



16 September 2011

Mr James Gunn  
Technical Director  
International Auditing and Assurance Standards Board  
International Federation of Accountants  
545 Fifth Avenue, 14th Floor  
New York, New York 10017 USA

Dear James,

**AUASB Submission on Consultation Paper**  
***Enhancing the Value of Auditor Reporting: Exploring Options for Change***

The Australian Auditing and Assurance Standards Board (AUASB) is pleased to have the opportunity to comment on the IAASB Consultation Paper *Enhancing the Value of Auditor Reporting: Exploring Options for Change*.

The AUASB commends the IAASB's initiative to consider a fundamental review of auditor reporting at this time of ever-increasing complexity in global financial systems. Exploring options that may help achieve reporting that better meets users' information needs is clearly in the interests of both users and providers of audit services.

In formulating its response, the AUASB sought input from its constituents in several ways: The first was an open invitation to comment placed on the AUASB website with an accompanying notification sent to subscribers. The second method was by way of hosting a number of "roundtable" discussions with stakeholders from a broad range of backgrounds including audit firms, assurance providers, regulators, professional accounting bodies, board audit committees and executives and institutional investors. In addition, the AUASB also undertook several focussed discussions with users of audit reports.

Our responses to the specific questions raised in the Consultation Paper are presented so as to articulate the views of our stakeholders where appropriate. We feel that this is consistent with the objectives of the exercise as described in the preface to the Consultation Paper.

In summary, the AUASB considers the following points of particular importance for the IAASB's consideration:

1. Under the auspices of the IAASB, National Standards Setters should co-operate to establish a proposal for representation to users, providers and regulators to influence change in financial reporting frameworks. Where user information needs are not being met, changes to the reporting framework are considered a more appropriate approach than changes to Auditing Standards and in particular, the auditor's report. The AUASB considers a global and co-ordinated response to be the most effective approach to introduce change.

2. Improvements in auditor reporting should not detract from the fundamental objective of the auditor's report on the financial statements. The current auditor's report is designed for the expression of an opinion on whether or not the financial statements fairly present the financial position, financial performance and the cash flows of the entity in accordance with the applicable financial reporting framework.

There may be some value in re-positioning the audit opinion within the auditor's report to the first paragraph of the report, as this may be useful to the user to prioritise this information. However further value from re-positioning information, or moving it outside the report is not seen as particularly helpful of itself.

3. When increasing or changing auditor reporting of a general purpose nature, care should be taken to ensure consistency in application. Differing levels of detail and/or style may lead to user confusion and/or misinterpretation that more detailed reporting by one auditor equates to a higher quality of audit assurance compared to less or different reporting by another auditor.
4. There were different perspectives obtained from the users of the financial report as distinct from the preparers of the report through the AUASB consultation process. Users of the financial statement and auditors report would generally value any additional reporting or assurance that the auditor is able to give within the context of the appropriate reporting framework.

On the other hand, some preparers take a different view, as it was reiterated that the communication that occurs between the audit committee of an entity and the auditor is highly valued. However, the notion of restructuring the audit report was perceived as 'tinkering' and is unlikely to bridge any perceived or real "information gaps". Auditors tend to concur with this view, in so far as if report users value the information, there is an appropriate reporting framework in place and the subject matter is capable of assurance, then in principle there is willingness to consider such developments.

5. The AUASB also notes that once entities move to an integrated reporting model, the need for assurance over additional information reported by the entity is likely to become more prevalent. These changes of course will bring with them, their own challenges and benefits, and the need for new assurance standards.

The AUASB's responses to the specific questions raised in the Consultation Paper are outlined in **Attachment 1** to this letter for the IAASB's consideration.

Should you have any queries regarding this submission, please do not hesitate to contact either Marina Michaelides at [mmichaelides@auasb.gov.au](mailto:mmichaelides@auasb.gov.au) or myself at [rmifsud@auasb.gov.au](mailto:rmifsud@auasb.gov.au).

Yours sincerely,

Richard Mifsud  
*Executive Director*

Attachments



## Responses to Specific Questions listed in the Consultation Paper

### Questions

1. Do respondents have any comments about the issues identified in Section II regarding the perceptions of auditor reporting today?
2. If respondents believe changes in auditor reporting are needed, what are the most critical issues to be addressed to narrow the information gap perceived by users or to improve the communicative value of auditor reporting? Which classes of users are, in the view of respondents, most affected by these issues? Are there any classes of users that respondents believe are unaffected by these issues?
3. Do respondents believe that changes are needed for audits of all types of entities, or only for audits of listed entities?

### AUASB Response:

- 1.1 Improved auditor reporting designed to assist users to assess the financial condition and performance of an entity and its corporate reporting is of value and supported by stakeholders. There is a general understanding that this must be done within the context of the appropriate reporting and assurance framework. As entities move to an integrated reporting model (International Integrated Reporting Committee's intention to release an Exposure Draft on an International Integrated Reporting Framework in 2012), the need for assurance over additional information reported by the entity may become more prevalent. These changes of course will bring with them, their own challenges and benefits, and the need for related assurance standard(s).
- 1.2 Paragraph 12(b) refers to users wanting, *inter alia*, to assess “the quality of the audit”. The AUASB has some doubts about whether this notion can be achieved by way of improved auditor reporting. Auditing is a professional activity, defined by the requirement to exercise professional judgement in the application of principles-based auditing standards in the circumstances of the engagement. The quality of an audit cannot be properly assessed without knowledge of all relevant facts – something that is unlikely to be provided by increasing auditor reporting as canvassed by the Consultation Paper. Formally assessing the quality of an audit should remain a matter for those charged with governance/audit committees, regulators and professional accounting bodies. However, the AUASB recognises that views on audit quality are made in the market place, regardless of the level of user knowledge. Accordingly, the better the information provided, the more likely that a reasonable assessment will be made. (On reflection we cannot be this definitive here – clearly institutional investors/analysts etc even retail shareholders have views here.)
- 1.3 The AUASB is not averse to changes to the structure and wording of an auditor's report, however, any such changes should not detract from the fundamental objective of the auditor's report – that is, to express an opinion on fair presentation of the financial position, financial performance and the cash flows of the entity in accordance with the applicable financial reporting framework.



- 1.4 The AUASB is supportive of co-operation with organisations whose mandates extend to regulatory and legislative frameworks. The AUASB is of the view that changes to reporting frameworks are the most appropriate method of bridging the “information gap” about an entity.
- 1.5 Paragraph 13 onwards, deals with the “expectation gap”. The historical “expectation gap” is often less apparent in capital markets until such time as it is tested by the legal and regulatory system once a ‘crisis’ or ‘collapse’ occurs. Care should be taken as to whose ‘expectation gap’ the auditor is endeavouring to close as different users will have varying knowledge/understanding and expectations of the auditor and their role.

It is the view of the AUASB that widely accessible and comprehensive educational material may be one solution and that limited information provided in the auditor’s report will not alone have the desired effect of closing this gap. A reference in the auditor’s report to such educational material might possibly seem a useful approach, conceptually along the lines adopted in the UK.

- 1.6 Paragraph 18 onwards, deals with the “information gap”. The AUASB supports improvements and more transparency of information about the entity and its financial statements. There continue to be differing views, from investors and analysts who would like as much information and insights about an entity from its auditors, as compared to members of audit committees and auditors, as to what information should be disclosed and by whom. An additional question is the level of assurance to be provided on any additional information, coupled with significant concerns over legal liability.

The points listed in paragraph 23 as suggested areas of additional information the auditor could report on, are seen as problematic by the profession. If an auditor were to provide information such as key business, operational and audit risks, key assumptions underlying material judgements affecting the financial report, changes to accounting policies that have a significant impact and significant unusual transactions, the auditor would effectively take responsibility for significantly influencing users’ investment and fiduciary decisions.

For example if the auditor believes accounting policies adopted are not appropriate and the effect is material, a qualified opinion is required. If, on the other hand, the effect is not material and the auditor reports that the accounting policies are permitted under the framework but are inappropriate or inconsistent with industry practice, the auditor has merely informed users that there is an acceptable difference of opinion:

- Is this valuable information or is it confusing?
- Has this information influenced users to lose trust in management and its judgement or in the auditor’s judgement?
- Does the user require further detailed explanation to dispel or confirm which party is right or wrong?
- How does a user use this information to achieve valuable outcomes?

Accordingly, the AUASB concurs with the view expressed in paragraph 24, that it is inappropriate for the auditor to originate information about the entity and any such approach would undermine the role of management/board. The directors of the board must take responsibility for their legal and fiduciary duty. This view was supported by a number of stakeholders with whom the AUASB consulted.

- 1.7 The AUASB supports the view expressed in paragraph 28 that it is important, as a matter of principle, to retain consistency in auditor reporting for the reasons given.



- 2.1 If changes in auditor reporting are needed, the most critical issues are:
- Improvements or changes in auditor reporting should be driven by changes in the financial reporting framework.
  - Improvements in information about the audit process should be provided by means other than increasing the content of the auditor's report on the financial statements. The objective of the auditor's report on the financial statements should remain that of expressing an opinion on compliance with a financial reporting framework.
  - Additional reporting by the auditor should comprise only information that the entity has already provided. The auditor should not originate information. The division of responsibilities should be maintained.
  - Additional auditor reporting requirements should be capable of consistent application.
- 2.2 The class of investors most affected by the issues raised are likely to be shareholders, other than large institutional investors. Most other users are likely to be able to obtain the information about the entity that they require.
- 3.1 Any changes to auditor reporting should be applied to audits of all types of entities to the extent that such reporting does not contravene laws or regulations.

### Questions

4. Respondents are asked for their reactions to the options for change regarding the format and structure of the standard auditors report described in Part A. Do respondents have comments about how the options might be reflected in the standard auditor's report in the way outlined in Appendix 1 of this Consultation Paper?
5. If the paragraphs in the current standard auditor's report dealing with management and the auditor's responsibilities were removed or re-positioned, might that have the unintended consequence of widening the expectations gap? Do respondents have a view regarding whether the content of these paragraphs should be expanded?

### AUASB Response:

- 4.1 The AUASB is supportive of further research on relocating certain information to another document, which may contain additional information, along the lines of the UK model as described in paragraph 41. Such relocation however should not result in the auditor's report becoming devoid of appropriate context. Users must be provided with a clear context within which the opinion is issued, albeit that context is in the form of reduced wording in the auditor's report and additional information in another location.

In Australia, auditing standards are legislative instruments and it is not possible to include material that is outside the legislative financial reporting and auditing framework.

Re-positioning within the auditor's report, with the exception possibly of moving the opinion to the first paragraph of the report, appears to serve little purpose or provide any discernable benefits in itself.

- 4.2 Moving the opinion paragraph in the auditor's report to the first paragraph of the report might assist in the users accessing what they perceive as the 'valuable' information as a priority. However, the specific location in the auditor's report of the opinion paragraph does not of itself appear to be important in bridging expectations or information gaps.



- 4.3 The AUASB does not argue against retaining the paragraphs in the auditor's report for the reasons described in paragraphs 44. However, should research indicate relocation has clear benefits, the AUASB would likely support such relocation (see paragraph 4.1 above).
  - 4.4 The AUASB supports the development of educational material about the meaning of an audit and the role of the independent auditor that can be readily available to users as described in paragraph 45.
  - 4.5 The AUASB supports more fully explaining the meaning of technical terms in a Glossary provided with or linked to the audit report, however, not in the auditor's report. The AUASB agrees with the sentiments expressed in paragraph 48 and supports relocation of such material in conjunction with more extensive explanation of the responsibilities of management and the auditors.
- 5.1 The AUASB does not support the removal or re-location of contextual material from the auditor's report without retaining in the auditor's report at least minimal contextual text.

For example, the contextual paragraphs in the auditor's report could be reduced to a simple:

*Management is responsible for the preparation of the financial report – further information is found at...*

*As auditors our responsibilities are for expressing an opinion on the financial statements – further information is found at...*
  - 5.2 The AUASB is supportive of expanded information about the responsibilities of management as well as, those charged with governance, and auditors. However, it was felt that this should not occur in the auditor's report, which would become unwieldy.

## Questions

6. Respondents are asked for their reactions to the possibility that the standard auditor's report could include a statement about the auditor's responsibilities regarding other information in documents containing audited financial statements. Do respondents believe that such a change would be of benefit to users?
7. If yes, what form should that statement take? Is it sufficient for the auditor to describe the auditor's responsibilities for other information in documents containing audited financial statements? Should there be an explicit statement as to whether the auditor has anything to report with respect to the other information?

## AUASB Response:

- 6.1 The AUASB supports a statement about the auditor's responsibilities regarding other information. Again, such information is better placed alongside expanded contextual information and educational material that has been relocated (see responses to questions 4 and 5 above).
- 6.2 Expanded information about the auditor's responsibilities as required by ISA 720 would be of benefit to users. However, any material inconsistencies or misstatement of fact should continue to be reported in the auditor's report under an Other Matter(s) paragraph.
- 7.1 The AUASB is of the view that it is sufficient to describe the auditor's responsibilities regarding other information.



The AUASB is not supportive of an explicit statement as to whether the auditor has anything to report in respect of the other information. Any such statement would imply that a level of assurance is given over that information – this would be misleading and confusing as the auditor is not required to perform either an audit or review of that other information.

## Questions

8. Respondents are asked for their views regarding the auditor providing additional information about the audit in the auditor's report on the financial statements.
9. Respondents are asked for their reactions to the example of use of "justification of assessments" in France, as a way to provide additional auditor commentary.
10. Respondents are asked for their reactions to the prospect of the auditor providing insights about the entity or the quality of its financial reporting in the auditor's report.

## AUASB Response:

- 8.1 The AUASB is supportive of the IAASB's current approach to the use of an Emphasis of Matter paragraph and an Other Matter paragraph as described in paragraphs 57 to 59 of the Consultation Paper.
- 8.2 Auditors are not largely in favour of providing increased information about the audit as described in paragraph 62, primarily for the cautions expressed in paragraphs 63 and 64.
- 9.1 The AUASB notes the results of the French survey described at paragraph 67 of the Consultation Paper, which indicated that the value ascribed to the additional disclosures by the auditor varied considerably. Australian auditors consulted by the AUASB, were generally not in favour of the French model of "Justification of Assessments". In particular, concern was expressed regarding the disclosure of information by auditors that has not been disclosed by the entity itself.
- 10.1 Whilst auditors are generally not in favour of providing insights about the entity or the quality of financial reporting, for all the reasons given in paragraphs 73 and 74 of the Consultation Paper, some users of audit reports see merit in the reporting of additional information by the auditor (such as that provided under the French model), as it may assist their understanding of areas such as materiality and matters involving management estimation in the financial statements. However, users do appreciate that there are constraints for the auditor in reporting on such additional matters, as well as the associated risk of auditor liability, if this information is not first reported by the entity itself.

## Questions

11. Respondents are asked for their reactions to the options for change relating to an enhanced model of corporate governance reporting, as described in Section III, Part D.
12. To the extent that respondents support this model, what challenges may be faced in promoting its acceptance? Also, what actions may be necessary to influence acceptance or adoption of this model, for example, by those responsible for regulating the financial reporting process?
13. Do respondents believe assurance by the auditor on a report issued by those charged with governance would be appropriate?



## AUASB Response:

11.1 The AUASB is supportive of the principles of an enhanced model of corporate governance as described in Section III, Part D. The model would provide information to the shareholders, stakeholders or analysts that is currently not available and would therefore be of value to some users. The model appears to overcome the issue of the auditor not disclosing information that the entity has not disclosed itself.

12.1 The issues raised in paragraph 86 would need to be addressed.

12.2 It would be necessary to clearly articulate the objectives of such increased reporting. Those charged with governance would need to be convinced of the benefits of what might be perceived as an additional administrative burden.

Where it can be demonstrated that additional reporting about corporate governance is valuable to the organisation by improving shareholder and stakeholder confidence, those charged with governance are more likely to be motivated to consider this exercise. Further research in those countries mentioned in the Consultation Paper would provide valuable input to the question of motivation.

12.3 It should be noted that with the rise of social media networks, corporate control and procurement of entity information will continue to decline and the role of the Board and auditor will need to adapt accordingly.

12.4 As presumably the content of audit committees' reports will vary, those responsible for regulating the financial reporting process will need to establish whether contents are to be prescribed or whether those charged with governance will be free to decide on content. This point would likely become an issue in terms of monitoring compliance.

13.1 The AUASB believes that a statement by the auditor that accompanies an audit committee report would be of value to users. However, "assurance" is not necessarily appropriate and there were mixed views on the probity value of this approach, both within and outside the profession.

13.2 The auditor's report would need to be clear as to the meaning of the "completeness and reasonableness" assertions, so that users understand the level of assurance to be provided by the auditor.

13.3 It would be very important to establish a framework within which the auditor would "report on the completeness and reasonableness" of the audit committee's report.

The auditor should only be able to report on a subject matter where the auditor has access to the relevant information. If the audit committee's report move away from communications with the auditor, it will be necessary for the auditor to have access to relevant supporting information. Any such "drift" in the audit committee's report would likely pose problems for the auditor's "completeness" assertion.

## Questions

14. Respondents are asked for their reactions to the need for, or potential value of, assurance or related services on the type of information discussed in Section III, Part E.
15. What actions are necessary to influence further development of such assurance or related services?



### AUASB Response:

- 14.1 Starting from the premise that independent attestation is generally perceived as valuable in providing credibility to the particular subject matter, the AUASB supports the concept of assurance or related services on the type of information discussed in Section III, Part E.
- 14.2 Any such assurance should not be intermingled with the current model providing an audit opinion on whether the financial statements comply with the applicable financial reporting framework.
- 14.3 The AUASB welcomes the IAASB's further deliberations on this topic and the concurrent review of standards on assurance of non-financial information. It also notes that once entities move to an integrated reporting model, the need for assurance or related services over additional information reported by the entity is likely to become more prevalent. These changes of course will bring with them, their own challenges and benefits.
- 15.1 Under the auspices of the IAASB, National Standards Setters should co-operate to establish a united plan for representation to users, providers and regulators to influence change in financial reporting frameworks. From section III, Part D of the Consultation Paper, it is clear that certain countries have already taken the initiative. The AUASB considers a global and co-ordinated response to be the most effective approach to introduce change.

### Questions

16. Respondents are requested to identify benefits, costs and other implications of change, or potential challenges they believe are associated with the different options explored in Section III.
17. Do respondents believe the benefits, costs, potential challenges and other implications of change, are the same for all types of entity? If not, please explain how they may differ.
18. Which, if any, of the options explored in Section III, either individually or in combination, do respondents believe would be most effective in enhancing auditor reporting, keeping in mind benefits, costs, potential challenges, and other implications in each case? In this regard, do respondents believe there are opportunities for collaboration with others that the IAASB should explore, particularly with respect to the options described in Section III, Parts D and E, which envisage changes outside the scope of the existing auditor reporting model and scope of the financial statement audit?
19. Are there other suggestions for change to auditor reporting to narrow the “information gap” perceived by users or to improve the communicative value of the auditor’s report?

### AUASB Response:

- 16.1 Potential for scope-creep with additional reporting responsibilities (assurance) may impact the financial report audit process and audit fees/cost. This may also be accompanied by the need for broader audit/commercial skills from the assurance practitioners to understand and report on key risks and sustainability of business models in the future.
- 16.2 Further research is required to establish user needs. Different user groups have differing information needs depending on the use to which the information is put, their level of financial sophistication and their knowledge of financial reporting and interpreting financial information. There is a risk of imposing an economic burden (i.e. increased reporting requirements) for the benefit of only some users may be in the minority.



- 16.4 Care has to be taken with increased reporting on individual aspects of the auditor's assurance work which may have little or no relationship to reporting on the financial report as a whole or on any prospective matters.
- 17.1 It is the AUASB's view that the benefits, costs, potential challenges and other implications are likely to be similar, albeit proportional, for all types of entities. This view is based on an assumption that any enhanced reporting requirements are mandated for all entities.
- 18.1 The AUASB is supportive of the following options:
  - IAASB-led initiatives to influence and co-operate with those parties responsible for setting financial reporting frameworks. The AUASB sees this as fundamental to addressing the question of user information needs not being met. Traditionally, audit mandates are set by reporting frameworks against which, auditors assess compliance by the responsible party. The AUASB supports continuation of this basic approach.
  - The development of educational material about the meaning of an audit, the role of the independent auditor and the meaning of technical terms that can be readily available to users.
  - Additional information about the responsibilities of management and auditors and such additional information not be included in the auditor's report but located elsewhere.
  - A statement about the auditor's responsibilities regarding other information.
  - Developing principles of an enhanced model of corporate governance.
  - The concepts of assurance or related services on the types of information discussed in Section III, Part E.
- 19.1 No further suggestions.

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