



Caryn Maitland <camaitland@gmail.com>

The impact of the recent civil unrest on audit engagements

1 message

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Reply-To: SAICA Standard and Legislation <saicanewsletters@saicanews.co.za>
To: camaitland@gmail.com

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Dear Caryn

Membership No.: 04855512

The civil unrest that occurred in Kwazulu-Natal and Gauteng between 9 - 17 July 2021 has had a devastating effect on the South African economy. It is estimated that the riots could cost the country approximately R50 billion while 150 000 jobs could be placed at risk. This does not bode well for an economy that was already struggling before the COVID-19 pandemic. While growing inequality, high levels of unemployment and poverty may not have triggered the recent riots, they were certainly contributing factors.

The impact of the civil unrest would have been felt by a lot of companies in South Africa. It is estimated that approximately 200 malls were targeted, 3000 stores were looted, and 1200 retailer outlets were impacted and damaged. Therefore, the economic effects will have an impact on the preparation and auditing of the financial statements of the companies and groups that are affected. Companies and their auditors will need to consider the impact of these riots.

Effects on the audit of financial statements of affected entities

Despite the effects of the civil unrest and the accompanying challenges it brings, auditors are still required to comply with the prescribed pronouncements, including the International Standards on Auditing (ISAs). This includes continuing to uphold the required quality control policies and procedures at both firm and engagement level to ensure that the required level of audit quality is maintained. Auditors should discuss with their clients the impact of the civil unrest on the entity, its operations, reporting and audit timetables and their contingency plans. The civil unrest could potentially cause a delay in clients' preparation of the financial statements.

In May 2020, after the outbreak of the COVID-19 pandemic in South Africa, SAICA issued a [Frequently Asked Questions: The impact of COVID-19 on audit considerations](#) (FAQ) document. While the FAQ may have been published in response to the pandemic, it is SAICA's view that the guidance provided in the FAQ is appropriate and suitable to assist auditors involved in the audit of financial statements of entities that have been affected by the civil unrest. Auditors are urged to consult the FAQ, particularly for guidance relating to:

- a. Specific risks relating to fair value measurement and impairment considerations.
- b. Revision in the risk assessment and the impact on materiality.
- c. The evaluation of the design and implementation of the controls that have been impacted by the civil unrest.
- d. Going concern considerations.
- e. Subsequent events.
- f. Physical verification of assets.

SAICA would also like to highlight the following areas that could warrant further consideration by the auditors:

- **Inventory**
 - Inventory may have been damaged, stolen or may have become obsolete.

- Net realisable value of inventory may have been impacted by the civil unrest.

- **Over-reliance on controls (including automated general and application controls)**

Auditors might aim to place more reliance on a client's controls in order to obtain sufficient appropriate audit evidence. Auditors would have to ensure, however, that the outcome of the assessment and testing of the controls support such reliance. The obligation on the auditor to comply with the requirements of ISA 330, *The Auditor's Responses to Assessed Risks*, has remained unchanged, including compliance with requirements about substantive procedures.

- **Evidence supporting recoverability of insurance claims**

It is expected that as a result of the civil unrest, affected entities will submit claims to their insurers. In South Africa, the state-owned South African Special Risk Insurance Association (SASRIA) covers claims caused by riots, civil unrest and terrorism, and vandalism caused by public disorder. For affected entities, auditors will need to ensure that they obtain sufficient appropriate audit evidence to support the recoverability of the claims.

- **The impact of the civil unrest on the auditor's report**

The potential impact of the civil unrest on the auditor's report may include:

- The reporting of Key Audit Matters (KAMs) for public interest entities;
- Including emphasis of matter paragraphs to highlight certain information disclosed in the financial statements as a result of the civil unrest (e.g. subsequent events disclosures);
- Scope limitations as a result of being unable to obtain sufficient appropriate audit evidence.

- **Non-compliance with laws and regulations (NOCLAR)**

Examples include:

- Breach of Companies Act requirements, specifically:
 - i. Failure to retain any documents, accounts, books, writing, records or other information that a company is required to keep in terms of Section 24 or any other public regulation for a period of seven years, or any longer period of time specified in any other applicable public regulation;
 - ii. Failure to prepare annual financial statements within six months after the end of its financial year in terms of **section 30**;
- Fraudulent actions (in terms of ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*) to inflate results, for example, overly aggressive assumptions, misleading disclosures, and inappropriate support of the going concern basis of accounting.
- Misappropriation of support funds made available by The Department of Trade, Industry and Competition and its Development Finance Institutions, the Industrial Development Corporation and the National Empowerment Fund.
- Non-compliance with the entity's tax obligations, including *inter alia*:
 - i. Failure to submit tax returns on time;
 - ii. Failure to make payment of tax liabilities on time; and
 - iii. Claiming tax relief provided in respect of the unrest (such as the extended ETI subsidy and the PAYE and excise duty payment deferrals) when they do not qualify for this relief.

Auditors need to be alert to the matters mentioned above and ensure that the appropriate level of professional scepticism and professional judgement is applied throughout the audit.

SAICA continues to monitor the impact of the civil unrest on the audit profession, including the need for further guidance.

Regards

Jeanne Viljoen
Acting Senior Executive: Audit and Assurance

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