant challenges faced at the time of preparing financial statements. Therefore, for the purposes of SLAuS for the Audits of non-SBEs, when management has not currently decided to liquidate or curtail business operations, obtaining a representation letter that management has not decided to do so, will be adequate.</p> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• If the management has no plans to discontinue but revive the business when circumstances become normal, disclose the uncertainty and the intention in the financial statements.</li> <li>• Auditor can inquire about and also use the past experience on how the client has revived the business amidst of challenges faced in history and the business strengths of the client to recover.</li> <li>• If the management has already closed down or intends to close down with no future plans to revive the business, use a different basis to prepare financials i.e. liquidation basis of accounting where all the assets and liabilities are recorded at realizable values using the order of liquidity for the presentation of the balance sheet.</li> <li>• Inquire about the conditions of loans already obtained. If there are non-compliances with such conditions, it could indicate material uncertainties about the ability of the non-SBEs to continue as a going concern, unless remedied after the balance sheet date.</li> <li>• Inquire about repayment deferrals or debt moratoriums granted by financial institutions.</li> </ul>
<p><b>14. In what circumstances COVID-19 and its impact on the non-SBE, would warrant the auditor to include an emphasis of matter to the opinion?</b></p>	<p>There are two circumstances in which Emphasis of matter paragraph can be used.</p> <ol style="list-style-type: none"> <li>1. When there is a material uncertainty regarding going concern: SLAuS for the Audits of non-SBEs in section 4.2.2 and 5.7 requires audit procedures to be carried out in response to assessed risks caused by any identified events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If the auditor determines that COVID-19 has such significant doubt, an emphasis of matter may be relevant.</li> </ol> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• Consider if appropriate disclosure about uncertainty of going concern is included in the financial statements.</li> <li>• Consider the following illustrative wording for the emphasis of matter:</li> </ul> <p>“COVID-19 has had a significant effect on the financial position and financial performance of [name of non-SBE], and accordingly a material uncertainty exists that may cast significant doubt on its ability to continue as a going concern. Our opinion is not qualified in respect of this matter.”</p>

Matter	Guidance				
	<p>2. In addition, under section 6.2.1, if in the auditor’s judgment Emphasis of Matter paragraph is required to draw attention to a matter appropriately presented or disclosed in the financial statements which is fundamental to users’ understanding of the financial statements, the auditor’s report may contain such an Emphasis of Matter.</p> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• Consider if appropriate disclosure about the implications of COVID-19 is included in the financial statements.</li> <li>• Consider the following illustrative wording for the emphasis of matter: “COVID-19 has had a significant effect on the financial position and financial performance of [name of non-SBE] which is further disclosed in note X. Our opinion is not qualified in respect of this matter.”</li> </ul>				
<p><b>15. What are the Accounting Estimates that the auditor will have to be more focused on due to COVID-19 pandemic ?</b></p>	<p>Areas such as estimation of Net Realisable Value (NRV) of inventory and debtors’ impairment can be impacted by COVID-19 significantly.</p> <p>Points for consideration:</p> <ul style="list-style-type: none"> <li>• Inquire and document the management judgment about the NRV and recoverability of debtors in the working papers.</li> <li>• Conclude on the adequacy and reasonableness of related estimates based on the past experience and the auditor’s knowledge of the type and nature of non-SBE business.</li> </ul>				
<p><b>16. What are the type of audit opinions that could be issued by the auditor for a non-SBE during COVID-19 pandemic?</b></p>	<p><b>Unmodified Audit Reports:</b></p> <table border="1" data-bbox="563 1285 1356 1783"> <tbody> <tr> <td data-bbox="563 1285 794 1570"> <p><b>Unmodified Opinion (Clean Opinion)</b></p> </td> <td data-bbox="794 1285 1356 1570"> <p>Despite the current challenges, if the auditor is satisfied that the auditor was able to obtain sufficient and appropriate audit evidence that the financial statements were prepared without any materially misstatements and the adequate disclosures have been made for the users’ understanding.</p> </td> </tr> <tr> <td data-bbox="563 1570 794 1783"> <p><b>Unmodified Opinion with Emphasis of Matter</b></p> </td> <td data-bbox="794 1570 1356 1783"> <p>In addition to the above, if adequate disclosures have been made with respect to the COVID-19 impact and the auditor feels it is fundamental to users’ understanding of the financial statements.</p> </td> </tr> </tbody> </table>	<p><b>Unmodified Opinion (Clean Opinion)</b></p>	<p>Despite the current challenges, if the auditor is satisfied that the auditor was able to obtain sufficient and appropriate audit evidence that the financial statements were prepared without any materially misstatements and the adequate disclosures have been made for the users’ understanding.</p>	<p><b>Unmodified Opinion with Emphasis of Matter</b></p>	<p>In addition to the above, if adequate disclosures have been made with respect to the COVID-19 impact and the auditor feels it is fundamental to users’ understanding of the financial statements.</p>
<p><b>Unmodified Opinion (Clean Opinion)</b></p>	<p>Despite the current challenges, if the auditor is satisfied that the auditor was able to obtain sufficient and appropriate audit evidence that the financial statements were prepared without any materially misstatements and the adequate disclosures have been made for the users’ understanding.</p>				
<p><b>Unmodified Opinion with Emphasis of Matter</b></p>	<p>In addition to the above, if adequate disclosures have been made with respect to the COVID-19 impact and the auditor feels it is fundamental to users’ understanding of the financial statements.</p>				



Matter	Guidance											
	<p><b>Modified Audit Reports:</b></p> <table border="1" data-bbox="564 481 1362 1256"> <thead> <tr> <th data-bbox="564 481 831 689" rowspan="2">Nature of Matter giving rise to the modification</th> <th colspan="2" data-bbox="831 481 1362 607">Auditor's Judgment about the Pervasiveness of the Effects or Possible Effects on the Financial Statements</th> </tr> <tr> <th data-bbox="831 607 1094 689">Material but not pervasive</th> <th data-bbox="1094 607 1362 689">Material and Pervasive</th> </tr> </thead> <tbody> <tr> <td data-bbox="564 689 831 992"><b>Financial statements are materially misstated due to the misstatements (including frauds) along with the COVID-19</b></td> <td data-bbox="831 689 1094 992">Qualified opinion</td> <td data-bbox="1094 689 1362 992">Adverse opinion</td> </tr> <tr> <td data-bbox="564 992 831 1256"><b>Inability to obtain sufficient appropriate audit evidence by the auditor due to the COVID-19 pandemic</b></td> <td data-bbox="831 992 1094 1256">Qualified opinion</td> <td data-bbox="1094 992 1362 1256">Disclaimer of opinion</td> </tr> </tbody> </table> <p data-bbox="544 1290 1388 1357">Please refer to chapter 6 of SLAuS for the Audits of non-SBEs for more guidance.</p>	Nature of Matter giving rise to the modification	Auditor's Judgment about the Pervasiveness of the Effects or Possible Effects on the Financial Statements		Material but not pervasive	Material and Pervasive	<b>Financial statements are materially misstated due to the misstatements (including frauds) along with the COVID-19</b>	Qualified opinion	Adverse opinion	<b>Inability to obtain sufficient appropriate audit evidence by the auditor due to the COVID-19 pandemic</b>	Qualified opinion	Disclaimer of opinion
Nature of Matter giving rise to the modification	Auditor's Judgment about the Pervasiveness of the Effects or Possible Effects on the Financial Statements											
	Material but not pervasive	Material and Pervasive										
<b>Financial statements are materially misstated due to the misstatements (including frauds) along with the COVID-19</b>	Qualified opinion	Adverse opinion										
<b>Inability to obtain sufficient appropriate audit evidence by the auditor due to the COVID-19 pandemic</b>	Qualified opinion	Disclaimer of opinion										
<p><b>17. What practical audit procedures can be carried out by an auditor on subsequent events affected by the COVID-19 pandemic?</b></p>	<p data-bbox="544 1435 1388 1637">The effects of the COVID-19 pandemic could be concluded generally as a 'non-adjusting event' for the December year end engagements. However, for reporting periods ending thereafter (e.g. for financial periods ending 31st March 2020), the effects of the COVID-19 would have to be incorporated into the financial statements as an 'adjusting event'.</p> <p data-bbox="544 1682 831 1709">Points for consideration:</p> <ul data-bbox="544 1715 1388 1955" style="list-style-type: none"> <li>• Inquire from the management and where appropriate, those charged with governance, on the impact of the COVID-19 outbreak on the financial statements and document their response.</li> <li>• Discuss on the resilience of the business and cash position and whether there are any unutilised facilities.</li> <li>• Obtain audit evidence about the reasonableness and completeness of the information disclosed in relation to subsequent events.</li> </ul>											