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ICAEW webinar – Auditing Standards Changes and the impact on Sport, Media and Entertainment Industry

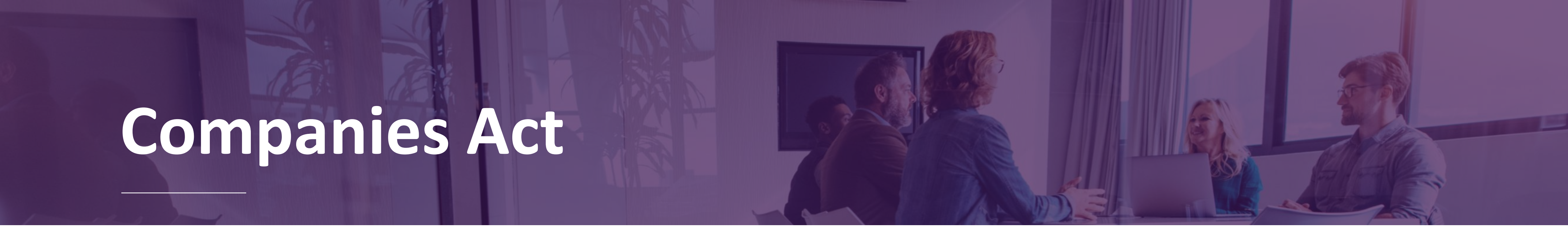
10 February 2021

Introduction to session

- ISA 570 – Going Concern
  - Directors/auditors responsibilities
  - Going concern and COVID-19, what have we learnt
  - Good practice we have seen
  - Description of new standard and auditors responsibilities
  - Reverse stress testing
- ISA 540 – Accounting estimates and judgements
  - Introduction to the new standard
  - Directors/auditors responsibilities
  - Examples from the sector
- ISA 700 – Audit opinion
- Questions

ISA 700 – Forming an opinion and reporting on financial statements

- Revision to ISA 700 requires the Audit Report to include of an explanation of how capable the audit was at detecting irregularities, including fraud
- Expect a change to your audit report in respect of this.
- This section of the report will be tailored to each entity's specific circumstances



Companies Act

Statutory duties as company directors, include the duties to:

- Exercise their powers only for a proper purpose
- Promote the company’s success
- Exercise independent judgement
- Exercise care and skill; and
- Avoid conflicts of interest

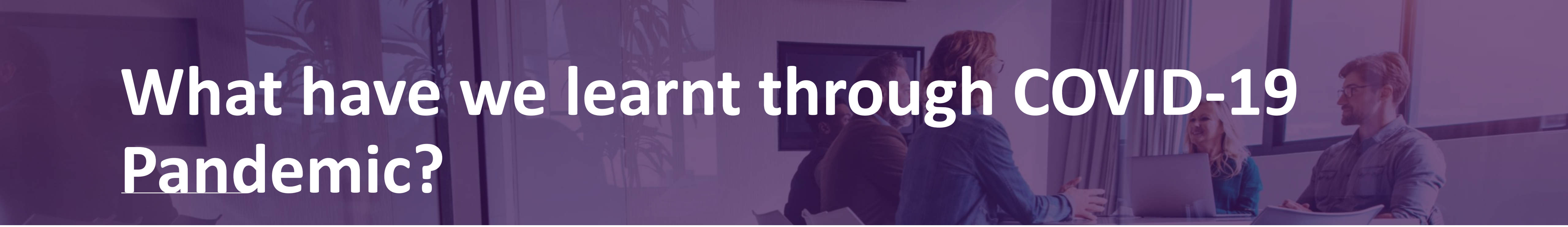
FRS 102 – Accounting Standard Going Concern

- An entity is a going concern unless management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so
- Management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the date when the financial statements are **authorised for issue**
- Management to consider material uncertainties related to events or conditions that cast significant doubt upon the entity's ability to continue as a going concern, the entity shall disclose those uncertainties

Charites SORP

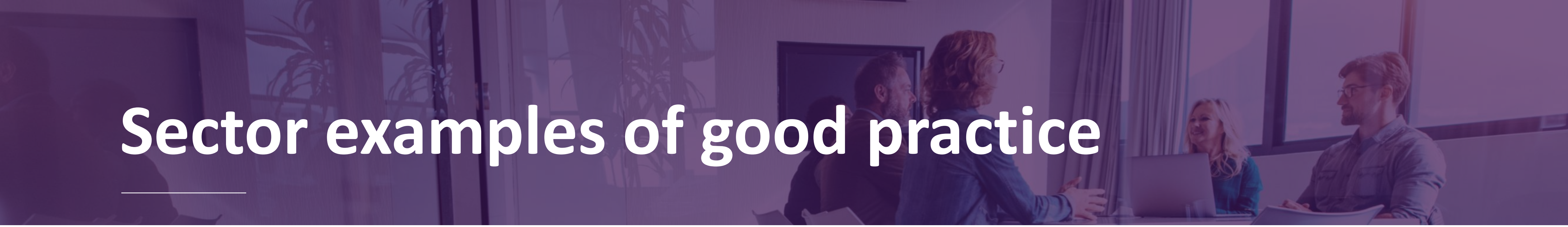
- The trustees **must make their own assessment** of their charity’s ability to continue as a going concern to assure themselves of the validity of this assumption when preparing their financial statements

- Trustees should take into account all available information about the future for at least, **but not limited to, 12 months from the date the financial statements are approved**



What have we learnt through COVID-19 Pandemic?

- The world is more uncertain
- Predicting the future and reviewing going concern can be very difficult
- Sustainability has had high priority out of necessity
- Review what we can do more efficiently
- Cashflow forecasting extremely important
- Assessing a range of scenarios important
- We need to think in worst case terms
- Those with the best financial governance have generally responded better



Sector examples of good practice

- Formal papers being prepared for boards which clearly forecast cash on base and worst-case scenarios that are reviewed and challenged by the board and with formal minute
- Longer than 12-month forecasting
- Clear documentation and justification of assumptions made in forecasts
- Range of scenarios
- Clear disclosure in financial statements

Key Assumptions

- Impact on live events – timescales
  - Live attendances are sport, theatres, cinemas etc, when?
  - Impact on other income streams
  - Cost savings
- Memberships
  - Predicting impact of future renewals
  - Not always down!
- Reliance on government funding schemes
  - JRS
  - CBILS
  - Likelihood of obtaining
  - Covenant obligations

Accounting policies

Notwithstanding the net current liabilities position at 31 December 2019 of £489,008 (2018: £8,689,724), the financial ~~statements have been prepared on a going concern basis. This is also the conclusion of the Club's Board after~~ taking full consideration of the material uncertainties faced by the Club resulting from the Covid-19 pandemic that is affecting both the UK and World's economies.

As set out in the Board's Responsibilities Statement on page 29, in preparing these financial statements the Board is required to prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Club will continue in operation. The Club currently meets its day to day working capital requirements with, when required, the help of an overdraft facility which will be in place until at least the end of March 2021. However, following the UK government's announcement on 22 March 2020 that there must be no group gatherings for the foreseeable future, the Club has been forced to close down its day to day operations. This has placed a far greater demand on the Club's financial resources and forced the Board to revisit its financial projections for the next twelve months after assessing the impact of limited or no cricket during the summer and a continuing cessation of its other core businesses. The Board have considered a range of scenarios ranging from merely a truncated cricket season covering the second half of the summer right through to a worse-case scenario where there is no cricket of any form in 2020 and the Club's hotel and conference and events business fails to re-open until early 2021. Under each of these sets of circumstances prudent assumptions have been made on the impact on each of the Club's revenue streams and how it can reduce costs whilst limiting the impact on the Club's ability to maximise its returns as soon as the pandemic is over and there is a return to trading as normal.

In preparing these projections the Club has reflected the committed financial support from the England & Wales Cricket Board and agreement by its bankers, Metro Bank plc, to extend a capital repayment period and waive any financial covenants for the next twelve months. The Club has also taken advantage of government support in reducing business rates, allowing deferral of VAT payments and to help continue paying salaries as well as taking measures to cease all non-critical revenue and capital expenditure and agree payment deferrals with suppliers that are able to help. In addition, whilst the above will ensure that the Club returns to being fully operational, the Board have considered and identified further measures that could, albeit without any absolute certainty, be put in place to ensure the Club's survival should the pandemic continue well beyond the summer and to the end of the year. These measures include insurance claims on the Club's Business Interruption policy and exploring opportunities available under the Government Business Interruption Loan Scheme and other forms of external investment that could provide long as well as short term support.

The Board has reviewed in detail these updated Club cash flow projections and the supporting banking facilities and funding options and considered the Club's ability to discharge its liabilities as they fall due. In doing so, and despite the challenges faced, they have a reasonable expectation that the Club has adequate resources to continue in

Accounting policies

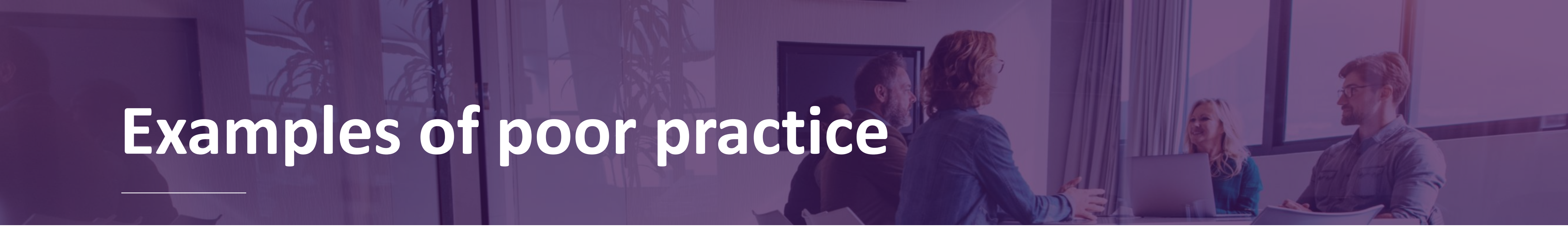
Going concern

Notwithstanding the year end consolidated balance sheet, which shows net current liabilities of £49,749,074 (2018 - £49,152,018) and net liabilities of £48,586,951 (2018 - £48,599,556), the financial statements have been prepared on a going concern basis.

As part of their going concern considerations, the directors have prepared detailed forecasts for the period to 28 February 2021 as part of the longer term forecasts prepared for the company. These forecasts show that the company needs additional funding from its shareholders for the period from June 2019 to February 2021.

The group has received written confirmations from its shareholders of their intention to continue to provide support to the group by not demanding repayment of loans owing to them for the foreseeable future. Shareholders have also confirmed to the parent company their intention to provide or source funding, as required by the parent company. The parent company has confirmed to Otium Entertainment Group Limited, its undertaking, to provide continuing support which will enable the group to continue as a going concern. Notwithstanding this intention, there is no contractual certainty that such funding will be made available nor that the shareholders loans will not be called upon for repayment within the next 12 months. This casts significant doubt on the company's ability to continue as a going concern.

The board continue to explore the possibilities of a return to the Ricoh for the playing season 2020-21, but in the absence of any agreement being reached, would seek to implement the option to continue the ground share at St. Andrew's. Therefore, at the date of approval of these financial statements, there remains uncertainty regarding the outcome of these negotiations. This uncertainty regarding the venue for the 2020-21 season may also cast significant doubt on the company's ability to continue as a going concern.



Examples of poor practice

- Reliance on a budget with limited cash flow forecasting
- Limited board input and challenge
- One scenario, limited thought about “what if?”
- Lack of realism over uncertainties

Introduction to ISA 570 (Revised) - Context

A response to high profile corporate failures – e.g. Carillion, BHS and Thomas Cook and focus on audit quality and effectiveness

New positive statements in the audit report that:

- Conclusion that management's use of going concern basis is appropriate
- No material uncertainty has been identified
- Clear positive conclusion on management's assessment of going concern for public interest entities, listed companies and very large private companies

Changing requirements for Auditors – Risk evaluation

More work is now prescribed in areas such as:

- The evaluation of methods used by management
- The evaluation of the relevance and reliability of the underlying data used by management
- The evaluation of the assumptions made by management in their assessment
- The evaluation of management’s plans for future actions and consideration of whether these are feasible

Changing requirements for Auditors – Greater challenge

- Greater challenge of management’s assessment of going concern
    - Thorough test of the adequacy of the supporting evidence,
    - A new term “management bias”
    - Evaluation of the risk of possible bias in the preparation of management’s assessment

Changing requirements for Auditors

- A “stand back” requirement for auditors to consider all of the evidence obtained, whether corroborative or contradictory, when the auditor draws their conclusions on going concern

- Increased documentation requirements
  - Understanding of the entity
  - Indicators of management bias
  - Significant judgements made in the auditors review of the going concern assessment and disclosures.

Reverse stress testing

- A reverse stress test is a stress test that starts from the opposite end – with the identification of a pre-defined outcome
    - What would it take for the entity to fail?
    - What individual event, or sequence of events, could lead to this outcome?
    - What can be done now to avoid this?

Introduction to ISA 540 (Revised) - Context

- Similar reasons for introduction as with ISA 570

- Carillion
  - £1.6bn of Goodwill (35% of total assets)
  - No impairment of goodwill in 5 years to 2017 despite losses in those businesses

Introduction to ISA 540 (Revised) – Risk Assessment

- Enhanced risk assessment procedures and requirements for separate inherent risk and control risk assessments
- Introduction of the concept of the spectrum of inherent risk
- Enhanced emphasis on the auditor's review of relevant controls over accounting estimates

Introduction to ISA 540 (Revised) – Audit procedures

- A requirement for further audit procedures to respond to the assessed risks of material misstatement – the higher the assessed risk the more persuasive the audit evidence needs to be
- Three types of procedures
  - Review of post year end outcomes
  - Review of entity calculation
  - Auditors reperformance of calculations
- Increased levels of audit analysis on testing methods, data and assumptions used by management in making estimates

Introduction to ISA 540 (Revised) – Challenge

- Professional scepticism – “a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence”
- Management bias (again) – “A lack of neutrality by management in the preparation of information”
- Audit work is designed and performed by the auditor to be balanced so it is not biased towards obtaining corroborative evidence or towards excluding contradictory evidence

Examples of estimates in the sector

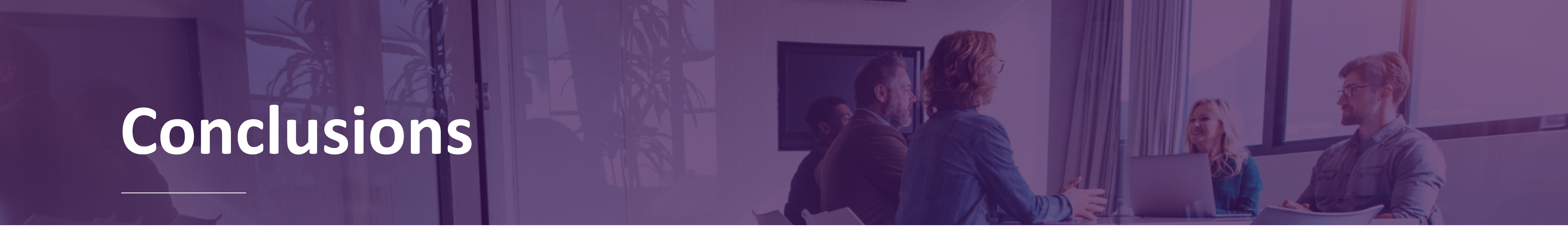
HBO

Common Estimates

- Property valuations
- Stock and receivables provisions – particularly at present
- Depreciation and amortisation policies
- Provisions for liabilities
- DB pension scheme
- Other asset impairment
    - Intangibles
    - Investments

What should you do?

- Review your accounting estimates
- What is your basis for making the estimate, document how and why it is appropriate?
- Consider the need for expert valuation
- Perform impairment reviews
- Review what has happened post year end prior to audit
- Consider you financial statements and improving disclosures



Conclusions

- The changes to ISA 540 and ISA 570 although not ground breaking increase the onus on auditors to challenge management in these areas. Both are prescriptive standards.
- Expect more scrutiny and a higher bar of evidence to your auditors in these areas. Particularly if you are a high going concern risk or you have several significant estimates or judgements in your financial statements.
- Be prepared!

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