

Research on Audit Risk of Transportation Industry -- from the Perspective of Key Audit Matters

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Keywords: Audit risk, Key audit matters, Transportation industry

Abstract: From the perspective of Certified Public Accountant and the particularity of the transportation industry, this paper studies the audit content and audit risk based on the perspective of key audit matters. By using the typical cases in transportation industry, this paper sums up the audit risks easily produced in transportation enterprises, evaluates the procedures adopted by the Certified Public Accountant, and then puts forward the countermeasures through the problems revealed by the cases. This paper summarizes the audit risk of transportation industry by the way of case study, which is of practical significance for transportation enterprises to avoid similar risk in operation.

1. Introduction

Key audit matters are those that the Certified Public Accountant considers, in its professional judgment, to be of the greatest importance to the audit of the current financial statements. After the financial crisis in 2008, the information content of the standardized audit report under the traditional model is little, the audit process is not transparent and other shortcomings highlighted. With the heated discussion in the academic circle, the international community has carried on the audit report reform one after another. In order to improve our market economy system, China also carried on the audit report standard reform in 2016 with the disclosure of key audit items as the core. China fully implements new auditing reporting standards from 1 January 2018. According to the requirements of the standards, in addition to the audit reports that cannot express an opinion, the audit reports of the financial statements of listed companies will be added to the 'key audit items' section to disclose the personalized information related to the audited items, to increase the information content and relevance of audit reports and improve the transparency of audit projects. This is the biggest change in audit reporting in decades. How To better disclose key audit matters and how to convey information accurately and appropriately to information users in audit reports is a question that every Certified Public Accountant should consider.

At present, there is still a serious disconnection between the theoretical research and the actual situation in China. There is not much research on the actual problems of the Certified Public Accountant in communicating key audit matters, how to improve the system, and how to put forward corresponding practical suggestions. This is the breakthrough point of this paper.

2. Certified Public Accountant 1504 -- Communicating Key Audit Matters in an Audit Report

2.1 Nature of Key Audit Matters

Key Audit Matter (KAM) is the matter which, in the opinion of the Certified Public Accountant, is of the greatest professional importance to the Audit of the current financial statements. The objective of the Certified Public Accountant is to identify and, after forming an opinion on the financial statements, communicate the key audit matters in a manner described in the audit report. (Standard 1504, Arts. 7,8) Key audit matters may relate to areas where the risk of material misstatement is high. Key audit items may also relate to particular risks identified by the Certified Public Accountant, such

as areas of the financial statements that involve significant management judgment, current significant transactions or events. Key audit matters should come from ‘matters communicated with the management’. In practice, the matters communicated with the management should be used as a starting point for identifying the key audit matters, followed by the selection of those that have been the focus of attention in the implementation of the audit. The Certified Public Accountant then selects the most important of these ‘focused matters’ as the key audit matters.

2.2 Difficulties in Identifying and Reporting Key Audit Matters

In practice, there are still many difficulties in how to determine the key audit matters and how to describe the key audit matters in the audit report.

How to apply the ‘most important’ concept. Identifying the key audit matters that need to be communicated in the audit report is highly dependent on the professional judgment of the Certified Public Accountant. In practice, Certified Public Accountant differ on how to understand ‘most important’, leading to widely varying professional judgments about what matters and how much matters matter most. Too Few or too many key audit items may not be appropriate for the information user. If the disclosure is not disclosed, it will be difficult to achieve the reform goal of the audit report; if too much information is disclosed, it may lead to information overload and reduce the value of the Audit Report.

How to avoid standardized descriptions. Guidelines for the application of the guidelines refer to ‘the need to relate matters directly to the specific circumstances of the auditee and to avoid the use of generic or standardized language’. However, in practice, the description of key audit matters of the same nature tends to be standardized and templated for the purpose of avoiding risks. This tendency is particularly evident for critical audit matters that are prevalent in the same industry. How to emphasize the specific aspect of the audited entity through the appropriate description, avoid the common language or the general formula in the industry, is a practical problem.

3. Analysis of Audit Report Forms of Listed Companies in Transportation Industry

This paper collected and analyzed the 2017 audit reports of 34 listed transportation companies: (1) the railway transportation industry, including Western entrepreneurship, Tie Long logistics, Da Qin railway, Guangzhou–Shenzhen Railway; (2) the road transport industry includes Guangdong Expressway A, modern investment, investment-inviting highway, Yangtze River Investment, Nanjing-shanghai Expressway, Shenzhen Expressway, Hunan Investment, Dongguan holding, Yichang Jiao Yun De Xin Jiao Yun; (3) water transport industry includes Shenzhen Chi Wan A, Zhuhai port, Chang Hang Phoenix, Jinzhou port, Xiamen Port, Port of Dalian, Strait shares, Rizhao port, Shanghai Port Group, COSCO Hai Neng ; (4) the air transport industry includes Hua Xia Aviation, Shan Hang B, Guangzhou Bai Yun International Airport, Shanghai airport, China Southern Airlines, China Eastern Airlines, hna holding, Xiamen airport, Chunqiu aviation and Air China.

Table 1 Statistics on The Types of Key Audit Matters of Railway Transportation Company

Types	Key audit matters	Companys
Revenue recognition	Revenue recognition-accuracy	Western business start-up, Iron Dragon Logistics
	Recognition-occurrence	Western business start-up
	Revenue recognition-cut-off	Western business start-up
Accounts receivable	Impairment of accounts receivable	Da-Qin railway, Guangzhou–Shenzhen Railway
Net realizable value of inventory	Inventory realizable net value	Iron Dragon logistics

Table 2 Statistics on The Types of Key Audit Matters of Road Transportation Company

Types	Key audit matters	Companys
Revenue Recognition	Revenue recognition-authenticity	Dexin transportation, Yangtze River Investment,

		Dongguan Holding, Yichang transportation,
	Revenue recognition-accuracy	Hunan Investment
Long-term equity investment	Long-term equity investment	Guangdong Expressway, investment highway, Hunan Investment assets impairment
Impairment of assets	Intangible asset	Shenzhen Expressway, Modern investment, Investment road
	Impairment of accounts receivable	Yangtze River Investment, Dongguan Holding
	Depreciation of fixed assets	Guangdong Expressway
	Income from disposal of assets	Yichang delivery intangible asset
Intangible Asset	Intangible Asset Amortization	Shenzhen Expressway and Nanjing-Shanghai expressway

Table 3 Statistics on The Types of Key Audit Matters of Water Transportation Company

Types	Key audit matters	Companys
Revenue Recognition	Revenue recognition-authenticity	Zhuhai Port, Strait shares, Shanghai Port Group, COSCO Haineng, Jinzhou port
	Revenue recognition-accuracy	Zhuhai port, Shanghai Port Group, COSCO Haineng
Accounts receivable	Provision for bad debts	shenchiwan, Changhang Phoenix, Xiamen Port
Long-term Equity Investment goodwill	Long-term equity investment	Strait stock
	Goodwill impairment	Rizhao port
Asset impairment	Ship impairment	COSCO Haineng
	Reserve for inventory decline	Jinzhou port
Major acquisition merger	Acquisition and reorganization of major assets	COSCO Haineng
Related party transaction	Related party transaction-sale business	Ningbo Shipping
	Related party relationship and completeness of disclosure of related party transactions	Rizhao Port, Port of Dalian
Other	Fair value measurement to equity method accounting	Shanghai Port Group
	Merger of enterprises under different control	Shanghai-hong Kong group

Table 4 Statistics on The Types of Key Audit Matters of Air Transportation Company

Types	Key audit items	Companys
Revenue Recognition	Revenue recognition-authenticity	Air China, HNA Holdings
	Revenue recognition-accuracy	Air China, HNA Holdings
	Revenue recognition-passenger services	huaxia Airlines, Shanhang B, China Southern Airlines, Spring and Autumn Airlines, Baiyun Airlines, Shanghai Airlines
Other	For-profit leasing aircraft and engine rental and repair preparation	Huaxia Airlines, Shanghai Airlines
	Operating rental aircraft and engine overhaul costs	Shanhang B, Air China
	Assessment of book value of aircraft and engines	Air China
	Aircraft and related equipment	China Southern Airlines, Xiamen Airport
	Major repair preparation	china Southern Airlines, Xiamen Airpor

4. Conclusion

General key matters refer to key matters that involve at least two or more companies. The number of key audit items disclosed by each of the 34 companies in this survey ranged from 1 to 4, with a maximum of 4 key items. After summing up, it can be concluded that the most frequently disclosed

items in the 2017 audit reports of listed transportation companies are revenue recognition, impairment of receivables from the sale of goods and services, preparation for major repairs of operating leased aircraft and impairment of assets such as aircraft and ships, impairment of long-term assets (except goodwill), impairment of goodwill, franchising and major acquisitions, together they account for more than 70 per cent of the industry's total number of critical audits.

In order to deal with the possible problems in practice, it is very important to identify and describe the key audit matters properly and use professional judgment reasonably. To define and describe the key audit items is not to mechanically 'follow the script', nor 'follow the clouds', but from the point of view of information users, the specific situation of the audited units and audit business 'tailored'. Specifically, the following aspects should be done well.

5. Strengthen Learning and Training

Key Audit matters place new requirements on the professional competence of the Certified Public Accountant. The firm shall organize targeted study and training, comprehensively improve the understanding and mastery of the standards of the practitioners, and help the practitioners correctly understand the objectives of the audit report reform and the connotation of key audit matters. At the same time, internal research and discussions should be actively carried out in the light of the problems found in the implementation process and the experience gained, to further emphasize the importance of professional judgment in the proper application of the guidelines.

6. Early Consideration of Key Audit Matter

While communication of key audit matters affects primarily the work at the audit report stage, consideration of key audit matters at a later stage may result in inadequate communication. It may also place greater time pressure on the timely completion of audits. Therefore, key audit matters can be considered as early as possible during the audit planning stage and preliminary views can be communicated to the auditee in a timely manner, ensure that the results of the procedures implemented and the audit evidence obtained throughout the audit process are fully considered in the final determination of key audit matters.

7. Strengthen Communication with the Auditee

Proper communication of key audit matters in the audit report requires the full support and cooperation of the auditee. The Certified Public Accountant needs to engage in active and in-depth discussions with management and governance on the identification, response, and disclosure of key audit matters to resolve any differences that may arise in a timely manner. Adequate two-way communication will not only help the Certified Public Accountant to develop a final view of the key audit matters, but will also help management and governance to take these matters seriously and to disclose them in the financial statements, thus promotes the financial report quality the enhancement.

8. Dare to Innovate and Try

There is no ready experience for critical audit matters, and the standards do not mandate the description of critical audit matters and the level of detail required. To avoid problems described repeatedly with peers or previous years, Certified Public Accountant needs to be proactive and innovative. For example, an attempt could be made to provide more in-depth insight by providing qualitative comments on certain accounting estimates where significant estimation uncertainties exist; or an attempt could be made to highlight key audit matters that have been added or changed significantly during the year.

9. Summary

This study analyzes the key audit items in the audit reports of 34 listed companies, which shows that the reform of audit reports has achieved initial results. The reform of audit report has laid a solid foundation for the full implementation of the new standards and opened a new chapter for the development of the audit industry. Communicating key audit matters and other reform measures in audit reports has improved the information content and communication value of audit reports and reawakened users' interest in audit reports, further set up the public awareness of the audit value. Of course, there are still many challenges in the application of the standards, which require Certified Public Accountant to better understand and grasp the standards, use professional judgment in practice, and communicate key audit matters properly. These initiatives will provide users with more relevant and useful information for decision-making.

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