

IFAC

Comment letter

Expectation Gap – Fraud and Going concern

Although there is no doubt that there is an expectation gap regarding auditing and financial statements, I cannot see any logical reason to join Fraud and Going Concern in one document which is meant to discuss the expectation gap.

Fraud is only one of several reasons why an enterprise may need to address "Going concern". By discussing fraud and going concern in a single document, this will only confuse more unless it is intended to produce a series of documents on going concern - each one devoted to one of the matters which would lead to going concern problems. If this is so then this needs to be stated. If this is the only document that will be produced, it will leave the impression that Fraud is the primary cause of Going Concern problems (which is definitely not the case) and will increase the expectation gap.

I would submit, however, that a detailed paper addressing all the matters leading to the expectation gap, would be helpful.

Let me comment on the expectation gap relating to these two matters.

Fraud

There is an expectation gap relating to the perception that the auditors should uncover any fraud in the presentation of the financial results. This is a matter relating primarily to "materiality" and not to "going concern". A misstatement in the financial statements is not necessarily the result of a fraudulent act. e.g. it can result from an inadequate system of internal control in the processes relating to the preparation of the financial statements or an inadequate appreciation of risks leading to poor provisioning.

Obviously, a fraudulent act, which deliberately aims to cover up a going concern problem, should be discovered by the audit if it is above the materiality levels set by the audit.

I believe the expectation gap relating to fraud is more general. People believe that all fraud should be found by the audit. Should a million dollar misappropriation in a billion dollar enterprise be discovered by the audit – unlikely. This is the job of management.

Going concern

I believe the expectation gap relating to going concern relates primarily to time – for how long will the enterprise be a going concern? I have read many financial statements which contain very detailed descriptions of the matters considered when management has assessed going concern. However, nowhere do they mention "for how long".

It is generally accepted that when discussing going concern, we are talking about at least the following 12 months. 12 months from the end of the reporting period or twelve months from the date of the directors' report and the approval of the financial statements. Or it can be more than twelve months if the matters considered will not reach conclusion in the next twelve months.

Why don't we state clearly to what time period we are referring?

Thank you for letting me comment on this matter.

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31.1.2021