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James Gunn
Technical Director
International Auditing and Assurance Standards Board
529 Fifth Avenue, 6th Floor
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Via electronic submission

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Dear Mr Gunn

INVITATION TO COMMENT: IMPROVING THE AUDITOR'S REPORT

CPA Australia welcomes the opportunity to comment on the Invitation to Comment: Improving the Auditor's Report (the ITC). CPA Australia is one of the world's largest accounting bodies and represents the diverse interests of more than 139,000 members in finance, accounting and business in 114 countries throughout the world. Our vision is for CPA Australia to be the global professional accountancy designation for strategic business leaders. We make this submission on behalf of our members and in the broader public interest.

CPA Australia supports the International Auditing and Assurance Standards Board's (IAASB) objective of positive change in auditor reporting, and agrees with the reasons specified in the ITC. A response to demands for change from the users of financial statements, and the lessons learned from recent financial crises is desirable to enhance the continued value and relevance of audit.

Valuable change requires a holistic approach incorporating all aspects of the financial reporting and audit supply chain. A one-dimensional approach to modify the auditor report alone is unlikely to achieve the aims of addressing identified user demands. To enable a genuinely enhanced form of auditor reporting, developments in reporting frameworks, and necessary revisions to the framework for audit and assurance engagement must be taken into account.

In many jurisdictions the audit report is a legally required document that conveys the auditor's conclusions to intended users using precise language. Whilst the approach to convey the auditor's findings using simple language appears an attractive proposition, changes to auditor reporting need to be considered in the context of auditors' regulatory and legal accountabilities.

The responsibility to navigate these important changes comes with a significant risk. If the groundwork required to enable enhanced auditor reporting is not sufficiently laid out, there is a risk that the result will be increased complexity and possible weakening in the value stakeholders glean from the simplicity of the current auditor's report format.

CPA Australia's responses to the specific questions raised in the ITC are attached. If you require further information on any of our views, please contact Amir Ghandar, CPA Australia by email at amir.ghandar@cpaaustralia.com.au.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Alex Malley', written in a cursive style.

Alex Malley FCPA
Chief Executive Officer

cc: A Ghandar

Appendix 1: Responses to the questions in the ITC

1. Overall, do you believe the IAASB's suggested improvements sufficiently enhance the relevance and informational value of the auditor's report, in view of possible impediments (including costs)? Why or why not?

The ITC outlines several objectives against which the overall sufficiency of the proposals must be considered including response to:

- 'demand for auditors to provide greater transparency about significant matters in the financial statements, as well as the conduct of the individual audit';
- demand for 'auditors to help assist in navigating increasingly complex financial statements';
- a general 'call for change' in various parts of the world.

CPA Australia also notes the IAASB's guiding principles for this project outlined in section 9 of the ITC.

CPA Australia believes that the suggested improvements provide a useful starting point to consider change in the auditor's report, but are not in their current form likely to meet the objective of enhancing relevance and information value. There is a risk that the relevance and informational value of auditor reporting could be weakened if these proposals are implemented without further development to address the impediments.

CPA Australia makes the following general observations on the objectives, guiding principles and proposals as drafted:

- There are significant hurdles to operationalization of the current proposals (refer also responses to specific questions below);
- The information relevant to specific users of financial statements varies depending on their individual objectives and situation. Auditors are not in a position to determine what information is most relevant to user's understanding of the financial statements;
- The principle of 'greater transparency' appears to have translated to 'more information' in the current proposals. More information without a clear reason and context will exacerbate, rather than resolve the problems raised in the ITC, particularly the issues of complexity in financial reporting, and the expectation gap;
- A number of initiatives are currently under way to improve financial reporting that meets identified user needs. Improvements to audit and auditor reporting should be considered in the context of such initiatives and how these will impact on auditor reporting.
- Genuinely enhanced reporting cannot be achieved without revisiting the current scope of ISA audits. The objective of an ISA audit and the supporting pronouncements do not currently include disclosing new information about the entity being audited or a role to aid 'navigation' of financial statements.

CPA Australia proposes a number of recommendations to address these observations under question 2.

2. Are there other alternatives to improve the auditor's report, or auditor reporting more broadly, that should be further considered by the IAASB, either alone or in coordination with others? Please explain your answer.

CPA Australia recommends the following alternatives to improve auditor reporting and address the problems and objectives raised in the ITC:

- Consider the option of an enhanced corporate governance model, as detailed in the IAASB's consultation paper, 'Enhancing the Value of Auditor Reporting: Exploring Options for Change' (May 2011) including:
 - Reporting by those charged with governance (or the audit committee) to the entity's shareholders (or other external stakeholders) on matters pertinent to their deliberations; in conjunction with
 - Expanded reporting by the independent auditor on the report provided by those charged with governance.

This model would address many of the hurdles to operationalization in the current proposals (see question 1 above), while still enhancing the information available for users significantly.

- Revisit the current scope of ISA audits and potential supplementary engagements in light of the evolving needs of stakeholders.
 - Consider whether there is demand for an enhanced type of engagement for public interest entities separate to the financial statement audit, and what framework and pronouncement is required to enable such engagements. User calls for more information on the auditor's views about entities indicate a possible demand for engagements similar to performance audits in the private sector.
- Revisit the *Framework for Auditing and Assurance Engagements* to:
 - Consider revising the definitions of limited and reasonable assurance, and whether there are other types of assurance relevant to the needs that currently exist in capital markets;
 - Consider whether there are other changes required to the Framework more broadly to enable meaningful assurance to be provided on evolving types of reporting (for example sustainability reporting and integrated reporting).
- Actively provide assurance-centric input to the development of enhanced reporting frameworks such as integrated reporting
 - The audit profession has a crucial perspective to bring to the development of reporting frameworks – valuable information for decision making must be capable of being credibly assured
 - Assurance-centric input up-front is critical to the development of useful reporting frameworks.
 - Developments in audit and financial reporting share common objectives – meeting user needs. Working together is important to reach complete solutions.

3. Do you believe the concept of Auditor Commentary is an appropriate response to the call for auditors to provide more information to users through the auditor's report? Why or why not?

CPA Australia does not believe the current proposals on auditor commentary in the ITC are a sufficient or appropriate response to the call for auditors to provide better information to users through the auditor's report.

CPA Australia notes several significant impediments to the operationalization of the proposed model:

- The information relevant to specific users of financial statements varies depending on their individual objectives and situation. Auditors are not in a position to determine what information is most relevant to user's understanding of the financial statements. Attempting to address the complexity of financial statements by adding further detail into the auditor's report could exacerbate the problem, and confuse users whose information needs differ from what the auditor has anticipated. The fundamentals of the current audit framework do not provide for the auditor to assess and understand user needs; such needs are largely addressed by the financial reporting framework.
- More specific information about the audit work performed requires technical detail that could be inaccessible to groups of users, or if over-simplified, fail to convey its full meaning and context.
- The core role of auditors is currently to provide assurance to users on the financial statements – a role that comes with significant legal and regulatory accountabilities. Developing and agreeing on wording to be included in the auditor commentary with those affected, and in the context of the auditor's accountabilities could involve substantial time and cost.
- These factors combined may lead to auditor commentary becoming standardised and 'boiler-plate'. This would mean more complexity, without adding value.

CPA Australia proposed a number of recommendations under question 2 above to address these observations.

Questions 4. to 7.

Refer question 3 response above.

8. What are your views on the value and impediments of the suggested auditor statements related to going concern, which address the appropriateness of management's use of the going concern assumption and whether material uncertainties have been identified? Do you believe these statements provide useful information and are appropriate? Why or why not?

CPA Australia believes that further explanation of the relevant terminology, clarity and simple language on the auditor's responsibilities with respect to going concern could be useful for users. Separately detailing this information outside the general description of auditor responsibilities in the form of a 'conclusion' on management's use of the going concern assumption could confuse users and be misinterpreted as an opinion on the solvency of the entity, or its ability to continue as a going concern. While a caveat is included in the illustrative report, it is unlikely this would fully address the risk of misinterpretation and consequent widening of the expectations gap.

As noted in the ITC, ISA 570 already requires the auditor to direct users to information disclosed on material uncertainties where they exist, in an emphasis of matter paragraph, and if the auditor does not agree with management's use of the going concern assumption, this would result in an adverse opinion.

CPA Australia recommends that the information on auditor's responsibilities with regard to going concern is included in the general description of auditor responsibilities. A genuinely valuable conclusion in regard to going concern would require revisiting the scope of the audit.

9. What are your views on the value and impediments of including additional information in the auditor's report about the auditor's judgments and processes to support the auditor's statement that no material uncertainties have been identified?

Refer question 8 response above.

10. What are your views on the value and impediments of the suggested auditor statement in relation to other information?

CPA Australia supports the inclusion of a statement in relation to other information presented with the financial report that would clarify the auditor's responsibilities.

11. Do you believe the enhanced descriptions of the responsibilities of management, TCWG, and the auditor in the illustrative auditor's report are helpful to users' understanding of the nature and scope of an audit? Why or why not? Do you have suggestions for other improvements to the description of the auditor's responsibilities?

In our view, the descriptions included in the illustrative report have not achieved 'plain English' quality, and include a considerable amount of audit terminology that may not be accessible to a large number of users. There is a risk that including such descriptions could exacerbate the issues of the expectation gap, and inaccessibility of auditor reporting.

CPA Australia believes that it is appropriate to include a basic description of the nature and scope of an audit, and relevant responsibilities to support the primary function of the auditor's report: providing an opinion on the financial statements.

CPA Australia recognises the critical need of improving the understanding of auditors' responsibilities, and addressing expectation gaps that exist in user's perceptions of financial reporting more broadly. Meeting this need requires more extensive explanation than would be appropriate in the auditor's report. As outlined under the response to question 14 below, CPA Australia supports allowing references to standardized material such as those describing the auditor's responsibilities outside the auditor's report.

12. What are your views on the value and impediments of disclosing the name of the engagement partner?

Engagement partners have been required to sign in their own name in Australian auditor reports since reforms introduced in 2004. Significant impediments have not been noted as a result of this requirement. CPA Australia recognises the value of disclosing engagement partners' names as detailed in the ITC.

13. What are your views on the value and impediments of the suggested disclosure regarding the involvement of other auditors? Do you believe that such a disclosure should be included in all relevant circumstances, or left to the auditor's judgment as part of Auditor Commentary?

CPA Australia believes that a clarification of the group auditor's ultimate responsibility for the audit could be helpful to users' understanding.

As noted in the ITC, the currently proposed disclosure could run counter to the concept of group auditors clearly adopting sole responsibility for the audit.

14. What are your views on explicitly allowing the standardized material describing the auditor's responsibilities to be relocated to a website of the appropriate authority, or to an appendix to the auditor's report?

CPA Australia supports this proposal. Refer also question 11 response above.

15. What are your views on whether the IAASB's suggested structure of the illustrative report, including placement of the auditor's opinion and the Auditor Commentary section towards the beginning of the report, gives appropriate emphasis to matters of most importance to users?

CPA Australia supports locating the auditor's opinion at the beginning of the report. Refer to question 3 response above in regard to auditor commentary.

16. What are your views regarding the need for global consistency in auditors' reports when ISAs, or national auditing standards that incorporate or are otherwise based on ISAs, are used?

CPA Australia believes global consistency in auditor's reports to the greatest extent possible is desirable. Auditor's reports are required by users making decisions in an increasingly globalised business environment – achieving consistency in the information provided should be a critical objective for the audit profession. CPA Australia recognises that certain jurisdictions may require content in auditor's reports that differs from the international standard, but suggest that this should only occur where there is a compelling reason.

17. What are your views as to whether the IAASB should mandate the ordering of items in a manner similar to that shown in the illustrative report, unless law or regulation require otherwise? Would this provide sufficient flexibility to accommodate national reporting requirements or practices?

CPA Australia supports the proposed approach.

18. In your view, are the IAASB's suggested improvements appropriate for entities of all sizes and in both the public and private sectors? What considerations specific to audits of small- and medium-sized entities (SMEs) and public sector entities should the IAASB further take into account in approaching its standard-setting proposals?

CPA Australia's views on the proposals as outlined above are relevant also from the perspective of SMEs and the public sector. CPA Australia notes below considerations specific to audits of SMEs and public sector entities.

SMEs

The ITC states that auditor commentary may replace the need for the concepts of emphasis of matter and other matter paragraphs. The ITC also proposes that auditor commentary should be optional for entities that are not public interest entities, which would likely include most SMEs. If the concept of emphasis of matter and other matter paragraphs is retired with the introduction of auditor commentary, it is not clear how the auditors of such SMEs would report these items.

Public Sector

Public Sector auditors often have reporting responsibilities that include and go further than what is envisaged in the ITC. For example, it is common for public sector auditors to report to their parliament in a detailed, discursive manner on the financial reporting of agencies, and undertake performance audits which provide insights beyond the scope of current ISA audits. In some cases, this could mean the proposals outlined in the ITC, particularly those in regard to auditor commentary, are not relevant or desirable from the perspective of the users of public sector auditor reporting.