



**Australian Government**

**Auditing and Assurance  
Standards Board**

# **AUASB RESEARCH REPORT 5**

## **COVID-19 SNAPSHOT OF AUDITOR REPORTING IN AUSTRALIA**

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## Executive Summary

In light of the significant economic disruption and uncertainty associated with the June 2020 financial reporting season, entities' ability to meet reporting obligations and make forward-looking estimates was extremely challenging. As such, the value of audit is increasingly critical to ensure investor confidence in the capital markets and financial reporting as a whole. Accordingly, this paper presents a snapshot and analysis of auditor reporting over the June 2019 and 2020 reporting seasons, focussing on the impact of the COVID-19 pandemic. To do so, the AUASB reviewed a matched sample of 1421 auditor reports and 239 review reports for listed entities with full and half-years ended 30 June 2019 and 2020. This allows for the identification of changes in auditor reporting while removing the impact of sample variance.

### *Auditor Reporting for Full-Years Ended 30 June 2019-2020*

In spite of the increased volatility and uncertainty associated with the June 2020 reporting period, the number of modified opinions in June end-of-year (EOY) auditor's reports did not substantially change. 16 auditor's reports in 2020 (1.1%) included qualified audit opinions compared to 18 (1.3%) in 2019. Only one auditor's report issued in 2020 included a disclaimer of opinion, compared to none in 2019. Reasons for the issuance of modified opinions in 2020 included the inability to verify the valuation of investments, non-current assets and inventory, while only two reports identified the impacts of COVID-19 as contributing to the issuance of a modified opinion. This suggests that financial report preparers are accurately presenting their entity's financial position, including the impacts of COVID-19.

The number of June EOY auditor's reports with Emphasis of Matter (EOM) paragraphs in 2020 increased to 29 (2%), compared to 24 (1.7%) in 2019. This increase is attributable to 10 of the EOMs (34.5%) in 2020 drawing attention to subsequent event disclosures related to the impact of COVID-19. Other prominent EOM topics across the two-year period included the non-going concern basis of preparation and carrying value of non-current assets.

342 June EOY auditor's reports (24.1%) issued in 2020 included a Material Uncertainty Related to Going Concern (MURGC) paragraph compared to 400 (28.1%) in 2019. Additionally, 94 Key Audit Matters (KAMs) related to going concern (approximately 3.5% of total KAMs) were reported in 2020 compared to 80 (3.1%) in 2019. 96 MURGCs (28.1% of total MURGCs) and 32 going concern KAMs (34% of total going concern KAMs) issued in 2020 referenced COVID-19 as a contributing factor leading to going concern issues. However,

86 (67%) of these auditor's reports also included a MURGC or going concern KAM in 2019 which indicates that, in most cases, COVID-19 exacerbated existing going concern issues rather than serving as the outright catalyst for such reporting. The reduced level of going concern reporting in 2020 is likely attributable to the robustness of entities' reporting and the success of government and other assistance available to support businesses. However, the level of going concern reporting is expected to increase in future years as this assistance subsides.

The number of KAMs reported in June 2020 EOY auditor's reports increased to an average of 1.91 per report compared to 1.81 in 2019. The most common KAM categories across 2019-2020 were the impairment of goodwill and other intangible assets (14.4% of total KAMs), exploration and evaluation (14.4%) and revenue recognition (10.9%). 54 auditor's reports (3.8%) in 2020 and 84 (5.9%) in 2019 included no KAMs at all. The impact of COVID-19 on KAM reporting has been significant, with 465 individual KAMs (17.1%) referencing the pandemic. Audit clients in the Real Estate sector received the highest proportion of KAMs referencing COVID-19 to overall KAMs with 79 of 117 (67.5%). The most common KAMs which referenced COVID-19 were impairment of goodwill and other intangible assets (31.6% of all KAMs referencing COVID-19) and valuation of property, plant and equipment (26.9%).

The analysis identified a limited amount of voluntary reporting in the June 2020 reporting season, primarily by Big 4 firms. 110 auditor's reports issued by PwC (98%) included a discussion of materiality and audit scoping while 16 reports, the majority of which were issued by KPMG and Deloitte, reported the procedures to determine the existence of a MURGC.

#### *Review Reporting for Half-Years Ended 30 June 2019-2020*

The number of June half-year (HY) review reports with modified audit conclusions has decreased to 6 (2.5%) in 2020, compared to 8 (3.3%) in 2019. Half of the 2020 modified opinions were issued for reasons including the impacts of COVID-19. 10 EOMs (4.2% of all review reports issued) were reported in 2020 review reports, of which 4 were related to the subsequent event of COVID-19, while only 4 EOMs (1.7%) were reported in 2019. 82 MURGCs (34.3%) were reported in 2020 review reports, which represents an increase of 15 compared to 2019. 36 (43.9%) of these MURGCs issued in 2020 referenced COVID-19, although 20 (24.4%) of these carried over from 2019. The low level of reporting on COVID-19 in review reports compared to auditor's reports can be attributed to reduced reporting by auditors in review reports (i.e. no KAM reporting) due to the limited scope of the engagement.

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## Introduction

The June 2020 financial reporting period has been described by regulators, preparers and auditors as one of the most challenging ever experienced, as entities were faced with unprecedented disruption and uncertainty. This uncertainty was even greater than the recent global financial crisis, as government-imposed restrictions forced many entities to temporarily close or make substantial changes to their operations. Going concern and solvency assessments, estimation of asset and liability values, and disclosure of risks and future prospects were particularly challenging areas. Questions were raised regarding how entities would report and make forward-looking assumptions and estimates given the volatility and uncertainty in the global economic environment. This unprecedented uncertainty poses a threat to investors' confidence in our capital markets.

In such times, the value of audit is more important than ever in enhancing investor confidence in the integrity of financial reporting and keeping the market informed. However, the audit profession is under intense scrutiny in Australia and internationally due to high profile corporate failures and scandals, and regulator inspection findings and criticism. In Australia, ASIC's inspection findings have continued to bring audit quality into question and there has been continued media criticism. In response, the Australian government have undertaken an inquiry into the Regulation of Auditing (Parliamentary Joint Committee on the Regulation of Auditing in Australia, 2019) which examined ways to improve audit quality in Australia. Investors are looking at June 2020 financial reports for vital information as to the impact of the COVID-19 pandemic on entities' results and, just as importantly, the impact on the future of the entities. This provides an opportunity for the audit profession to demonstrate its value by contributing to high-quality financial reporting.

The purpose of this research paper is to provide a snapshot and analysis of auditor reporting over the June 2019-20 reporting period, with a primary focus on the impact of COVID-19. Reference to COVID-19 in the auditor's report was determined by searching for the terms 'COVID-19', 'Coronavirus' and 'pandemic' in the auditor's report and, if relevant, the financial report disclosures directly referred to by the auditor's report. Reviewing auditor's reports also provides insights as to the quality of financial reporting during this period as an unmodified auditor's opinion indicates that the financial report was prepared in all material respects in accordance with the financial reporting framework, which indicates that the

disclosures were materially correct. This means that the impact of COVID-19 on entities' results, going concern assessments and disclosures are materially correct.

To facilitate this analysis, the AUASB used a matched design dataset comprising the same 1660 Australian Stock Exchange (ASX)-listed companies with full and half-years ended 30 June 2019 and 2020. This allowed for the identification of changes in auditor reporting over time, and to gain a more comprehensive understanding of the impact of COVID-19 on the June 2020 reporting season. The analysis considered the various facets of auditor reporting including audit opinion modifications, Emphasis of Matter (EOM) paragraphs, Material Uncertainty Related to Going Concern (MURGC) paragraphs, Key Audit Matters (KAMs) and any additional/voluntary reporting. This ensures that the results capture a complete picture of auditor reporting over the two-year period.

## Analysis of Auditor Reporting in Australia

### 1. Sample Overview and Analysis

This report focuses on auditor's reports on Australian listed companies with 30 June 2019 and 2020 financial reporting year-ends. The sample for this snapshot of auditor reporting in Australia comprises 2842 auditor's reports and 478 review reports for ASX-listed clients with full-years and half-years ended 30 June over the period of 2019-2020. This represents a matched design whereby the auditor and review reports for the same 1421 and 239 clients, respectively, are analysed for the full and half-years ending 2019 and 2020, to identify changes in auditor response while controlling for sample variation<sup>1</sup>. The most represented sector within this sample, based on 2-digit GICS industry classification, is Materials with 537 total auditor and review reports followed by Financials (236), Information Technology (162), Consumer Discretionary (153) and Healthcare (150). See Table 1 for a full breakdown of GICS industry classification for audit clients within the sample.

**Table 1: Sample by 2-Digit GICS Industry Classification**

| GICS Industry Classification | Frequency (Full-Years Ended 30 June) | Frequency (Half-Years Ended 30 June) | Percentage of Total Reports |
|------------------------------|--------------------------------------|--------------------------------------|-----------------------------|
| Materials                    | 467                                  | 70                                   | 32.3%                       |
| Financials                   | 222                                  | 14                                   | 14.2%                       |
| Information Technology       | 131                                  | 31                                   | 9.8%                        |
| Consumer Discretionary       | 128                                  | 25                                   | 9.2%                        |
| Healthcare                   | 126                                  | 24                                   | 9.0%                        |
| Industrials                  | 115                                  | 15                                   | 7.8%                        |
| Energy                       | 95                                   | 31                                   | 7.6%                        |
| Real Estate                  | 60                                   | 14                                   | 4.5%                        |
| Consumer Staples             | 45                                   | 7                                    | 3.1%                        |
| Utilities                    | 16                                   | 6                                    | 1.3%                        |
| Telecommunication Services   | 16                                   | 2                                    | 1.1%                        |
| Total                        | 1421                                 | 239                                  | 100%                        |

250 of the audit clients included in this sample are in the ASX 300<sup>2</sup>, 214 of which reported full-year results and the remaining 36 reported half-year results. 1586 of the 1660 individual clients within the sample with full and half-years ended 30 June were audited based on Australian Auditing Standards while the remainder were primarily audited based on International Standards on Auditing (ISAs) as they are based in overseas jurisdictions (although

<sup>1</sup> 15 auditor's reports and 6 review reports issued in 2020 were not included in the sample as they were newly listed or were missing data for the 2019 reporting period.

<sup>2</sup> The remaining 50 ASX 300 clients have reporting dates other than 30 June.



listed on the ASX). There is no significant identifiable difference in overall reporting results between the auditor’s reports which were audited based on Australian Auditing Standards and those audited based on International Auditing Standards<sup>3</sup>.

## 2. Audit Composition of the Listed Market

*30 June EOY auditor’s reports and HY review reports issued by auditor type:*

In 2020, 815 auditor’s reports (57.4%) were issued by Big 4 and Large Non-Big 4 firms while the remaining 606 auditor’s reports (42.6%) were issued by Medium Non-Big 4 and Small Non-Big 4 firms (as defined in Table 2). In 2019, 829 auditor’s reports (58.3%) were issued by Big 4 and Large Non-Big 4 firms with the remaining 592 (41.7%) issued by Medium Non-Big 4 and Small Non-Big 4 firms. In 2020, 159 review reports (66.5%) were audited by Big 4 and Large Non-Big 4 audit firms while the remaining 80 (33.5%) were audited by Medium Non-Big 4 and Small Non-Big 4 audit firms. In 2019, 163 review reports (68.2%) were audited by Big 4 and Large Non-Big 4 audit firms with the remaining 76 (31.8%) audited by Medium Non-Big 4 and Small Non-Big 4 audit firms.

**Table 2: Auditor’s Reports Issued by Audit Firm Type**

| <b>Auditor Type</b> | <b>Auditor’s Reports: June 2020 (%)</b> | <b>Auditor’s Reports: June 2019 (%)</b> | <b>Review Reports: June 2020 (%)</b> | <b>Review Reports: June 2019 (%)</b> |
|---------------------|---|---|--------------------------------------|--------------------------------------|
| Big 4               | 544 (38.3%)                             | 554 (39.0%)                             | 105 (43.9%)                          | 108 (45.2%)                          |
| Large Non-Big 4     | 271 (19.1%)                             | 275 (19.4%)                             | 54 (22.6%)                           | 55 (23.0%)                           |
| Medium Non-Big 4    | 515 (36.2%)                             | 499 (35.1%)                             | 66 (27.6%)                           | 63 (26.4%)                           |
| Small Non-Big 4     | 91 (6.4%)                               | 93 (6.5%)                               | 14 (5.9%)                            | 13 (5.4%)                            |

Note:

1. Big 4: Deloitte, EY, KPMG and PwC

2. Large Non-Big 4: BDO, Grant Thornton

3. Medium Non-Big 4: Issued transparency report in one or more years across the period 2012–2018: Bentleys, Crowe Horwath, Hall Chadwick, HLB Mann Judd, KS Black, Lawler Hacketts, Moore Stephens, Nexia, Pitcher Partners, PKF Hacketts, PKF Mack & Co, Rothsay, RSM Bird Cameron, ShineWing, Somes Cooke, Stantons International, William Buck and all firms are included as Medium Non-Big 4 Firms in each year of the analysis.

4. Small Non-Big 4: auditors not otherwise classified.

<sup>3</sup> The 40 auditor’s reports (AR) and 34 review reports (RR) based on Non-Australian Auditing Standards had a similar proportion of EOMs (AR: 2.5%, RR: 5%), MURGCs (AR: 25%, RR: 30%) and modified opinions (AR: 2.5%, RR: 3%) and a similar average number of KAMs (AR: 2.1) as the auditor and review reports based on Australian Auditing Standards.

Overall, this indicates a slight decrease in the market share of Big 4 auditors in favour of mid-tier auditors, which is consistent with the trend identified between 2012-2018 by Carson (2019). Of the entities that switched from Big 4 to Non-Big 4 auditors in 2020, none were in the ASX 300, which is consistent with the trend identified by Carson (2019). Table 2 provides an overview of the sample auditor's reports issued by audit firm type (as per Carson, 2019).

*Audit firm composition of the ASX 300:*

In 2020, 214 of 1421 June EOY auditor's reports (15.1%) were issued for clients in the ASX 300 with financial years ended 30 June. 194 (90.7%) of these auditor's reports were issued by Big 4 firms with only 20 (9.3%) issued by Non-Big 4 firms. This represents a slight increase from 2019 whereby 191 of 214 auditor's reports for clients in the ASX 300 (89.3%) were issued by Big 4 firms and the remaining 23 (10.7%) were issued by Non-Big 4 firms. 36 of 239 June HY review reports (15.1%) were issued for clients in the ASX 300, of which 34 (94.4%) were issued by Big 4 audit firms – which remains consistent with 2019.

Overall, the vast majority (94%) of large entities (i.e. those on the ASX 300) are audited by Big 4 auditors, which has remained consistent between 2019 and 2020. This is in accordance with the findings of Carson (2019) that the Big 4 audit firms dominate the market share among larger and more complex audit clients. Refer to Table 3 for an overview of auditor's reports issued for clients in the ASX 300 by auditor type.

**Table 3: Auditor's Reports Issued for ASX 300 Clients by Audit Firm Type**

| <b>Auditor Type</b> | <b>Auditor's Reports: June 2020 (%)</b> | <b>Auditor's Reports: June 2019 (%)</b> | <b>Review Reports: June 2020 (%)</b> | <b>Review Reports: June 2019 (%)</b> |
|---------------------|---|---|--------------------------------------|--------------------------------------|
| Big 4               | 194 (90.7%)                             | 191 (89.3%)                             | 34 (94.4%)                           | 34 (94.4%)                           |
| Large Non-Big 4     | 7 (3.3%)                                | 7 (3.3%)                                | 1 (2.8%)                             | 1 (2.8%)                             |
| Medium Non-Big 4    | 11 (5.1%)                               | 14 (6.5%)                               | 1 (2.8%)                             | 1 (2.8%)                             |
| Small Non-Big 4     | 2 (0.9%)                                | 2 (0.9%)                                | 0 (0%)                               | 0 (0%)                               |

**3. Audit Opinion Modifications in 30 June EOY Auditor's reports**

If the auditor concludes that misstatements are material, but not pervasive, to the financial report, a qualified audit opinion is issued. In 2020, 16 auditor's reports (1.1%) included qualified audit opinions in 2020, which represents a slight decrease from 2019, where 18 reports (1.3%) contained qualified opinions. Nine (56%) of the qualifications issued in 2020 carried over from 2019, indicating that six (44%) were new for 2020. All qualified opinions in

auditor's reports in 2019 and 2020 were issued for small clients not in the ASX 300. Across both 2019 and 2020, 15 qualifications (44%) were issued by Big 6 audit firms.

The most common reason reported for qualifications issued in 2020 was the inability for the auditor to obtain sufficient appropriate audit evidence to verify the valuation of investments in associates and joint ventures, with five such instances. Other reasons given for qualifications in 2020 included the inability to verify the valuation of assets such as PPE, right-of-use assets and intangibles due to a lack of observable market evidence (4 instances) and the inability to verify the existence of inventory due to non-attendance at stocktakes (2 instances).

The majority of these qualifications were issued for reasons unrelated to COVID-19, although two identified the impacts of the pandemic, among other matters, as reason for the issuance of such an opinion. In one such case, the auditor's report was qualified due to the limited evidence available to support the carrying value of the client's investment while the economic uncertainty associated with the COVID-19 pandemic further impacted the availability of appropriate documentation to support this valuation assessment. The second report was qualified due to limited/restricted market and internal evidence as to whether property, plant and equipment and right-of-use assets were impaired at reporting date. This was primarily attributed by the auditor to the impact of COVID-19 and subsequent government restrictions which have resulted in a lack of market transactions that ordinarily serve as a strong source of evidence for valuing these types of assets. Both of these reports received unqualified opinions in 2019.

If the auditor is unable to obtain sufficient appropriate audit evidence on which to base their opinion and concludes that the possible effects of undetected misstatements could be both material and pervasive, a disclaimer of opinion is issued. One disclaimer of opinion was issued in 2020, compared to zero in 2019, which was due to a lack of sufficient appropriate audit evidence to determine whether the client would be able to continue as a going concern. As the auditor did not refer to the impacts of COVID-19 in the basis of disclaimer and the entity is in the energy sector it is unlikely that COVID-19 was a factor in the auditor's conclusion. No adverse audit opinions were reported in 2019 or 2020.

Overall, the impact of COVID-19 on the modification of audit opinions in 2020 auditor's reports appears to have been minimal. Despite the inherent uncertainty associated with the pandemic's impacts, financial report preparers are largely fairly representing their

firm's financial situation, as evidenced by the overall decrease in audit opinion modifications in 2020 relative to 2019.

#### 4. Emphasis of Matter Reporting in 30 June EOY Auditor's Reports

If the auditor considers it necessary to draw users' attention to a matter in the financial report that, in their judgement, is fundamental to users' understanding of the financial report, an Emphasis of Matter (EOM) paragraph is included in the auditor's report. 29 auditor's reports (2%) issued in 2020 included EOM paragraphs, which was a slight increase from 2019 where 24 auditor's reports (1.7%) included EOMs. Nine (37.5%) of the EOMs reported in 2019 carried over into 2020. The most common EOM topics reported in 2020, as detailed below in Table 4, were subsequent events related to the general future uncertainty associated with the COVID-19 outbreak (10 instances), followed by the non-going concern basis of accounting or preparation (five instances) and carrying value of non-current assets (five instances). In 2019, the most common EOMs were related to the non-going concern basis of accounting/preparation with 10 instances, followed by the carrying value of non-current assets (five instances).

**Table 4: Frequency of EOM Topics Reported in 2019 vs 2020**

| <b>EOM Topic</b>  | <b>Frequency (2020)</b> | <b>Frequency (2019)</b> | <b>+/- 2020 vs 2019</b> |
|---|-------------------------|-------------------------|-------------------------|
| Subsequent events (COVID-19 outbreak)                         | 10                      | 0                       | +10                     |
| Non-going concern basis of accounting                         | 5                       | 10                      | -5                      |
| Carrying value of non-current assets                          | 5                       | 5                       | 0                       |
| Contingent liabilities  | 3                       | 2                       | +1                      |
| Material uncertainty relating to carrying value of investment | 2                       | 2                       | 0                       |
| Restatement of comparative balances                           | 2                       | 2                       | 0                       |
| Other (>1 frequency)  | 2                       | 3                       | -1                      |

A further 22 auditor's reports (1.5%) included EOMs titled 'Emphasis of Matter' or 'Emphasis of Matter - Material Uncertainty Related to Going Concern' (EOM-MURGC) but were fundamentally MURGCs, which is not in accordance with AUASB standards<sup>4</sup>. This

<sup>4</sup> ASA 570 *Going Concern* paragraph 22 states that, if a MURGC exists that the auditor agrees is adequately disclosed in the financial report, the auditor's report includes a section titled 'Material Uncertainty Related to Going Concern' which is separate to the reporting of an EOM. As a result, these 22 'EOMs' reported in 2019 and 2020 were treated as MURGCs for the purposes of this analysis.

figure is consistent with 2019. 12 auditor’s reports (0.8%) included EOM-MURGCs across both 2019 and 2020.

Ten of the 29 EOMs in 2020 auditor’s reports (34.5%) were related to COVID-19 by drawing users’ attention to subsequent events disclosures detailing the impacts of COVID-19 on operations and financial position subsequent to year end. These disclosures identified the COVID-19 outbreak as a non-adjusting subsequent event. Although over one-third of all EOMs issued in 2020 were related to COVID-19, the overall number of references to the pandemic was significantly lower than those in KAMs and MURGCs. This may be attributable to auditors’ belief that EOMs are not necessary to convey the implications of COVID-19 on the audit client as it has already been reflected in the financial report and there were no disclosures which were fundamental to users’ understanding of the financial report.

*Variation in EOM Reporting by Audit Client Size and Audit Firm Type:*

All EOMs in 2020 and 88% of the EOMs in 2019 were reported for audit clients outside the ASX 300. This may be attributable to smaller clients’ reduced complexity of operations, meaning matters such as the basis of preparation of the financial report, impact of subsequent events and the carrying value of assets are fundamental to understanding the financial report. In contrast, entities in the ASX 300 are generally larger, more complex and diverse, meaning these types of disclosures may be less fundamental to users’ understanding of the financial report. Thus, as per ASA 706<sup>5</sup>, the auditor is required to include an EOM paragraph drawing financial report users’ attention to the relevant disclosures. As such, all EOMs related to COVID-19 were reported for clients not in the ASX 300. Table 5 details the variation in EOM reporting by audit client size from 2019-2020.

**Table 5: EOM Reporting by Audit Client Size**

| <b>Audit Client Size</b> | <b>EOMs Reported (2020)</b> | <b>Percentage of Total Reports with an EOM (2020)</b> | <b>EOMs Reported (2019)</b> | <b>Percentage of Total Reports with an EOM (2019)</b> | <b>EOMs Referencing COVID-19</b> | <b>Percentage of Total EOMs Referencing COVID-19</b> |
|--------------------------|-----------------------------|---|-----------------------------|---|----------------------------------|--|
| In ASX 300               | 0                           | 0%  | 3                           | 1.4%  | 0                                | 0%   |
| Not in ASX 300           | 29                          | 2.4%  | 21                          | 1.7%  | 10                               | 34.5%  |

<sup>5</sup> ASA 706 *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*

Medium Non-Big 4 audit firms reported the most EOMs as a proportion of total auditor’s reports issued in 2020 with 16 of 515 (3.1%). This was followed by Small Non-Big 4 firms with 2 EOMs (2.2%), Large Non-Big 4 firms with 5 EOMs (1.8%) and Big 4 firms with 6 EOMs (1.1%). This remained largely consistent with 2019, with the only difference being that Big 4 firms issued proportionally more EOMs than Large Non-Big 4 firms. Large Non-Big 4 firms were the most likely to refer to COVID-19 in EOMs with four of five EOMs (80%) drawing attention to the subsequent event of the pandemic. This was followed by Medium Non-Big 4 firms with six of 16 total EOMs (37.5%) referencing COVID-19, while neither Big 4 nor Small Non-Big 4 firms issued EOMs related to COVID-19. Refer to Table 6 for an overview of the variation in EOM reporting by audit firm type from 2019-2020.

**Table 6: EOM Reporting by Audit Firm Type**

| <b>Audit Firm Type</b> | <b>EOMs Reported (2020)</b> | <b>Percentage of Total Reports with an EOM (2020)</b> | <b>EOMs Reported (2019)</b> | <b>Percentage of Total Reports with an EOM(2019)</b> | <b>EOMs Referencing COVID-19</b> | <b>Percentage of Total EOMs Referencing COVID-19</b> |
|------------------------|-----------------------------|---|-----------------------------|--|----------------------------------|--|
| Big 4                  | 6                           | 1.1%  | 9                           | 1.6%   | 0                                | 0%   |
| Large Non-Big 4        | 5                           | 1.8%  | 2                           | 0.7%   | 4                                | 80%  |
| Medium Non-Big 4       | 16                          | 3.1%  | 11                          | 2.2%   | 6                                | 37.5%  |
| Small Non-Big 4        | 2                           | 2.2%  | 2                           | 2.1%   | 0                                | 0%   |

## 5. Going Concern Reporting in 30 June EOY Auditor’s Reports

### *Reporting of Going Concern Key Audit Matters (KAMs):*

When there are events or conditions identified that may cast significant doubt on the entity’s ability to continue as a going concern, it is necessary for the auditor to perform more work in order to conclude if there is Material Uncertainty Related to Going Concern (MURGC) or whether the going concern basis of accounting is not appropriate. If the auditor concludes a MURGC does not exist and the going concern basis of accounting is appropriate, depending on the severity of the issues and the amount of work required in reaching those conclusions, the auditor may conclude that going concern is a key audit matter (KAM). For the purposes of this analysis, a going concern KAM was identified as any KAM with the terms ‘going concern’ or ‘basis of preparation’ in the title. The total number of going concern KAMs increased in 2020 relative to 2019, with 94 (3.5% of all KAMs) in 2020 compared to 80 (3.1%) in 2019. Of

the 94 going concern KAMs reported in 2020, 40 carried over from 2019 while a further 32 reported a MURGC in 2019. Therefore, of the 94 clients which received a going concern KAM in their auditor's report, 72 (76.6%) had existing going concern issues prior to 2020.

32 of the 94 going concern KAMs (34%) referenced the impacts of the COVID-19 pandemic on the respective audit client's operations and financial position. Of the 32 auditor's reports with going concern KAMs that reference COVID-19, 10 (31%) included a going concern KAM and 3 (9.4%) included a MURGC in the previous comparative reporting period. This indicates that the difference in the number of going concern KAMs between 2019 and 2020 may be driven by the impacts of COVID-19.

#### *Reporting of Material Uncertainties Related to Going Concern (MURGCs):*

The number of overall MURGCs decreased in 2020 relative to 2019, with 342 (24.1% of all auditor's reports issued) in 2020 compared to 400 (28.1%) in 2019. Of the 342 MURGCs reported in 2020, 22 (6.4%) were incorrectly identified as EOM or EOM-MURGC while, in 2019, 22 of 400 (5.5%) were identified as such. Of the 342 MURGCs reported in 2020, 266 reported a MURGC in 2019 while a further 28 reported a going concern KAM in 2019. Therefore, of the 342 clients which received a MURGC in their auditor's report, 293 (85.7%) had existing going concern issues pre-2020.

96 (28.1%) of the MURGCs reported in 2020 referenced the impacts of COVID-19, either directly or by drawing readers' attention to notes in the financial report which describe the impact of the pandemic on the client's ability to continue as a going concern. Of the 96 auditor's reports containing MURGCs which reference COVID-19, 67 (69.8%) also contained a MURGC in the previous period. A further six (6.3%) included a going concern KAM in the previous period. This indicates that, in the majority of cases, COVID-19 served to exacerbate existing going concern issues rather than serve as the outright catalyst for MURGC reporting.

Overall, despite the significant impact of COVID-19 during the June 2020 reporting season, the level of auditor reporting on going concern was less than might reasonably have been expected, especially given the unprecedented circumstances. The AASB and AUASB joint publication [The Impact of COVID-19 on Going Concern and Related Assessments](#) (2020) predicted that the uncertainty associated with the COVID-19 pandemic would result in the identification of more events or conditions that may cast significant doubt on the ability to continue as a going concern for entities in the current year compared to previous years.

However, despite an increase in the number of EOMs and going concern KAMs reported, the number of MURGCs decreased significantly compared to 2019, and only 23 MURGCs which referenced COVID-19 (23.9%) in 2020 did not have pre-existing going concern issues in the previous reporting period (in the form of a MURGC or going concern KAM). This is likely due to the robustness of entities' reporting at 30 June 2020, and many had addressed any potential going concern or liquidity issues before year end through capital raisings and access to lines of credit. It also likely that this is at least partially attributable to the success of the government and other assistance available to support businesses, such as Job-keeper wage subsidies, business grants and loan repayment deferrals made available by financial institutions. However, it is expected that the level of going concern reporting will increase again in the coming months and years as such assistance subsides and entities which were significantly impacted by the pandemic, or whose pre-existing liquidity issues were temporarily abated by concessions, struggle to stay afloat.

*Variation in MURGC Reporting by Audit Client Size and Audit Firm Type:*

The vast majority (99%) of MURGCs in both 2019 and 2020 were reported for audit clients not in the ASX 300. This can be attributed to smaller clients' greater likelihood of experiencing going concern issues due to their limited access to funding, reduced flexibility with regards to operations and greater susceptibility to the negative impacts of macroeconomic events. This is consistent with prior research (Carson, Fargher & Zhang, 2016). However, two of three MURGCs reported for clients in the ASX 300 referenced COVID-19 compared to less than one third (27.7%) for clients not in the ASX 300. Table 7 details the variation in MURGC reporting by audit client size from 2019 to 2020.

**Table 7: MURGC Reporting by Audit Client Size**

| <b>Audit Client Size</b> | <b>MURGCs Reported (2020)</b> | <b>Percentage of Total Reports with a MURGC (2020)</b> | <b>MURGCs Reported (2019)</b> | <b>Percentage of Total Reports with a MURGC (2019)</b> | <b>MURGCs Referencing COVID-19</b> | <b>Percentage of Total MURGCs Referencing COVID-19</b> |
|--------------------------|-------------------------------|--|-------------------------------|--|------------------------------------|--|
| In ASX 300               | 3                             | 1.4%   | 2                             | 0.9%   | 2                                  | 66.6%  |
| Not in ASX 300           | 339                           | 28.1%  | 398                           | 33%  | 94                                 | 27.7%  |



Proportionally, the Large Non-Big 4 audit firms, BDO and Grant Thornton, reported the most MURGCs in 2020, with 102 of 271 (37.6%) of all auditor’s reports issued containing a MURGC. This is followed by Small Non-Big 4 firms with 31 MURGCs (34.1%), Medium Non-Big 4 firms with 141 MURGCs (27.4%) and Big 4 firms with 68 MURGCs (12.5%). This order is the same as for 2019. Large Non-Big 4 firms were additionally the most likely to reference COVID-19 in 2020 MURGCs, with 44 MURGCs (43.1% of all MURGCs reported) referencing the pandemic. This is followed by Big 4 firms with 23 (33.8%), Medium Non-Big 4 firms with 24 (17.0%) and Small Non-Big 4 firms with 5 (16.1%). Refer to Table 8 for an overview of the variation in MURGC reporting by audit firm type from 2019 to 2020.

**Table 8: MURGC Reporting by Audit Firm Type**

| <b>Audit Firm Type</b> | <b>MURGCs Reported (2020)</b> | <b>Percentage of Total Reports with a MURGC (2020)</b> | <b>MURGCs Reported (2019)</b> | <b>Percentage of Total Reports with a MURGC (2019)</b> | <b>MURGCs Referencing COVID-19</b> | <b>Percentage of Total MURGCs Referencing COVID-19</b> |
|------------------------|-------------------------------|--|-------------------------------|--|------------------------------------|--|
| Big 4                  | 68                            | 12.5%  | 71                            | 12.8%  | 23                                 | 33.8%  |
| Large Non-Big 4        | 102                           | 37.6%  | 116                           | 42.2%  | 44                                 | 43.1%  |
| Medium Non-Big 4       | 141                           | 27.4%  | 177                           | 35.5%  | 24                                 | 17.0%  |
| Small Non-Big 4        | 31                            | 34.1%  | 36                            | 38.7%  | 5                                  | 16.1%  |

*Reporting of Both a MURGC and Going Concern KAM:*

In 2020, there were 13 auditor’s reports (0.9%) containing both a MURGC paragraph and a KAM related to going concern which is not in accordance with the Australian Auditing Standards<sup>6</sup>. This represents a slight decrease from 2019 whereby there were 14 auditor’s reports (1%) containing both of these. Eight auditor’s reports contained both a MURGC and a going concern KAM in both 2019 and 2020. All of these reports across both 2019 and 2020 were

<sup>6</sup> As per ASA 570 *Going Concern*, the auditor is required to include a separate section in the auditor’s report under the heading “Material Uncertainty Related to Going Concern” when a material uncertainty exists related to events or conditions exist that may cast significant doubt on the entity’s ability to continue as a going concern. However, if there is significant auditor judgement involved in determining whether a material uncertainty related to going concern exists, but the auditor concludes there is no MURGC, the matter may be reported as a key audit matter (KAM) if in the auditor’s judgement it was a matter of most significance to the audit in accordance with ASA 701 *Communicating Key Audit Matters in the Independent Auditor’s Report*.

audited by Small and Medium Non-Big 4 firms with all audit clients outside the ASX 300. These reporting errors may be attributable to confusion among smaller audit firms in understanding and applying the Auditing Standards.

## 6. Key Audit Matter Reporting in 30 June EOY Auditor's Reports

*Average number of KAMs overall, and by industry sector:*

Key Audit Matters (KAMs) are those matters determined by the auditor to be those of most significance and therefore requiring significant auditor attention in performing the audit. In total, 2721 individual KAMs were included across the 1421 separate auditor's reports for clients with years ended 30 June 2020. Across the 1421 auditor's reports for the previous year (2019), a total of 2576 KAMs were reported. Thus, the average number of KAMs reported increased in 2020 to 1.91 compared with 1.81 in the previous year.

Based on GICS industry classification, the highest average number of KAMs in 2020 were reported for audit clients within the Consumer Discretionary sector with 2.45, followed by Telecommunication Services (2.44) and Consumer Staples (2.33). Among all industries within the sample, all but the Real Estate and Telecommunication Services sectors received more KAMs, on average, in 2020 compared to 2019. The greatest average increase in KAMs reported in 2020 relative to 2019 was in the Utilities industry whereby audit clients received, on average, 2.19 KAMs compared to 1.94 in the previous period. See Table 1 for the breakdown of industries represented by audit clients within the sample.

*Number and percentage of KAMs which referred to COVID-19, and by industry sector:*

In total, 320 auditor's reports within the sample included at least one KAM which directly references COVID-19. This represents 22.5% of the entire sample and was the most common method used by auditors to draw financial report users' attention to the impacts of the pandemic on the matters of greatest importance to the audit. Across these 320 auditor's reports, 465 separate KAMs which directly reference COVID-19 were reported. This represents approximately 17% of the total KAMs reported in 2020.

Of the sectors comprising the audit clients within the sample, Real Estate received the greatest proportion of KAMs which reference COVID-19, with 79 of 115 total KAMs (67.5%) reported for audit clients within the sector including direct reference to the impacts of the pandemic. This is likely attributable to the significant impact COVID-19 had on estimation of

asset values in the real estate sector. This was followed by the Consumer Discretionary sector with 115 of 313 KAMs (36.7%) referencing COVID-19 and the Industrials sector with 54 of 255 (21.2%). As these sectors comprise industries such as transportation, retailing and consumer services, the significant proportion of COVID-19 related KAMs is largely attributable to the operational impacts of lockdowns and quarantines imposed by federal and state governments to control the spread of the virus. The industry with the lowest proportion of KAMs which reference COVID-19 to overall KAMs was Materials with just 21 KAMs (2.8% of total KAMs reported). Refer to Table 9 below for the full breakdown of COVID-19 references in KAMs by GICS Industry.

**Table 9: Total KAMs Reported and COVID-19 References by GICS Industry**

| GICS Sector                | Number of Reports | Number of KAMs (2020) | Average KAMs (2020) | Number of KAMs (2019) | Average KAMs (2019) | KAMs Referring to COVID-19 | Proportion of COVID-19 KAMs to Overall KAMs |
|----------------------------|-------------------|-----------------------|---------------------|-----------------------|---------------------|----------------------------|---|
| Materials                  | 467               | 753                   | 1.61                | 716                   | 1.53                | 21                         | 2.8%  |
| Financials                 | 222               | 418                   | 1.88                | 405                   | 1.82                | 79                         | 19.6%                                       |
| Information Technology     | 131               | 299                   | 2.28                | 274                   | 2.09                | 36                         | 12.0%                                       |
| Consumer Discretionary     | 128               | 313                   | 2.45                | 281                   | 2.20                | 115                        | 36.7%                                       |
| Healthcare                 | 126               | 234                   | 1.86                | 227                   | 1.80                | 33                         | 14.1%                                       |
| Industrials                | 115               | 255                   | 2.22                | 235                   | 2.04                | 54                         | 21.2%                                       |
| Energy                     | 95                | 149                   | 1.57                | 148                   | 1.56                | 19                         | 12.8%                                       |
| Real Estate                | 60                | 117                   | 1.95                | 121                   | 2.02                | 79                         | 67.5%                                       |
| Consumer Staples           | 45                | 105                   | 2.33                | 98                    | 2.18                | 17                         | 16.2%                                       |
| Telecommunication Services | 16                | 39                    | 2.44                | 40                    | 2.5                 | 7                          | 17.9%                                       |
| Utilities                  | 16                | 35                    | 2.19                | 31                    | 1.94                | 5                          | 14.3%                                       |

*The most common KAMs overall, and by industry sector:*

The most common KAMs reported by auditors in 2020 were impairment of goodwill and other intangible assets with 391 instances (14.4% of total KAMs reported) and exploration and evaluation with 390 instances (14.4%). These KAMs were additionally the most common in 2019 and increased in number by approximately 5% from 2019 to 2020. Of the most prominent categories of KAMs reported by auditors in 2020 (detailed below), all except those KAMs relating to investments and capitalisation increased in 2020 relative to 2019. This reflects an overall increase in KAM reporting in 2020 relative to 2019. The greatest increase

in reporting on a particular type of KAM relates to the application of new accounting standards, which increased by approximately 56% from 2019 to 2020. This was primarily due to audit clients' recent adoption of AASB 16 *Leases* which resulted in significant changes to the classification of leases. Table 10 summarises the variation in reporting of KAM categories between 2019 and 2020.

**Table 10: Frequency of KAM Categories Reported in 2019 vs 2020**

| <b>KAM</b>   | <b>Frequency (2020)</b> | <b>Frequency (2019)</b> | <b>+/- 2020 vs 2019</b> |
|--|-------------------------|-------------------------|-------------------------|
| Impairment of goodwill and other intangible assets     | 391                     | 370                     | +21                     |
| Exploration and evaluation                             | 390                     | 373                     | +17                     |
| Revenue recognition                                    | 292                     | 287                     | +5                      |
| Investments  | 185                     | 187                     | -2                      |
| Valuation of property, plant and equipment             | 179                     | 160                     | +19                     |
| Taxation   | 131                     | 123                     | +8                      |
| Acquisitions and business combinations                 | 126                     | 123                     | +3                      |
| Share based payments                                   | 106                     | 105                     | +1                      |
| Inventory  | 99                      | 91                      | +8                      |
| Financial instruments and related assets               | 99                      | 87                      | +12                     |
| Going concern/basis of preparation                     | 94                      | 80                      | +14                     |
| Provisions   | 87                      | 79                      | +8                      |
| Receivables and allowances                             | 80                      | 72                      | +8                      |
| Asset impairment (other than goodwill and intangibles) | 76                      | 75                      | +1                      |
| Application of new accounting standards*               | 64                      | 41                      | +23                     |
| Management and performance fees                        | 54                      | 53                      | +1                      |
| Capitalisation   | 46                      | 48                      | -2                      |

\*Specifically AASB 16 *Leases* and AASB 15 *Revenue from Contracts with Customers*

*Auditor's reports which include no KAMs:*

In total, 54 auditor's reports which included no KAMs (3.8%) were issued for clients with 30 June year ends in 2020, compared to 84 (5.9%) in 2019. This indicates that, in 2020, more auditors included at least one KAM in their report to identify the matter(s) that required the most auditor attention. The majority of auditor's reports containing no KAMs were issued for clients in the Materials (20), Financials (14) and Energy (9) sectors. These were primarily

comprised of junior explorers, ETFs/stapled securities and trusts. Additionally, the majority of clients which received no KAMs in their auditor's reports were smaller and less complex with only 2 of 54 in the ASX 300 and an average market capitalisation of \$73.330 million.

*Types of KAMs which referenced COVID-19:*

The 465 individual KAMs which referenced COVID-19 comprised a range of categories, outlining the impacts of the pandemic on various facets of audit clients' operations and financial position, and how the auditor addressed them. The most common KAM categories whereby COVID-19 was referenced were the impairment of goodwill and/or other intangible assets and the valuation of property, plant and equipment. 32 KAMs related to going concern referenced COVID-19 while an additional 20 KAMs were specific to the impacts of the COVID-19 pandemic on operations and financial position. Table 11 summarises the most prominent categories of KAMs which reference COVID-19.

**Table 11: Categories of KAMs Referencing COVID-19**

| <b>KAM Category</b>   | <b>Number of COVID-19 References</b> | <b>Proportion of Total KAMs Referencing COVID-19</b> |
|---|--------------------------------------|--|
| Impairment of goodwill and/or other intangible assets             | 147                                  | 31.6%  |
| Valuation of property, plant and equipment                        | 125                                  | 26.9%  |
| Expected credit loss provisions and recoverability of receivables | 40                                   | 8.6%   |
| Going concern   | 32                                   | 6.9%   |
| Inventory   | 29                                   | 6.2%   |
| Financial instruments and related assets                          | 24                                   | 5.2%   |
| Revenue recognition   | 21                                   | 4.5%   |
| Impact of COVID-19 pandemic                                       | 20                                   | 4.3%   |

Impairment of Goodwill/Other Intangible Assets

147 separate KAMs which referenced COVID-19 were related to the impairment of goodwill or other intangible assets. This represents approximately 31.6% of the total KAMs which referenced COVID-19 for 30 June 2020 auditor's reports. These KAMs were identified as such due to, among other matters, the heightened subjectivity surrounding the valuation of these assets as a result of the COVID-19 pandemic, meaning greater judgement was required to assess impairment. The audit procedures to address these KAMs included evaluating

management's assessment of the impact of COVID-19 on the Group to assess any indicators of impairment.

#### Valuation of Property, Plant and Equipment

125 separate KAMs which referenced COVID-19 were related to the valuation of property, plant and equipment. This represents approximately 26.9% of the total KAMs which referenced COVID-19 for 30 June 2020 auditor's reports. These KAMs were determined as such due to, among other factors, the inherent subjectivity and uncertainty involved in valuation of such assets, which is heightened by the economic uncertainty caused by COVID-19. The audit procedures to address these KAMs included challenging the key inputs and assumptions in management's valuation models, including an assessment of the impact of COVID-19.

#### Expected Credit Loss Provisions/Recoverability of Trade Receivables

40 separate KAMs which referenced COVID-19 were related to expected credit loss provisions or the recoverability/carrying value of trade receivables. This represents approximately 8.6% of the total KAMs which referenced COVID-19 in 30 June 2020 auditor's reports. These KAMs were identified as such due, among other factors, to the heightened subjectivity and estimation uncertainty surrounding the impacts on audit clients' customers. The audit procedures to address these KAMs typically involved consideration of management's forward-looking estimates in ECL models, assessment of the economic environment applicable to customers and questioning the entity's assessment of the impact of the COVID-19 pandemic on the risk of default.

#### Going Concern

32 separate KAMs which referenced COVID-19 were related to going concern issues or the basis of preparation of the financial report. For the purposes of this snapshot, a going concern KAM was identified as any KAM with the terms 'going concern' or 'basis of preparation' in the title. This represents approximately 6.9% of the total KAMs which referenced COVID-19 for 30 June 2020 auditor's reports. These KAMs were identified as such due to the expected continuation of significant economic impacts arising from COVID-19, among other factors, on audit clients' operations and financial position. The audit procedures to address these KAMs included reviewing the appropriateness of management's forecasts in

light of the pandemic impacts and assessing the adequacy of COVID-19 related disclosures in the financial report.

### Inventory

29 separate KAMs which referenced COVID-19 were related to the valuation and/or existence of inventories. This represents approximately 6.2% of the total KAMs which referenced COVID-19 for 30 June 2020 auditor's reports. These KAMs were identified as such due to, among other factors, the economic impacts of the COVID-19 pandemic on the net realisable value of inventory or the physical impacts of the pandemic on auditors' ability to attend stocktakes. Audit procedures to address these KAMs included either challenging management's assumptions in their determination of inventory NRV in light of COVID-19 impacts or virtual attendance at stocktakes.

### Financial Instruments and Related Assets

24 separate KAMs which referenced COVID-19 were related to the valuation of financial instruments and/or related assets. This represents approximately 5.2% of the total KAMs which referenced COVID-19 for 30 June 2020 auditor's reports. These KAMs were identified as such due to, among other matters, the subjectivity in significant assumptions surrounding the valuation of these accounts as a result of the uncertainty associated with the economic impacts of COVID-19. Audit procedures to address these KAMs included challenging the assumptions and inputs in valuation models, including an assessment of the impact of COVID-19.

### Revenue Recognition

21 separate KAMs which reference COVID-19 were related to revenue recognition. This represents approximately 4.5% of the total KAMs which referenced COVID-19 for 30 June 2020 auditor's reports. These KAMs were identified as such due to, among other factors, the disruptions to operations (including store closures and construction projects) as a result of government-implemented COVID-19 lockdown measures. Audit procedures to address these KAMs included consideration of COVID-19 impacts on collection of receivables and developing expectations of future revenue based on various factors including COVID-19.

## COVID-19 Specific KAMs

20 separate KAMs were specifically related to the impacts of the COVID-19 pandemic. These were determined as KAMs with the terms ‘COVID-19’, ‘Coronavirus’ or ‘pandemic’ in the title of the KAM. This represents approximately 4.3% of the total KAMs which referenced COVID-19 for 30 June 2020 auditor’s reports. These KAMs typically detailed the impacts of the COVID-19 pandemic on either the audit client’s operations and financial position or the conduct of the audit. These KAMs were identified as such due to the underlying uncertainty surrounding the short, medium and long-term impacts of the pandemic on audit clients. Audit procedures to address these KAMs typically included an evaluation of management’s assessments regarding COVID-19 impacts and responses to such impacts.

### *Variation in KAM Reporting by Audit Client Size and Audit Firm Type:*

On average, audit clients in the ASX 300 received more KAMs than those not in the ASX 300 with 2.59 compared to 1.80. This variation was largely consistent with 2019. The difference may be attributable to larger clients being inherently more complex, meaning auditors are required to assess a wider range of facets of the client’s operations to provide an opinion. 213 of 554 total KAMs (38.4%) reported for clients in the ASX 300 included reference to COVID-19, compared to just 252 of 2167 (11.6%) for non-ASX 300 clients. This indicates that KAMs served as the primary means for auditors of ASX 300 clients to convey the impacts of the pandemic to financial report users; albeit not in a way that required the reporting of a MURGC or EOM. All qualifications were issued for clients outside the ASX 300. Table 12 details the variation in KAM reporting by audit client size from 2019 to 2020.

**Table 12: KAM Reporting by Audit Client Size**

| <b>Audit Client Size</b> | <b>KAMs Reported (2020)</b> | <b>Average Number of KAMs (2020)</b> | <b>KAMs Reported (2019)</b> | <b>Average Number of KAMs (2019)</b> | <b>KAMs Referencing COVID-19</b> | <b>Percentage of Total KAMs Referencing COVID-19</b> |
|--------------------------|-----------------------------|--------------------------------------|-----------------------------|--------------------------------------|----------------------------------|--|
| In ASX 300               | 554                         | 2.59                                 | 545                         | 2.55                                 | 213                              | 38.4%  |
| Not in ASX 300           | 2167                        | 1.80                                 | 2031                        | 1.68                                 | 252                              | 11.6%  |



On average, Big 4 audit firms issued the most KAMs per auditor’s report in 2020 with 2.1. This is followed by Small Non-Big 4 firms (2.08), Medium Non-Big 4 firms (1.84) and Large Non-Big 4 firms (1.62). This order was consistent with 2019. Additionally, Big 4 audit firms had the greatest proportion of KAMs referencing COVID-19 to overall KAMs with 344 of 1143 (30.1%) referring to the pandemic’s impacts. Large Non-Big 4 firms issued 48 KAMs which referenced COVID-19 out of 440 (10.9%), followed by Small Non-Big 4 firms with 18 of 189 (9.5%) and Medium Non-Big 4 firms with 55 of 947 (5.8%). Refer to Table 13 for an overview of the variation in KAM reporting by audit firm type from 2019 to 2020.

**Table 13: KAM Reporting by Audit Firm Type**

| <b>Audit Firm Type</b> | <b>KAMs Reported (2020)</b> | <b>Average Number of KAMs (2020)</b> | <b>KAMs Reported (2019)</b> | <b>Average Number of KAMs (2019)</b> | <b>KAMs Referencing COVID-19</b> | <b>Percentage of Total KAMs Referencing COVID-19</b> |
|------------------------|-----------------------------|--------------------------------------|-----------------------------|--------------------------------------|----------------------------------|--|
| Big 4                  | 1143                        | 2.10                                 | 1118                        | 2.02                                 | 344                              | 30.1%  |
| Large Non-Big 4        | 440                         | 1.62                                 | 440                         | 1.60                                 | 48                               | 10.9%  |
| Medium Non-Big 4       | 947                         | 1.84                                 | 845                         | 1.69                                 | 55                               | 5.8%   |
| Small Non-Big 4        | 189                         | 2.08                                 | 173                         | 1.86                                 | 18                               | 9.5%   |

## 7. Voluntary Reporting in 30 June EOY Auditor’s Reports

*Reporting on materiality and audit scoping:*

The only firm with auditor’s reports based on Australian Auditing Standards which voluntarily outlines materiality and scoping of the audit is PwC Australia. Of 112 auditor’s reports issued by PwC Australia for clients with 30 June 2020 financial year ends, only two did not include a discussion of the audit materiality and scoping. Both of which were entities whereby no KAMs were reported within the audit opinion. In contrast, 19 of the 40 auditor’s reports (47.5%) which were audited based on ISAs<sup>7</sup> reported audit scoping and/or materiality in 2020. These comprised a wider range of firms including all Big 4 firms, BDO and PKF.

<sup>7</sup> These clients were dual-listed in Australia and in another jurisdiction.

### *Reporting on procedures to determine the existence of a MURGC:*

16 auditor's reports (1.1%) included the auditor's procedures to determine the existence of a MURGC, similarly to the procedures ordinarily reported for KAMs. 14 (87.5%) of these were reported by Big 4 firms KPMG and Deloitte with the remainder reported by Non Big-4 firms. Similarly to KAMs, the degree of detail in the procedures reported varies based on the firm but largely retains a similar format to the 'How the matter was addressed in our audit' section of KAMs.

## **8. 30 June Half-year Review Reporting**

### *Auditor Conclusion Modifications in Review Reports:*

The number of HY review reports with qualified review conclusions decreased slightly from six (2.5%) in 2019 to five (2.1%) in 2020. Three of the qualifications issued in 2020 carried over from 2019. All qualifications in both 2019 and 2020 were issued for clients outside the ASX 300. Only one of the qualified conclusions in 2020 was issued by a Big 6 audit firm compared to three in 2019. Reasons provided for the issuance of qualified conclusions in 2020 included the inability to verify the existence and condition of inventory, collectability of receivables, valuation of investments and sales forecast assumptions in relation to the valuation of CGUs. One disclaimer of opinion was reported in 2020 compared to two in 2019. This was issued for a client in the ASX 300 and audited by a Big 4 firm.

Two review reports issued in 2020 received a qualified review conclusion for reasons including COVID-19 impacts. In one case, this was due to the auditors' inability to review sales forecast assumptions in the financial model in relation to the carrying amount of the CGU as a result of COVID-19 disruptions. In the second case, the report was qualified due to the Directors not providing an estimate for the net realisable value of inventory as a result of COVID-19 slowing the process of identifying potential buyers to allow for a commercial assessment of inventory pricing. One review report issued in 2020 received a disclaimer of conclusion due to uncertainties (including those associated with COVID-19) that were so material and pervasive that the auditors were unable to express a conclusion on the report. All three of these reports which received modified audit conclusions due to matters including COVID-19 received unqualified audit conclusions in 2019. This indicates that COVID-19 had an impact on the modification of review report conclusions in 2020.

### *EOM Reporting in Review Reports:*

The total number of HY review reports which included EOMs increased in 2020 to ten (4.2%), compared to four (1.7%) in 2019. The most prominent topics of EOMs issued in 2020 included subsequent events relating to the COVID-19 pandemic (4 instances) and valuation of non-current assets (2 instances). 18 further review reports (7.5%) contained EOMs that were incorrectly classified as such, as they were fundamentally MURGCs, which is down from 26 (10.9%) in 2019.

Four review reports (1.7%) issued in 2020 included EOM paragraphs relating to the impacts of COVID-19. Consistent with the EOMs issued in auditor's reports in 2020, these highlighted the uncertainty of the impacts of COVID-19 on the client's operations and financial position subsequent to year end, drawing users' attention to disclosures in the financial report which identify the COVID-19 outbreak as a non-adjusting subsequent event.

Two of 10 EOMs (20%) in 2020 review reports were issued for clients in the ASX 300 compared to none in 2019. Incidentally, both of these EOMs were related to the subsequent event of COVID-19 which is in contrast to EOY auditor's reports whereby KAMs were primarily used to communicate the impacts of COVID-19 on ASX 300 clients. This may indicate that auditors of clients in the ASX 300 are using EOMs as a substitute for KAMs (which are not required in a review report) to outline the impacts and uncertainties associated with COVID-19. 6 EOMs (60%) in 2020 were reported by Big 6 audit firms, which is up from 1 (25%) in 2019. 3 of the 4 EOMs related to COVID-19 (75%) were issued by Big 6 audit firms.

### *MURGC Reporting in Review Reports:*

The total number of HY review reports containing MURGCs has increased in 2020 to 82 (34.3%), compared to 67 (28%) in 2019. 55 of the 82 MURGCs (67%) reported in 2020 carried over from 2019, indicating that existing going concern issues were not primarily driven by factors exclusive to the 2020 reporting season.

36 (43.9%) of the MURGCs included in 2020 review reports included reference to COVID-19. Similarly to the 2020 EOY auditor's reports, these MURGCs either directly referred to the impacts of the pandemic on the client firm's ability to continue as a going concern in the MURGC paragraph or drew financial report users' attention to notes in the

financial report which outlined this. Of the 36 review reports containing MURGCs which reference COVID-19, 20 (55.6%) additionally had a MURGC in the previous half-year, which indicates that, in the majority of cases, there were pre-existing going concern issues not solely driven by the impacts of COVID-19.

80 of 82 MURGCs (97.6%) in 2020 review reports were issued for audit clients not in the ASX 300, 35 (44%) of which included reference to COVID-19. Similarly, in 2019, 65 of 67 MURGCs (97%) were reported for clients not in the ASX 300. This suggests a two-tier client base, roughly approximated by the ASX 300. One of the two MURGCs reported for clients in the ASX 300 in 2020 included reference to COVID-19, which carried over from 2019. This supports the notion that smaller clients are more susceptible to significant going concern issues, especially those recently presented by the widespread impacts of COVID-19. 47 MURGCs (57.3%) in 2020 were reported by Big 6 audit firms, up from 31 (46%) in 2019. 27 (75%) of the total MURGCs related to COVID-19 were issued by Big 6 audit firms.

Overall, the proportion of review reports containing reference to COVID-19 was significantly lower than that for EOY auditor's reports, with only 15.9% compared to 28.1%. This is primarily attributable to the limited scope of review reports whereby KAMs, which were the most prominent means of conveying the impact of the pandemic in auditor's reports, are not included. Thus, auditors have less flexibility with regard to the reporting of matters that are not either fundamental to users' understanding of the financial report (i.e. an EOM) or related to the entity's ability to continue as a going concern.

## Conclusion and Research Questions

The unprecedented nature of the June 2020 financial reporting season has led to concerns surrounding the reporting on going concern and solvency assessments, estimation of asset and liability values and disclosure of risks and future prospects. As such, audits are increasingly critical to ensure the accurate representation of companies' financial positions and enhance investor confidence. We provide a snapshot and analysis of auditor reporting over this incredibly volatile and uncertain period, with a particular focus on the impact of COVID-19 on the various facets of auditor reporting.

This analysis demonstrates that the impact of COVID-19 on auditor reporting during the June 2020 period has been significant. In total, 400 (28.1%) of all EOY auditor's reports in 2020 included at least one reference to the COVID-19 pandemic. The number of auditor's reports with qualified opinions has decreased to 16 (1.1%) in 2020 compared to 18 (1.3%) in 2019. Only two auditor's reports in 2020 reference COVID-19 as one of the reasons for the modification.

29 auditor's reports (2%) included EOMs in 2020, compared to 24 (1.7%) in 2019. 10 of the 2020 review reports (34.5%) referenced COVID-19 by drawing financial report users' attention to subsequent event disclosures relating to the impact of COVID-19 on operations.

The number of auditor's reports containing MURGCs decreased significantly to 342 (24.1%) in 2020 compared to 400 (28.1%) in 2019. 94 auditor's reports (6.6%) included KAMs related to going concern in 2020, which represents an increase from 2019 whereby 80 (5.6%) were reported. 96 MURGCs and 32 going concern KAMs reported in 2020 included reference to COVID-19, although 72% of these had a MURGC or going concern KAM in 2019, indicating going concern issues preceding the pandemic.

The average number of KAMs reported in auditor's reports increased from 1.81 in 2019 to 1.91 in 2020, with the most prominent topics including the impairment of goodwill and other intangible assets, exploration and evaluation and revenue recognition. KAMs served as the most common method for auditors to convey the impacts of COVID-19, with 465 individual KAMs (17.1% of all KAMs reported in 2020) referencing the pandemic. The most common categories of KAMs which reference COVID-19 include the impairment of goodwill and other intangible assets and the valuation of property, plant and equipment while audit clients in the Real Estate sector received the greatest proportion of KAMs related to COVID-19 to overall

KAMs with 79 of 117 (67.5%). 138 auditor's reports (4.9%) across both years reported no KAMs at all.

36 HY review reports (15.9%) in 2020 included one or more references to COVID-19. 6 review reports (2.5%) received modified audit opinions compared to 8 (3.3%) in 2019, of which half referenced COVID-19 as a factor contributing to the modification. The number of review reports containing EOMs increased in 2020 to 10 (4.2%) from 4 (1.7%) in the previous year, while 4 included reference to COVID-19 by referring to subsequent events disclosures in the financial report. The number of review reports including MURGCs increased to 82 (34.3%) in 2020, compared to 67 (28%) in 2019. 36 of these 82 MURGCs (43.9%) included reference to COVID-19, 20 (55.6%) of which carried over from 2019.

Overall, despite the significant proportion of auditor's reports in June 2020 which included reference to COVID-19, the level of modified audit opinions remained largely similar to 2019. This indicates that, despite the difficulty and uncertainty faced by financial report preparers, entities are largely fairly reporting the material impacts of the COVID-19 pandemic. Similarly, the reduced level of going concern reporting during the June 2020 reporting period is unexpected given the uncertainty associated with the future impacts of COVID-19 and the disruptions to operations. This indicates that preparers had addressed any potential going concern / liquidity issues via ensuring there was adequate access to cash, and the unprecedented level of government and other financial assistance provided to entities had the desired impact of keeping them operating. However, the AUASB expect the level of going concern reporting to again increase in the coming months and years as assistance provided to entities begins to subside.

Our analysis of the June 2019-20 auditor reporting season prompts a number of further questions. As such, the AUASB propose five research questions which may provide further insights into the future and usefulness of auditor reporting:

1. Will the decreasing trend of modified audit opinions and going concern reporting continue in the coming years? What factors will influence this trend?

As evidenced by the reduction in the reporting of both modified audit opinions and MURGCs in 2020 relative to 2019, the government and other financial assistance provided to entities during the COVID-19 crisis has had the desired effect of keeping them operating. However, it will be interesting to note whether entities have made the necessary plans to ensure

they stay afloat after the assistance subsidies. Therefore, the “true” impacts of the COVID-19 pandemic may be felt by entities in the coming reporting periods, and how this is reflected by auditor reporting will be critical. It will also be interesting to determine whether any additional factors were responsible for this trend, and how these will impact reporting in the future.

2. Do financial report users understand the difference between a MURGC and a going concern KAM? Will they undertake different actions depending on which of these types of auditor reporting is used?

While the number of MURGCs reported has decreased in 2020 relative to 2019, auditors are increasingly reporting on going concern issues through KAMs. Additionally, a small number of auditor’s reports include both a MURGC and going concern KAM. Although the Auditing Standards distinguish between the reporting of a MURGC and going concern KAM, it would be interesting to determine whether financial report users can understand the difference, especially given the potential for more going concern issues to arise in the coming reporting periods as COVID-19 government and financial assistance subsidies. It will be equally important to determine whether the reporting of a MURGC vs a going concern KAM causes financial users to act differently in their economic decision-making.

3. Do financial report users consider voluntary reporting to be useful and how do they use such information?

Presently, voluntary reporting in Australia is limited relative to overseas jurisdictions, with only a small proportion of auditor’s reports containing such reporting. Therefore, it would be interesting to determine whether financial report users find information such as the reporting of audit scoping, materiality and the procedures undertaken to determine the existence of a MURGC to be useful. It would additionally be interesting to determine how, and to what extent, such information is utilised by financial report users in their economic decision-making. This would provide insights into the usefulness of making such reporting more widespread in Australia.

4. Has/will the impact of COVID-19 affect the reporting of KAMs?

Although a significant proportion of the KAMs reported in 2020 auditor’s reports included reference to COVID-19, it remains to be seen whether the pandemic has impacted the reporting of KAMs as a whole. Firstly, it will be interesting to examine the KAMs which

reference COVID-19 in more detail to determine whether they have significantly changed from the previous year or simply carried over. It will additionally be interesting to note the change to KAMs in future reporting periods to determine whether or not they simply revert back to those reported pre-COVID-19.

5. Is the half-year review report sufficiently communicating the key focus areas of the auditor's review?

The inherently limited scope of the review report can be primarily attributed to KAMs, the reporting of which is not permitted in review reports. This is reflected by the reduced level of reporting in review reports compared to auditor's reports, particularly with regard to COVID-19, over 2019-2020. As such, it would be interesting to determine whether financial report users perceive the review report as sufficiently communicating the key focus areas of the review to determine whether the scope of the review report needs to be expanded. The AUASB is currently undertaking a post-implementation review and possible update of ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity* and any such research would greatly contribute to this.



## References

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## Appendix 1 Summary Tables of 30 June Auditor Reporting in Australia

### Summary Table 1 – 30 June 2019 and 2020 Full-Year Reports

|                                      | 2020                      | 2019                      |
|--------------------------------------|---------------------------|---------------------------|
| Total 30 June 2020 Auditor's Reports | 1421                      | 1421                      |
| Total Unmodified Auditor's Reports   | 1038                      | 990                       |
| Total Qualified Audit Opinions       | 16                        | 18                        |
| Total Disclaimers                    | 1                         | 0                         |
| Total MURGCs                         | 342                       | 400                       |
| Total EOMs                           | 29                        | 24                        |
| Total GC EOMs*                       | 22                        | 22                        |
| Total reports with at least one KAM  | 1367<br>(54 with no KAMs) | 1337<br>(84 with no KAMs) |
| Total KAMs                           | 2715                      | 2576                      |
| Average KAMs                         | 1.91                      | 1.81                      |
| Total GC KAMs                        | 94                        | 80                        |

\*MURGCs labelled incorrectly as EOMs (classified as MURGCs for the purposes of this analysis)

### Summary Table 2 – 30 June 2019 and 2020 Half-Year Reports

|                                    | 2020 | 2019 |
|------------------------------------|------|------|
| Total 30 June 2020 Review Reports  | 239  | 239  |
| Total Unmodified Review Reports    | 141  | 160  |
| Total Qualified Review Conclusions | 5    | 6    |
| Total Disclaimers                  | 1    | 2    |
| Total MURGCs                       | 82   | 67   |
| Total EOMs                         | 10   | 4    |
| Total GC EOMs*                     | 18   | 26   |

\*MURGCs labelled incorrectly as EOMs (classified as MURGCs for the purposes of this analysis)

**Summary Table 3 – 30 June 2020 Auditor/Review Reporting: COVID-19 References**

|  | <b>Full-Year Ending 30/06/20</b> | <b>Half-Year Ending 30/06/20</b> |
|--|----------------------------------|----------------------------------|
| Total 30 June 2020 Auditor's/Review Reports Which Reference COVID-19 | 400                              | 38                               |
| Total Unmodified Auditor's/Review Reports Which Reference COVID-19   | 298                              | 0                                |
| Total Qualified Opinions/ Conclusions Due to COVID-19                | 2                                | 2                                |
| Total Disclaimers Due to COVID-19                                    | 0                                | 1                                |
| Total MURGCs Which Reference COVID-19                                | 96                               | 36                               |
| Total EOMs Which Reference COVID-19                                  | 10                               | 4                                |
| Total Reports with at least one KAM that References COVID-19         | 320                              | N/A                              |
| Total KAMs Which Reference COVID-19                                  | 465                              | N/A                              |
| Total GC KAMs Which Reference COVID-19                               | 32                               | N/A                              |