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Stowarzyszenie Księgowych w Polsce

Key Audit Matters reporting for Polish listed companies

Kluczowe sprawy badania raportowane dla polskich spółek giełdowych

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Abstract

Purpose: The main purpose of the article is to identify and characterize the key audit matters (KAMs) indicated during an audit of the financial statements of the largest companies in the Polish market.

Methodology/approach: We analyzed the KAMs presented in the verification of the consolidated financial statements of the 30 largest companies listed on the main market of the Warsaw Stock Exchange for 2014–2022. The total sample was 270 auditors' reports. The basis of the methodology was empirical research; deductive and inductive reasoning were used to formulate the results.

Findings: The number of KAMs reported in individual years did not fluctuate significantly, and the average number disclosed for one audit coincides with general global trends. The auditors reported the riskiest areas were for entities from the insurance sector, media and telecommunications, and the fuel industry. The most important KAMs include contingent liabilities, revenue, long-term assets, and goodwill.

Research limitations/implications: The main constraint is the limited research sample relating only to the audit of the financial statements of WIG30 companies. However, it covers the largest entities for which auditors indicated the most KAMs and prepared their most extensive descriptions.

Originality/value: The article concerns a relatively new research area for which there are few studies on the Polish market, which additionally have a narrow substantive scope. This paper comprehensively characterizes KAMs reported by auditors in the long term.

Keywords: key audit matters, auditing, auditors' report, ISA 701, financial statement, risk.

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Streszczenie

Cel: Głównym celem artykułu jest identyfikacja oraz pogłębiona charakterystyka kluczowych kwestii badania (KAMs) wskazywanych przy audycie sprawozdań finansowych największych spółek na polskim rynku.
Metodyka/podejście badawcze: Analizie poddano kluczowe kwestie badania zaprezentowane przez audytorów w badaniu skonsolidowanych sprawozdań finansowych 30. największych spółek notowanych na rynku podstawowym warszawskiej GPW za lata 2014–2022. Łączna próba wyniosła 270 sprawozdań biegłych rewidentów. Podstawę metodyki stanowiło głównie badanie empiryczne, zaś do sformułowania wyników wykorzystano wnioskowanie dedukcyjne i indukcyjne.
Wyniki: Liczba KAM's raportowana w poszczególnych latach nie ulegała znacznym wahaniom, a ich średnia liczba ujawniana dla jednego audytu pokrywa się z ogólnymi trendami światowymi. Najwięcej obszarów ryzyka audytorzy zgłaszali dla podmiotów sektora ubezpieczeniowego, mediów i telekomunikacji oraz branży paliwowej. Do najważniejszych kluczowych spraw badania należy zaliczyć zobowiązania warunkowe, przychody, długoterminowe aktywa i wartość firmy.
Ograniczenia/implikacje badawcze: Głównym ograniczeniem jest zawężona próba badawcza odnosząca się wyłącznie do badania sprawozdań finansowych spółek WIG30. Obejmuje ona jednak największe podmioty, dla których audytorzy wskazywali najwięcej KAMs oraz przygotowali ich najszersze opisy.
Oryginalność/wartość: Artykuł dotyczy stosunkowo nowego obszaru badawczego, który, w kontekście polskiego rynku, nie był dotychczas przedmiotem wielu badań, a istniejące opracowania mają wąski zakres merytoryczny. Niniejsza praca prezentuje kompleksową charakterystykę kluczowych spraw badania raportowanych przez audytorów w dłuższej perspektywie czasu.

Słowa kluczowe: kluczowe sprawy badania, audyt, sprawozdanie biegłego rewidenta, KSB 701, sprawozdanie finansowe, ryzyko.

Introduction

The process of implementing systematic changes in auditors' reporting has been ongoing for several years. Practice has shown that the scope and content of the opinions issued by statutory auditors are no longer fit for purpose. The information needs of readers of financial statements have changed, as they want to learn about the broader context of auditors' work to analyze the conclusions included in their reports more effectively. Thus, the auditor was obliged to present key audit matters (KAMs) along with the verification procedures applied. KAMs refer to the issues that, in the auditor's opinion, were of the greatest importance when auditing the financial statements for a given reporting period and that indicate risk areas.

This area has already become the subject of academic interest, although it is relatively new. Most papers concern the relationship between KAMs and various aspects of the way businesses and auditors function. They include analyses of the scope of KAM disclosures and auditor liability (Gimbar et al., 2016; Backof et al., 2022; Brasel et al., 2016; Brown et al., 2020) and how KAMs influence investor decisions (Christensen et al., 2014; Backof, 2015; Köhler et al., 2016; Hoang et al., 2023; Lennox et al., 2023). Subsequent studies show how the obligation to disclose KAMs impacts the quality of financial data published (Bentley et al., 2021; Gold et al., 2020; Reid et al., 2019). A separate trend refers to the substantive analysis of KAMs and verification procedures disclosed in the auditors' reports. The most extensive analyses were performed on the British and Australian markets, mainly because these countries were among the first to implement the new reporting standards.

In Poland, this obligation was introduced with financial statements prepared from December 31, 2018, although audit firms were allowed to adopt these practices earlier. Therefore, the new reporting rules have been in operation for several years, and thus, a deeper analysis has become possible, although the scope of research on the Polish market is limited. Some authors characterized the KAMs reported by statutory auditors for listed companies, mainly for 2017/2018, i.e., immediately after the introduction of this obligation (B. Iwanowicz, 2019; T. Iwanowicz, 2019; Warzocha, Bujak, 2020). Other studies contain broader analyses of KAMs but only for selected economic sectors (Karmańska, 2020; Natkaniec, 2020). Therefore, there is no comprehensive study that presents a broader description of KAMs reported by auditors in the long term. This paper fills this research gap. It is one of the first studies to present detailed information on KAMs included in the reports of auditors examining the largest enterprises in the Polish capital market. The research results make it possible to clearly identify the main risk areas in financial statements, the key industries with the highest level of this risk, and the auditors who present the most KAMs in their reports. The analysis covers a longer time horizon and presents the scale of both optional and mandatory reporting of KAMs. There has been no such research conducted on the Polish market.

The article aims to identify and characterize in-depth the KAMs indicated during the audit of the financial statements of the largest Polish listed companies. A preliminary analysis of the auditors' reports indicated that the general scope of KAM disclosures for these companies is comparable to other countries, and it is also possible to determine certain trends in this reporting. Due to the above, the following research questions were formulated:

– Did Polish auditors take advantage of the option to voluntarily report KAMs before the obligation to present them for the audit of financial statements for 2018 came into force, taking into account global trends? If so, what was the scale of these disclosures?
– Is it possible to distinguish specific KAMs for individual sectors of the economy?
– How many KAMs were reported by individual auditors and for selected industries?
– What were the KAMs identified by Polish auditors? And to what extent did they coincide with the results of international research in this area?

The KAMs presented by auditors when auditing the consolidated financial statements of the 30 largest Polish listed companies between 2014 and 2022 were analyzed in detail. The total research sample included 270 auditors' reports, of which 171 contained broader descriptions of KAMs.

The research methods include critical, comparative, and descriptive analysis. The basis of the methodology is empirical research and an analysis of the subject literature and legal acts. Deductive and inductive reasoning were used to formulate the results based on the method of analysis and synthesis.

The article is structured as follows. First, the legislative and theoretical foundations related to the new auditor reports are presented, including the results of preliminary international research in this area. The next section includes general conclusions from the analysis of reports presented by statutory auditors for the selected research sample, followed by detailed results regarding the disclosed KAMs. The final section contains a summary.

1. The legal and theoretical basis for KAM reporting in auditors' reports

Work on reforming the audit services market in recent years has resulted in a broad amendment of the International Standards on Auditing (ISAs) regarding the principles of preparing reports on the audit of financial statements. The main purpose of these changes was to increase the scope of information disclosed by statutory auditors relating to the nature of the audited business, certain risk areas and the verification procedures used. It has been widely commented that audit reports contain very general statements and are highly formalized, making them not very valuable to readers of financial statements (Church et al., 2008; Mock et al., 2013; Bédard et al., 2016). The vast majority of auditors issued unqualified opinions, which were identical in each case, even for very diverse entities. Statutory auditors were not obliged to present any additional content related to significant issues analyzed during their work. Thus, this reporting model was not only clearly of little use to either professional (Coram et al., 2011; Gray et al., 2011) or ordinary investors (Turner et al., 2010), but it also gave rise to information asymmetry. Many researchers have pointed out that as the market has developed, the "expectations gap" is significantly increasing, i.e., the discrepancy between the perception of the role of auditors by the auditor community itself and social expectations regarding the essence of the work they perform (Ruhnke, Schmidt, 2014; Coram, Wang, 2020; Vanstraelen et al., 2012; Mock et al., 2013).

Concerns about the limited usefulness of auditors' reports frequently arose in discussions on the systematic development of the financial reporting system for enterprises. Mock et al. (2013) indicated that capital market participants need more information about the audited financial statements, as well as the auditor himself and the procedures he applied. Research further identified the specific type of additional information that should be included in auditors' reports:

- Descriptions that explain the scope of the work performed by the auditor and the specific terms relating to the methodology for verifying financial data. This would facilitate market participants' understanding of the purpose and the significant limitations of auditing financial statements (Church et al., 2008; Gray et al., 2011; Turner et al., 2010).

– Data on the audit team involved and the specialists used, which would make it possible to assess the professionalism of the work performed (Knechel et al., 2007; Carey, Simnett, 2006).
– A presentation of the audit process along with the characteristics of the main verification procedures performed. Readers of financial statements could then appreciate the scope of the work performed and better understand the auditor's findings, conclusions, and the final result (Church et al., 2008; Knechel et al., 2007).
– Additional disclosures not necessarily related to the core scope of the audit, for example, the non-financial information that companies present (De Villiers et al., 2014; Simnett, Huggins, 2015; Turner et al., 2010).

Widespread criticism of the current model of reporting audit results led to major legislative changes, initially at the global level and later also at the regional and local levels. In January 2015, the International Auditing and Assurance Standards Board (IAASB) published the first significant changes to the standards, which became effective for audits of financial statements ending on December 15, 2016, or later. In total, five standards were revised: ISA 700 *Forming an Opinion and Reporting on Financial Statements*, ISA 705 *Modifications to the Opinion in the Independent Auditor's Report*, ISA 706 *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*, ISA 570 *Going Concern*, ISA 260 *Communication with Those Charged with Governance*. In addition, one new standard was introduced, ISA 701 *Communicating Key Audit Matters in the Independent Auditor's Report*, which is the most important in the context of the issues discussed. Some countries (i.e., Great Britain, the Netherlands and Australia) did not wait for the ISA reform; they had already implemented auditors' reporting of risk areas in audited financial statements. Great Britain was the first country in the world to introduce this obligation – for audits of annual financial statements ending on September 30, 2013, or later.

Similar actions have been taken at EU level. New guidelines for expert reporting are presented in Directive No. 2014/56/EU of the European Parliament and of the Council of 16/04/2014 (Article 28) and Regulation of the European Parliament and of the Council No. 537/2014 of 16/04/2014 (Article 10). Pursuant to these acts, new reporting rules became applicable to audits of financial statements beginning on or after June 17, 2016, i.e., they effectively applied to annual reports ending on June 30, 2017, at the earliest.

Polish legislation introduced new rules for auditor reporting, although with a slight delay. The main legal basis was Resolution No. 2041/37a/2018 of the National Council of Statutory Auditors of March 5, 2018, on national standards for practicing the profession, which presented templates of auditors' reports. In turn, an update to the reporting rules encompassing the disclosure of KAMs was included in Resolution No. 2039/37a/2018 of the National Council of Statutory Auditors of February 19, 2018, on national auditing standards (700 (Z), 701, 705 (Z), 706 (Z), 720 (Z), 260 (Z), 570 (Z)). Pursuant to this resolution, the mandatory presentation of risk areas by auditors was implemented for the first time for audits of financial statements ending on December 31, 2018. However, audit companies had the option to introduce new optional rules earlier, for financial statements prepared as of December 31, 2017. Many auditors, mainly associated with the Big 4, opted for this approach.

Subsequent changes to KSB 701 *Presentation of key audit matters in the independent auditor's report* under Polish legislation were closely related to changes introduced in other professional standards. The most important concern the amendment to KSB 315 (Z) introduced by resolution No. 2272/38a/2022 of the National Council of Statutory Auditors of July 7, 2022, and the amendment to KSB 540 (Z) introduced by resolution No. 1107/15a/2020 of the National Council of Statutory Auditors of 8 September 2020.

In accordance with these regulations, a new obligation was imposed on statutory auditors in the context of auditing financial statements of public interest entities - presentation of KAMs in the report. KAMs are those matters that, in the auditor's professional judgment, were most significant when verifying the work performed and required the auditor's particular attention. When deciding which aspects should be presented in the report, the auditor should primarily consider the identified areas of high risk of material misstatement, which he estimated at the audit planning stage. In each case, the auditor must indicate and justify their choice of KAMs, and provide a response, i.e., the verification procedures used in response to the identified risks. Previously, no such obligation existed. Thus, its introduction significantly improves the quality and usefulness of information presented in auditors' reports and allows investors to draw broader conclusions about the financial data that companies publish.

2. Directions of current research in the field of KAM reporting

Changing the method of reporting and disclosing KAMs has become an area of analysis not only for practitioners but also researchers. Many papers have investigated the relationship between KAMs and various aspects of the way businesses and auditors function, for example, the relationship between the scope of KAM disclosures and auditor liability. While experiments conducted by Gimbar et al. (2016) and Backof et al. (2022) show that presenting KAMs increases the auditor's exposure to risk, other studies found the opposite (Brasel et al., 2016; Brown et al., 2020). Meanwhile, Kachelmeier et al. (2020) indicated that KAM disclosures may partially protect auditors from liability. Participants in the experiments mentioned above significantly reduced the scope of auditor responsibility for extensive disclosures of KAMs in their reports. Vinson et al. (2019) additionally verified the long-term effects of disclosing selected risk areas in auditors' reports. They demonstrated that removing KAM reported for many years compared to adding a new KAM reported for one year has a stronger impact on the recipients of this information.

Much research examines how KAM disclosures impact investor decisions and overall market reactions. Christensen et al. (2014) and Backof (2015) argued that

KAMs do not have much influence on the decisions made by small investors who are not professionals in their field. Carver and Trinkle (2017) found similar results. Nevertheless, Köhler et al. (2016) found that they are important for professionals. Additionally, negative aspects of KAMs have a much stronger impact than positive KAMs (Hoang et al., 2023). Meanwhile, Sirois et al. (2018) demonstrated that additional information presented by auditors focuses the attention of report readers on these areas at the expense of other issues. Other studies have shown that risk areas are disclosed by auditors too late, and this information is already known to the readers of the report (Lennox et al., 2023).

The obligation to disclose KAMs often increases the auditor's vigilance when performing verification, which then affects decisions made by the management of the audited companies. For example, Bentley et al. (2021) found that managers are more likely to speculate and are less likely to hedge when they anticipate a KAM disclosure. However, this effect is mitigated when the KAM report contains a disclaimer related to the scope of the auditor's assurance role. Gold et al. (2020) examined whether the disclosure of risk areas in auditors' reports influenced the level of aggressive financial reporting used by the management boards of audited companies. They found that the obligation to disclose KAMs significantly reduced the willingness of management to use mechanisms of fraudulent reporting.

Reid et al. (2019) obtained similar results when examining the impact of new reporting requirements on the quality of financial statements published in the UK. They found that the reliability of financial data increased while maintaining the current prices for the audit service. There were also no significant delays in the preparation of reports by statutory auditors. However, Gutierrez et al. (2018), who also analyzed the British market, obtained slightly different results. They did not identify a strong link between the introduction of the obligation for auditors to disclose risk areas and an increase in the quality of financial statements. They did confirm, however, that there was no increase in the cost of auditing financial statements.

A separate strand of research is the substantive analysis of KAMs presented by auditors, although it is more often performed by institutions related to the audit services market. The Association of Chartered Certified Accountants ACCA (2018) assessed the content of KAMs in 560 auditors' reports issued in 10 different countries where the new rules were implemented. The most important risk areas reported by statutory auditors include asset impairments (other than goodwill), revenue (not mentioning fraud), allowance for doubtful debt, goodwill impairment, and taxation, including deferred tax. The analysis indicated that the problem of impairment losses on assets occurred in almost 30% of the reports. Overall, the number of KAMs per audit ranged from 1.9 in Nigeria to 4.1 in the UK, with most within a range of two to three KAMs per audit.

Similar conclusions can be drawn from the Financial Reporting Council's (FRC) analysis of the British market, where the new form of auditor reporting was implemented first (FRC, 2021). The study covered 396 reports of enterprises listed on the main market of the London Stock Exchange. It found that auditors most often described issues related to revenue recognition, which is presumed to be a fraud risk by the auditing standards. Other common KAMs were related to financial statements, where estimation uncertainty and management judgment created heightened risks for manipulative financial reporting – investments, asset impairments, financial instruments, and goodwill. Most reports included three KAMs, but there was significant variation between reports. While several reports included many KAMs, the number of reports with only one KAM (12%) was greater than the number with six or more (10%). However, over time, the number of reported risk areas per company generally decreases.

Extensive research has also been conducted on the Australian market, where the obligation to present risk areas in auditors' reports was also introduced quite early. The study by Chartered Accountants Australia and New Zealand covered 1,400 units (CA ANZ, 2022). The distribution of the number of KAMs is tightly clustered around the mean; 39% of audit reports had one KAM, and 36% had two. There are also a few reports in which the auditor did not indicate any risk areas (3%) or where there were more than 4 (6%). Auditors most often reported problems related to the impairment of assets, exploration assets, revenue, business combinations, share-based payments, inventory, intangibles, and provisions.

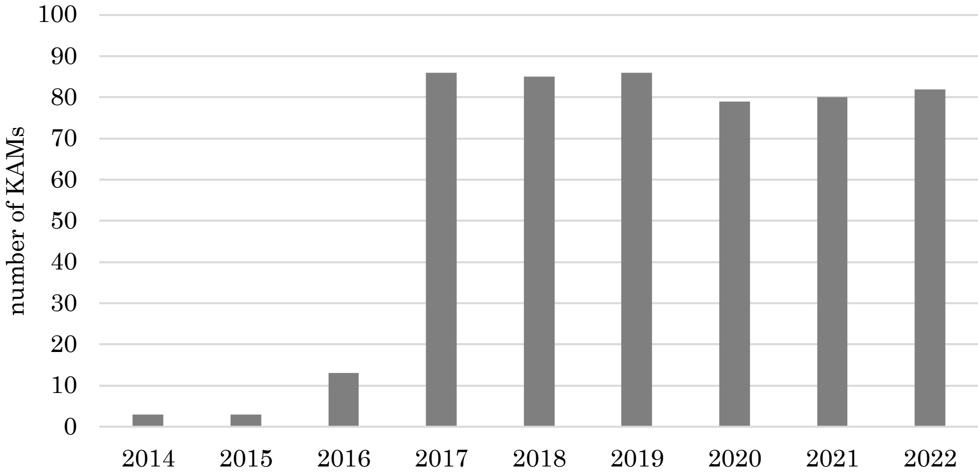
In the Polish audit market, a more thorough analysis of KAMs is already underway. The first research showed that the first descriptions of risk areas appeared in the audit reports as far back as 2014, i.e., several years before the introduction of the obligation (Kutera, 2019). This allowed for the characterization of initial risks related to Polish financial reporting. Subsequent analyses focused on later years, verifying statutory auditors reports of financial statements for listed companies for 2017–2018, i.e., immediately after the introduction of the obligation to disclose KAMs (B. Iwanowicz, 2019; T. Iwanowicz, 2019; Warzocha, Bujak, 2020). Other studies also outlined the main risk areas in the financial statements of Polish companies, but more in the context of selected industries, e.g., construction (Karmańska, 2020; Natkaniec, 2020).

3. General trends in KAM reporting when auditing the financial statements of the largest Polish companies

We conducted an analysis to assess the extent to which statutory auditors comply with new reporting regulations and the main trends in KAM reporting. The examination focused on documents issued by auditors for the consolidated reports of the 30 largest Polish listed companies between 2014 and 2022. The total sample comprised 270 auditors' reports, of which 171 reports contained descriptions of KAMs. The smaller number of reports containing KAM's indications results from the fact that for audits of financial statements for the period 2014-2017, their presentation was voluntary, and only selected auditors opted to disclose them. The research sample accounts for changes in the companies included in the WIG30 index, with the list being updated for each year of the analysis.

Chart 1 provides detailed data on the number of KAMs disclosed for individual financial years. It can be concluded that some auditors optionally implemented the description of risk areas several years before the formal introduction of this obligation.

Chart 1. Number of KAMs included in auditors' reports



Source: own study based on auditors' reports for WIG30 companies, 2014–2022.

Polish regulations mandated KAM reporting starting from the financial statements prepared as of December 31, 2018, although the first disclosures appeared as early as 2014. KPMG was a pioneer, introducing additional descriptions in its reports for two clients in that year (Kutera, 2019), and again in 2015. During the 2016 audits, four companies were identified, for which statutory auditors reported a total of 13 KAMs. A breakthrough occurred in 2017, when auditors took advantage of the opportunity to earlier implement the provisions of ISA 701 *Communicating Key Audit Matters in the Independent Auditor's Report* in accordance with the regulations issued by the Polish Chamber of Statutory Auditors. Risk areas were presented for almost all WIG30 companies, which is because, at the time, virtually all of the largest listed companies were audited by the Big 4, which had introduced the new reporting rules within their networks. Statutory auditors presented a total of 86 risk areas in their reports. Chart 1 shows that this number did not fluctuate significantly in subsequent years, with auditors indicating between 79 and 85 KAMs for all WIG30 companies.

Interesting conclusions can also be drawn by analyzing the number of KAMs reported by individual audit companies. Between 2014 and 2022, statutory auditors issued 171 reports with descriptions of risk areas, collectively presenting a total of 523 KAMs (see Table 1 for detailed information). Most KAMs were included in the EY reports – a total of 226 issues were reported as a result of the audit of 62 financial statements. EY performed by far the most audits in the analyzed period. PwC reported far fewer KAMs (121), although they also audited almost 30% fewer financial statements. In third place is KPMG, which reported 91 KAMs in the 32 auditors' reports it issued. The remaining companies no longer play a significant role. The WIG30 in the analyzed period was not supported exclusively by the Big 4. In recent years, smaller network audit companies have also obtained audit orders from this group of companies, such as Grant Thornton, BDO, Mazars, and PKF Consult.

Table 1. KAMs by auditor

	Number of KAMs	**Number of auditors' reports**	**Average number of KAMs in the report**
KPMG	91	32	3
PwC	121	44	3
EY	226	62	4
Deloitte	53	19	3
Grant Thornton	20	7	3
BDO	7	4	2
Mazars	4	2	2
PKF Consult	1	1	1
TOTAL	**523**	**171**	

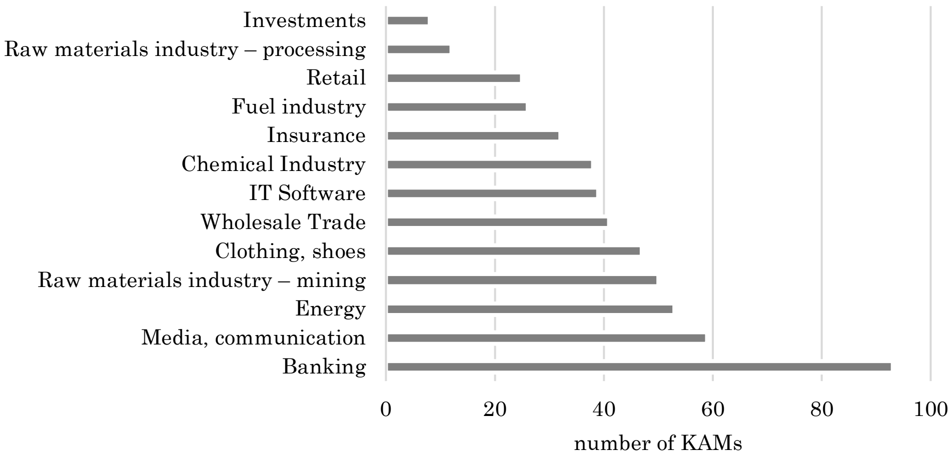
Source: own study based on auditors' reports for WIG30 companies, 2014–2022.

Table 1 also shows the average number of KAMs reported in a single audit, with most reports containing about three risk areas. However, smaller auditing companies offer a slightly narrower scope, especially PKF Consult, a newcomer to the market.

4. KAMs reported for selected economic sectors

The number of KAMs varies significantly in the context of verifying companies that belong to specific industries. This is clearly visible in Chart 2. Selected economic sectors are more exposed to various risks, which are also considered when auditing annual financial statements. Moreover, some entities on the WIG30 are companies that conduct banking or insurance activities, which have specific financial reporting. At the same time, they play a greater role from the point of view of the security of economic transactions. In such a case, professional skepticism and the associated cautious approach to the audit are particularly important. It should also translate into reliable information for readers about potential risk areas.

Chart 2. KAMs divided into main industries



Source: own study based on auditors' reports for WIG30 companies for the period 2014–2022.

Analysis of the data in Chart 2 shows that most of the KAMs are reported for the banking sector. During the analyzed period, auditors presented 93 risk areas for these entities. The next sectors are media and communications, energy, natural resource extraction activities, and light industry, although the number of key issues investigated here is much lower (45–60). However, as the number of companies that belong to the WIG30 varies by industry, the average conversion of KAMs reported per entity from a given sector is important. In this way, it is possible to identify industries that are assessed as the riskiest from the point of view of auditing their financial statements. Table 2 presents information for the ten most important sectors.

Table 2. The average number of KAMs per company in a given industry

Item	Number of KAMs	Number of companies	Average number of KAMs per company
Insurance	32	1	32
Media and communication	59	2	30
Fuel industry	26	1	26
Clothing, shoes	47	2	24
Wholesale Trade	41	2	21
IT Software	39	2	20
Chemical Industry	38	2	19
Energy	53	3	18
Raw materials industry – mining	50	3	17
Banking	93	6	16

Source: own study based on auditors' reports for WIG30 companies for the period 2014–2022.

The data clearly show that the insurance sector had the most risk areas reported. While there was only one insurance company among the companies studied, as many as 32 KAMs were reported for it during the analyzed period. They mainly concern reporting items specific to insurance, i.e., estimating technical provisions, but also contingent liabilities, goodwill, and control over related entities. The next group on the list comprises media and telecommunications companies, with an average of 30 KAMs per company. Auditors paid particular attention to the recognition of sales revenues that result mainly from small fees paid by customers, deferred income tax calculations, write-offs for long-term assets (including goodwill), implementing new leasing rules in accordance with IFRS 16, and procedures related to the first-year audit. The WIG30 also includes one entity belonging to the fuel sector, for which auditors presented a total of 26 risk areas. The most important problems include contingent liabilities arising from court disputes and claims, impairments of property, plant, equipment and tangible assets, derivatives and hedging, mandatory inventory limits, accounting settlement of the takeover of control over individual entities, and the first-time application of IFRS 16 "Leases".

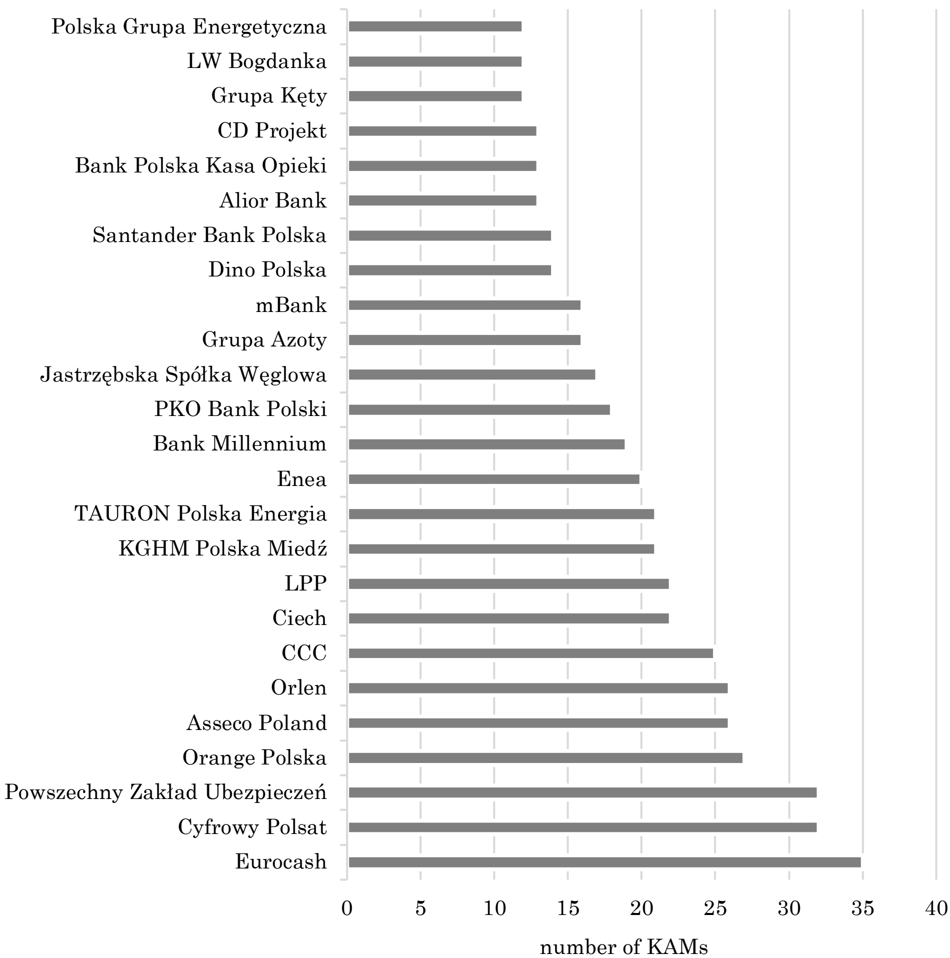
Subsequent industries have two or three companies, and the average number of KAMs described ranges from 16 to 24 areas. Each of them usually has some specific KAMs that are characteristic of companies in a given industry. Examples include the valuation of inventories for manufacturing and trading enterprises, the estimation of the value of research and development work in the IT sector, and provisions for the costs of mining activity, e.g., mining damage and other environmental risks.

With six companies, the banking sector has the most entities listed on the WIG30. Chart 2 shows that auditors presented the most risk areas for this industry in total. However, if we consider the average number of KAMs per bank, their financial statements are not burdened with the highest risk. Auditors mainly focus on allowances for credit losses, revenue recognition of interest income and fee and commission income, the impact of adopting IFRS 9, and contingent liabilities.

Another element of the analysis is an in-depth verification of the risk areas in the audit of the financial statements of individual WIG30 companies. Chart 3 presents the number of KAMs divided into specific entities; only those entities for which auditors identified more than ten risk-related issues are presented. The Eurocash group, which deals in wholesale trade, had the most KAMs – 35 for six audited financial statements. Each year, auditors looked at five or six important issues, which is a significant number compared to other companies because, on average, the reports contain about 3 KAMs. For Eurocash, the most important factors were the valuation related to goodwill and other intangible property rights, impairment losses on inventories and long-term assets, revenue recognition, unusual tax settlements, the presentation of leases, and, recently, issues related to going concern.

Other entities with a relatively high number of reported risk areas include Cyfrowy Polsat, Powszechny Zakład Ubezpieczeń, Orange Polska, Asseco Poland, Orlen, and CCC. In almost all of those companies, auditors indicated a higher-than-average number of KAMs. For Cyfrowy Polsat, the verification of the settlement of the acquisition of individual companies, contingent liabilities, goodwill write-offs, recoverability of deferred tax assets, revenue recognition, and changes in accounting policy to recognize leasing contracts were of particular importance. When auditing PZU's statements, the following were key: valuation of provisions for outstanding claims and benefits for third-party motor liability insurance, valuation of life insurance provision, impairment of loans to customers in banking activity, revenues recognition, impairment of goodwill, policy changes, and conduct risk, including disputes and customer complaints in banking activity.

Chart 3. WIG30 companies with the most KAMs



Source: own study based on auditors' reports for WIG30 companies for the period 2014–2022.

The KAMs identified during the first verifications of the financial statements were usually repeated in subsequent financial years, often even after a change in auditor. Therefore, the question arises as to what extent the new statutory auditors made their own reliable identification of risk areas and to what extent the previous auditor's results guided them. Nevertheless, certain risks must be considered significant in every audit. Additionally, selected items of the financial statements are important in each financial year because they result from the specific nature of the business activity. There, a certain repeatability of KAMs in individual financial years is also justified.

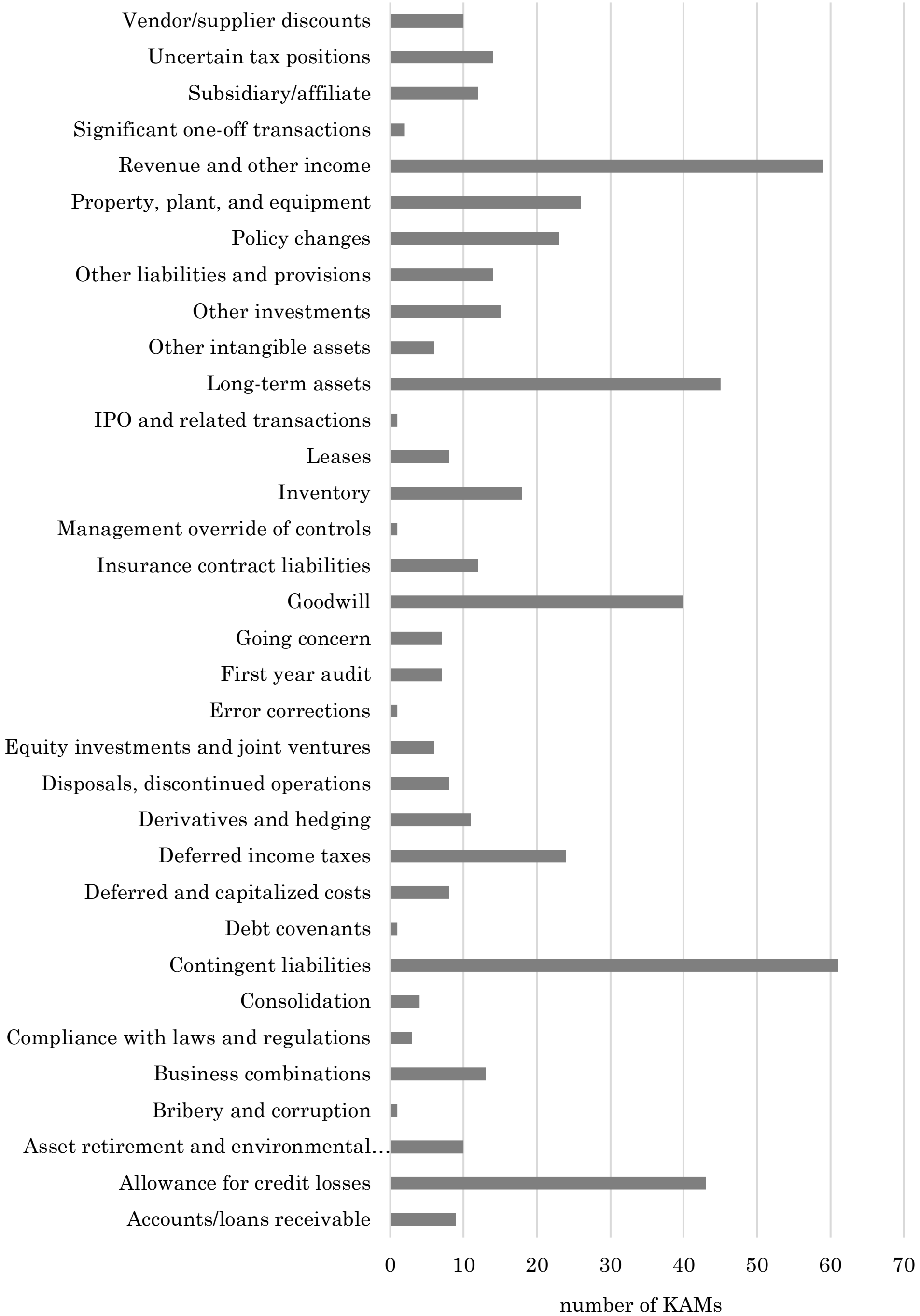
5. Main types of key audit matters included in auditors' reports

An important element of the analysis of KAMs is identifying the risk areas most frequently indicated by auditors in enterprise financial reporting. This classification highlights the most difficult elements in auditing financial statements and draws attention to specific reporting items. It also underscores the need for careful interpretation of the results that companies present. Legal regulations mandate that auditors include in their reports a description of the most significant types of risk of material misstatement and a response from an expert in this area. The auditor should clearly indicate what verification techniques were used for each KAM and what the results were.

Chart 4 summarizes the most important areas disclosed as KAMs in the entire research sample. It shows that the largest risk areas include contingent liabilities, revenue and other income, long-term assets, goodwill, and allowance for credit losses. Property, plant, and equipment, policy changes, deferred income taxes, and inventory are much less important, although they were also relatively often mentioned by statutory auditors.

Contingent liabilities appeared in 61 auditors' reports, with almost half being for the banking sector. Statutory auditors mainly looked at conduct risk, including litigation and customer complaints. They focused on the essence and number of provisions for legal claims and contingent liabilities relating to mortgage loans indexed to the Swiss Franc (CHF) calculated by banks. This risk was indicated for virtually all six banks included in the WIG30. In the financial sector, the sole insurer also faces the risk of litigation and proceedings before supervisory authorities. For other industries, current court disputes with clients were the main focus. However, there were also a few indications of situations specific to selected entities, such as TAURON Polska Energia S.A., where the auditors looked at legislative and regulatory changes regarding electricity sales prices in 2019 and in subsequent years. For Orlen S.A., they focused on compensation related to an accident on an installation for ethylene production in its subsidiary UNIPETROL RPA s.r.o. For LPP S.A., they looked at uncertainties connected with the tax implications of selected transactions, while for Jastrzębska Spółka Węglowa S.A., the focus was on provisions for potential litigation related to the free coal allowance for old-age and disability pensioners.

Chart 4. Types of KAMs included in auditors' reports



Source: own study based on auditors' reports for WIG30 companies for the period 2014–2022.

Due to the high risk of intentional manipulation, revenue was unsurprisingly the top KAM, with 59 instances. Pursuant to the provisions of ISA 240, auditors must treat revenue as a high-risk area for overstatement of revenue due to premature recognition or recording of fictitious transactions. Only in exceptional circumstances can the statutory auditor deviate from this assumption, for example, when there is one type of simple income transaction (e.g., rent for renting a premises). Consequently, revenue should nearly always be recognized as a KAM and described in more detail.

In the companies from the banking sector, the auditors paid particular attention to revenue recognition of interest income and fee and commission income. PwC also provided its clients with estimates resulting from the introduction of the act enabling customers to use credit moratoria. Risks related to special bonuses and discounts for customers were also presented for selected entities (i.e., Orange Polska S.A., Eurocash S.A., Asseco Poland S.A., KGHM Polska Miedź S.A.). For CD Project S.A., particular attention was paid to the risk of assigning revenues from game sales to the incorrect reporting period, for Allegro.eu S.A., they looked at marketplace revenue recognition and accounting for Smart! Program, and for Orlen S.A., they focused on the correctness of revenue recognition from petrochemical products and electricity sales.

The KAMs reported for long-term assets concern very different industries, although they focus mainly on impairment losses for individual assets. An analysis of auditors' reports shows that some discussed impairment for every material item in the financial statements while others treated them collectively, indicating one KAM related to impairment tests for all long-term assets (i.e., fixed assets, intangible assets, and financial instruments such as shares, loans granted). In all 45 KAMs that concerned long-term assets, the auditors indicated the accuracy of impairment loss estimates or the need to create them as a risk area.

Goodwill was indicated in 40 auditors' reports. This is also not surprising because the analysis covered consolidated financial statements, which in most cases automatically present this reporting item and is often of high value. According to international standards, goodwill is not subject to amortization; however, an annual impairment test must be performed. Therefore, the methodology for conducting these tests and their results is a particularly sensitive and important element in auditing financial statements. The accuracy of impairment tests was consistently indicated as a risk area across all KAMs related to goodwill.

Allowance for credit losses is a KAM identified for virtually all banks. It was presented in 43 auditors' reports, and the vast majority concerned expected credit losses on loans and advances to customers, along with provisions for off-balance sheet commitments.

The research results clearly show that when verifying the financial statements of the largest listed Polish companies, auditors focus on five main KAMs in their reports: contingent liabilities, revenue and other income, long-term assets, goodwill, and allowance for credit losses. Other risk areas do not occur so often and are much less important.

Conclusions

The analysis clearly indicates that the stakeholders currently obtains more information not only about the audited entity but, above all, about the auditors' work. This allows for a broader understanding of the essence of the audit and the identification of potential risk areas in published financial statements. The research confirms that the largest audit companies had already prepared for the changes and optionally implemented new provisions in their reports. The number of KAMs reported in individual years since 2017 has not fluctuated significantly. EY indicated the most risk areas in its reports, mainly because it conducts the most audits for WIG30 companies. The average number of KAMs disclosed by auditors for a single audit coincides with general global trends. Auditors reported the most risk areas for companies in the insurance sector, in media and telecommunications, and in the fuel industry.

Analysis of the content of auditors' reports indicates that the most important KAMs include contingent liabilities, revenue and other income, long-term assets, goodwill, and allowance for credit losses. Property, plant and equipment, policy changes, deferred income taxes, and inventory are slightly less important. These results largely overlap with similar analyses conducted for other countries.

The analysis is not without its limitations. For example, the limited research sample relates only to the audit of the financial statements of WIG30 companies. However, it includes the largest entities for which auditors indicated the most KAMs and provided the most extensive descriptions. This ensures reliable research material while also making it possible to clearly define directions for further research. Future studies will undoubtedly involve an in-depth analysis of the scope and type of KAMs disclosed and the verification procedures used, broken down into various research criteria regarding the audited entities and the auditors themselves.

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