

# MANDATORY REPORTING ON FRAUD AND GOING CONCERN IN THE AUDITOR'S REPORT TO THE ANNUAL ACCOUNTS

What does this mean for you, as a client?

Royal Netherlands  
Institute of Chartered  
Accountants

**NBA**

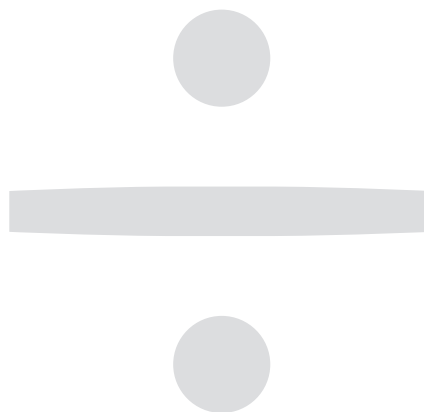
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## CLARIFICATION OF THE DUTIES OF THE AUDITOR WHEN AUDITING THE ANNUAL ACCOUNTS

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Users of the annual accounts, like investors, supervisory bodies, and banks, have been wondering for some time which work the auditor performs regarding to fraud and going concern when auditing the annual accounts. Investors and other interested users of annual accounts also have an increasing need for transparency in both the annual accounts and the board/management report on, for example, company-specific insights and long-term perspectives.

In order to fulfil this need, auditors are required to report on (their work performed on) fraud and going concern in their auditor's report as of the audit year of 2022<sup>1</sup>. Not in general terms, but specifically with respect to the client, with a focus on the identified risks, the work performed, and, if possible and relevant, the outcomes of this work. In other words, the report for the user of the annual accounts will be more tailored.

This brochure describes what this change means for you, and what is expected from you during an audit.

## EARLIER ADOPTION

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Even though the report on fraud and going concern in the auditor's report is not yet mandatory for the financial year of 2021, the NBA is already calling on auditors to report on these topics because of their public interest. This offers both the auditors and yourself the opportunity to gain experience with the early adoption before the new standard actually takes effect.

But what does this actually mean? Auditors will start a conversation to further improve both your and their report on these topics in the coming months.

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<sup>1</sup> Audits of organisations with a public interest (Dutch OOBs) are already required to report on fraud as of the audit year of 2021.



# FRAUD REPORT

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## WHY SHOULD AN ORGANISATION REPORT ON FRAUD?

A global study conducted in the period from January 2018 to September 2019 shows that respondents identified 2,504 cases of fraud. The 2,504 cases of fraud led to more than \$3.6 billion dollars in damage for the organisations involved.<sup>2</sup>

Fraud can have a great impact on the reputation of organisations and can (as set out in the frame above) lead to large financial losses. This is why it is in the interest of both yourself and your stakeholders, including purchasers, investors, and banks, that you pay explicit attention to control fraud risks in your board/management report.

This is why you are expected to identify fraud risks and take adequate measures to control these. Because fraud involves deliberate actions by employees or the management, a thorough fraud risk analysis is also in the interest of yourself, your management and your organisation in order to prevent actual fraud.

If you subsequently provide information about the way how to control fraud (for example, in the risk section of the board/management report), and, if applicable, suspected fraud, conducted investigations, and measures taken to avoid recurrence, insofar as these are public, this contributes to the trust stakeholders have in your organisation. This will benefit your relationship with them.

## IMPACT OF AUDITOR ATTENTION ON FRAUD RISKS

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The fraud risk analysis you conducted yourself (as discussed above) will serve as the point of departure for auditors when performing their work related to fraud risks. Taking into account the reporting obligations for auditors that will take effect for the financial year 2022, based on which they will discuss fraud in their report, auditors will already discuss this topic with you in 2021. During the audit, the auditor will discuss the following with you:

- the fraud risks analysis of the organisation and organisation-specific fraud risks;
- the assessment of fraud risks that are the most relevant to the audit;
- potential fraud incidents and corresponding follow-up.

As of 2021, the auditor will also want to discuss the contents of the auditor's report with you, and how the auditor will refer to the risk analysis described by you in the board/management report. By already discussing the fraud risk factors, previously identified fraud risks, and the corresponding reporting by the auditor, you will be better able to acknowledge relevant risks and to adapt accordingly and make your internal control measures more effective.

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<sup>2</sup> ACFE Report to the nations: 2020 Global study on occupational fraud and abuse

# REPORTING ON GOING CONCERN

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## WHY SHOULD AN ORGANISATION REPORT ON GOING CONCERN?

Between 2015 and 2020, an average of 3,349 companies and institutions went into liquidation (source: Statistics Netherlands). According to a study by Statistics Netherlands, an unpaid debt of 4.4 billion euros remained after settling the liquidation proceedings of companies and institutions in 2015. The overall debt of the settled liquidation proceedings amounted to 4.9 billion euros in 2015. An amount of 464 million euros (9.5 per cent) was repaid to creditors.

From the perspective of reporting obligations, directors of organisations have an important responsibility to provide information about the ability to continue as a going concern and potential risks and uncertainties in this respect. Information based on which users of the annual accounts can make decisions. The users of the annual accounts have an increasing need for transparent information about, for example, company-specific insights and long-term perspectives. Laws and regulations, specifically RJ Guideline 170, offer guidelines for the necessary disclosures. You are expected to offer adequate notes to the annual accounts and the board/management report.

Considering the economic damage of liquidation proceedings (refer to the frame above), and because the preparation of the annual accounts is based on the going concern assumption, going concern is also an important topic of auditors when auditing the annual accounts. Directors, their supervisory bodies, and auditors have a shared interest in identifying and reporting on going concern risks in a timely fashion<sup>3</sup>.

## IMPACT OF AUDITOR ATTENTION TO GOING CONCERN RISKS

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If the auditor pays more attention to going concern risks, this may lead to organisations reflecting on their going concern assumption more often, acting on this, and to (more extensive) reporting in the board/management report. The auditor can rely on this and refer to the relevant section in the auditor's report.

In case of going concern risks, you are responsible for conducting a detailed evaluation to determine to what extent the organisation can maintain its ability to continue as a going concern, including a cash flow and/or covenants forecast<sup>4</sup>. The auditor will assess these plans and measures and evaluate the forecasts. As of the financial year of 2022, he or she will also report on this work.

Discussing going concern risks and the associated measures and disclosures to the annual accounts and the auditor's report in a timely fashion contributes to the effectiveness of the audit of the annual accounts. In addition, the informative value of the annual accounts and the auditor's report for users of your annual accounts will increase.

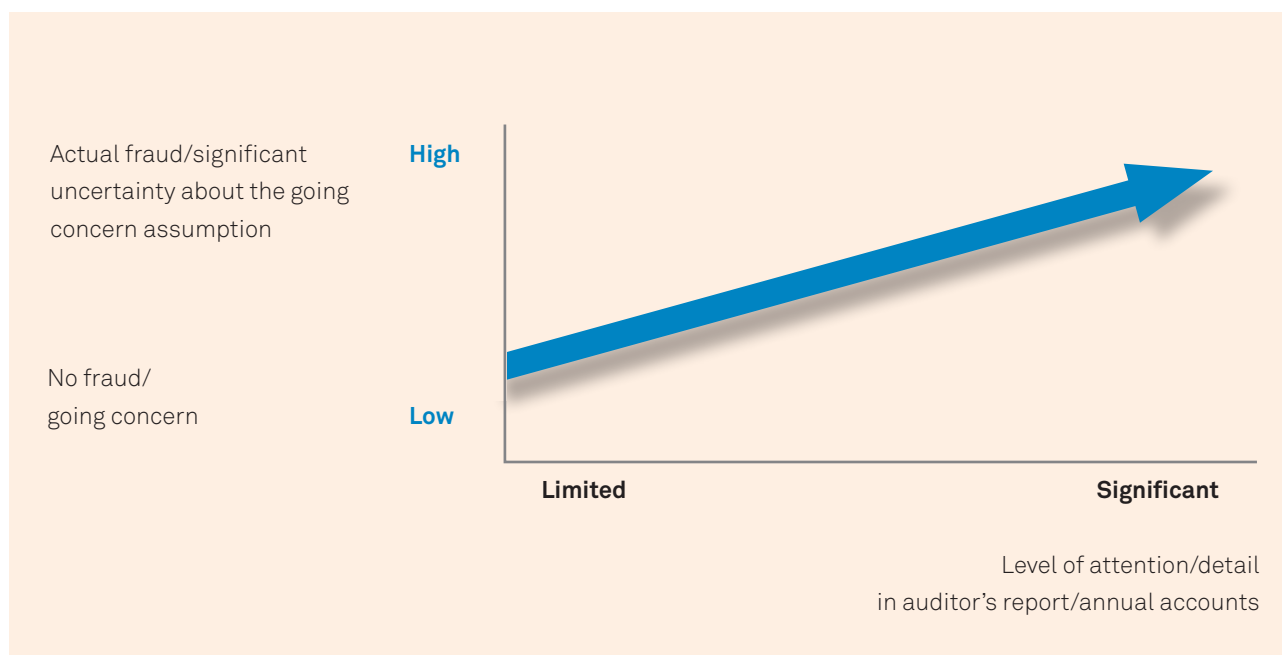
<sup>3</sup> Refer to Audit Standard 570 Going concern

<sup>4</sup> Covenant forecasts: a forecast of the financial situation to determine to what extent the financing covenants will be achieved, for example, if measures X and Y are successful or unsuccessful.



# CONTENT OF THE FRAUD AND GOING CONCERN SECTION IN THE AUDITOR'S REPORT

The level of detail and the extent of the report on fraud and going concern in the auditor's report depend, inter alia, on the identified risks, the scope, and the nature of the organisations, as well as the findings arising from the work. This means that as the suspicions and signs of fraud become clearer or the extent of the going concern risks increase, the disclosures in the annual accounts and the text in the relevant sections in the auditor's report will become more extensive. If there is little to report on, the report may be briefer. The image below illustrates this.



The fraud and going concern section in the auditor's report will be tailored to the customer in the own words of the auditor. However, the sections have a specific structure:

### **Structure of fraud section:**

- The fraud risk factors relevant to the auditor and the identified fraud risks will be listed. Management override is always a fraud risk. In addition, a fraud risk related to turnover reporting will often be included;
- A description of the audit work performed by the auditor to mitigate these risks, addressing the specific circumstances of the organisation;
- (Optional) A description of the specific findings if the circumstances and outcomes of the work require.

### **Structure of going concern section:**

- A description of the going concern risks identified by the organisation and a reference to the relevant notes to the annual report, if applicable;
- A description of the work performed by the auditor when assessing (i) the evaluation by the organisation concerning the ability of the entity to continue as a going concern and (ii) the related disclosures to the annual accounts, if applicable;
- (Optional) The findings of the auditor concerning the suitability of the application of the going concern assumption by the organisation when preparing its financial overviews.

## CONCLUSION

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The NBA expects that this brochure is a first step towards clarifying the upcoming new regulations concerning the auditor's report, specifically with respect to the themes of fraud and going concern, and what is expected from you. Discuss these changes with your auditor in a timely fashion and determine the impact on your board/management report together. A joint step forwards by you and your auditor in order to achieve a greater informative value for the users of annual accounts





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