Question 1(a)-2 - What do you think is the main cause of the expectation gap relating to going concern in an audit of financial statements.

1. In regard to the expectation gap (see Section I):

a) ***What do you think is the main cause of the expectation gap relating to fraud and going concern in an audit of financial statements?***

b) In your view, what could be done, by the IAASB and / or others (please specify), to narrow the expectation gap related to fraud and going concern in an audit of financial statements?

Q1a-2.1 - Combination of one or more components (evolution gap, knowledge gap, or performance gap)

1. Monitoring Group

Basel Committee on Banking Supervision (BCBS)

The Committee understands that there may be gaps between what the users expect from the auditor and the financial statement audit. As noted in the discussion paper, this could include a misunderstanding of the role of auditors (knowledge gap), unclear or inconsistently applied requirements (performance gap) or the need for enhancements to add more value (evolution gap).

International Organization of Securities Commissions (IOSCO)

We appreciate the discussion on the audit expectation gap included in the Paper on page 11, "which described three components of the expectation gap: the "knowledge gap", the "performance gap", and the "evolution gap".

In our view, there is an overlap between the knowledge and evolution gaps, in terms of financial statement users' expectation of auditors. This relates to not only what auditors' current responsibilities are today based upon the existing standards, but what the users expect they should be. We believe the IAASB should consider as part of its information gathering activities what, if any, expectations that users have of auditors beyond the core responsibilities to provide reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error, when it pertains to undetected fraud.

The last component of the expectation gap outlined in the Paper is the performance gap, where we believe a critical activity for the IAASB during the information gathering phase is to analyze the root causes of recent events, in order to determine the cause(s) of the performance gap.

2. Regulators and Audit Oversight Authorities

Committee of European Auditing Oversight Bodies (CEAOB)

We would like to emphasize the fact that difficulty in detecting material misstatements in the financial statements resulting from fraud (rather than error) does not reduce the auditor's responsibility. Similarly, difficulty in assessing the management's use of the going concern assumption and whether a material uncertainty exists related to future events or conditions that may cause an entity to cease to continue as a going concern does not reduce the auditor's responsibility.

In certain cases involving fraud, even where the fraud was very significant or where the auditor's report did not highlight concerns regarding the situation of an entity which collapsed shortly after its issuance, the "expectation gap" has been put forward by auditors to explain that no material misstatements or uncertainties were identified during the audit. However, in instances where auditors have not complied with the requirements of the ISAs, including ISA 240 (on fraud) and ISA 570 (on going concern), putting forward the "expectation gap" alone is not an appropriate explanation to justify the failure.

Financial Reporting Council (FRC)

In relation to both fraud and going concern, we agree with the description of the three components of the expectation gap that are described on page 11 of the Discussion Paper. We also broadly agree with the examples of aspects that could be better addressed by standard setting, including supporting materials, and aspects that require further consideration. The extent to which these different components and the related aspects exist will vary across and within jurisdictions. For example, in any one jurisdiction there may be stakeholders who have a very good understanding of what auditors do and others who do not. Similarly, different stakeholders may have different views as to how they would wish audit to evolve, and the level of assurance they want that audit to provide. While audit inspections and investigations into corporate failures and major frauds have revealed audit performance failures and inconsistency of application, there is no evidence of general performance failures in all audits.

In light of this, we would not suggest that, from a global perspective, there is one particular "main cause" of an expectation gap.

Independent Regulatory Board for Auditors (IRBA)

The consolidated view of the stakeholders consulted (see the cover letter) is that each component – the "knowledge gap", the "performance gap" and the "evolution gap" – contributes to the audit expectation gap in a significant manner.

The "evolution gap" is a common concern shared by regulators and those charged with governance. Concerns raised include whether the audit product and, consequently, the standards that support the audit product are evolving at the same pace as business; and whether they can keep up with the evolving business models, information systems and accounting standards that are more judgement and estimation based today than they were a few years ago.

Irish Auditing and Accounting Supervisory Authority (IAASA).pdf

We would like to emphasize the fact that difficulty in detecting material misstatements in the financial statements resulting from fraud (rather than error) does not reduce the auditor's responsibility. Similarly, difficulty in assessing management's use of the going concern assumption and whether a material uncertainty exists related to future events or conditions that may cause an entity to cease to continue as a going concern does not reduce the auditor's responsibility.

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National Association of State Boards of Accountancy (NASBA)

(a) NASBA believes the expectation gap relating to fraud and going concern in a financial statement audit may be caused by a few factors: lack of understanding by the public as to what an audit is and what auditors do; inconsistent audit execution in these areas by some auditors due to lack of understanding and, in some cases, competence; and the inherent limitations of a financial statement audit.

3. National Audit Standard Setters

Australian Auditing and Assurance Standards Board (AUASB)

Knowledge gap

We consider the expectation gap to contain a knowledge gap due to users not fully understanding management, TCWG and auditor's differing responsibilities for maintaining the entity as a going concern, a once a year going concern assessment and reporting thereof, and for ensuring there are fulsome and timely disclosures of key judgements and risks. Users also may not understand what a going concern assessment is, and the auditor's responsibility to conclude on the appropriateness of management's use of the going concern basis of accounting does not provide a guarantee that the entity will continue to exist until the next audit report is issued. Going concern assessments are forward looking which involves judgement about inherently uncertain future outcomes of events or conditions. Users' expectations may not be realistic, however the AUASB consider that more could be done to explain the current responsibilities and provide definitional transparency.

The IAASB is encouraged to further engage with users to understand if further reporting on responsibilities would be beneficial. If the IAASB considers that further reporting on relevant responsibilities may be beneficial, we expect the reporting by the auditor to be aligned with proportionate reporting by management / TCWG. It is difficult to communicate complex matters such as going concern and audit concepts succinctly so the IAASB is encouraged to carefully evaluate whether any increased reporting will inadvertently increase the expectation gap. Some of our stakeholders also expressed a view that further reporting on going concern matters for all audits when there is no going concern issue, may not be beneficial as users won't see this reporting as an "alert".

The current reporting requirements for going concern issues in the auditor's report is complex and users may not understand and interpret the difference between a MURGC and a KAM, or their importance to their decision making. By way of example, the information required to be communicated in the audit report if going concern is a KAM is greater than if a MURGC. We have feedback from academic studies that the greater the volume of words in the audit report can be interpreted as the issue having greater importance, however in the case of MURGCs versus KAM this is not proportionate to the relative severity of the issue. The auditing standards note a MURGC is by its nature a KAM. With the background above, in our view this connection confuses the purpose of each, clouds the distinction needed for readers of severity and importance to their decision making, and the resultant volume of communication in the auditor's report should reasonably expected therefore to be consistent, which it is not. The AUASB remains supportive of retaining the separate distinction of MURGC paragraphs as this gives this appropriate prominence in the auditor's report. However, the IAASB should consider if the required reporting of a MURGC should be disconnected from KAMs as a concept and contemplate more balanced qualitative information to be communicated regarding the key factors and the procedures in the audit report. The IAASB can use this feedback to also reflect on the volume of words and communicative expectations for modification to the audit report, in comparison to KAMs as well.

Performance gap

The AUASB considers that there is a performance gap, not only for auditors, but also for preparers of financial statements which needs to be addressed through greater education and enhanced Accounting Standard requirements. Whilst acknowledging that auditors could do more to improve how going concern related audit issues are addressed, the AUASB received feedback that the main issue driving the performance gap is the inconsistency in how management / TCWG fulfil their responsibilities when making going concern assessments, and ensuring fulsome disclosure of significant judgements and assumptions to keep users informed on matters relevant to going concern. The Accounting Standards need to be enhanced using a multi-layered approach, covering definitional issues, measurement expectations for a going concern assessment, and more explicit disclosure requirements of key matters relevant to the going concern assessment and whether a MURGC exists.

The Accounting and Auditing Standards should be better aligned. Management / TCWG also need more detailed requirements and / or guidance on how to make going concern assessments including how to identify whether there is a material uncertainty, how to determine if an entity is not a going concern, and a framework for reporting when the going concern basis is not appropriate.

Enhanced reporting by entities on going concern matters will also assist with addressing the knowledge gap as users will be more informed on issues arising, risk factors relevant to going concern, and key judgements made by management /

TCWG on which their conclusions were made. By way of compare and contrast, the accounting standards have very few paragraphs relating to the fundamental concept of going concern, and hundreds of paragraphs/pages related to other individualised accounting issues. Given the focus of users on going concern, the importance of the concept to the operation of the capital markets and economic investment, this misalignment needs to be addressed. Refer to question 1b) for more detail.

The AUASB has received feedback and have observed that there are some inconsistencies in how auditors comply with ISA 570 including the reporting requirements which should be addressed. Refer to question 3a) for further detail. However, in our view these are not contributing greatly to the expectation gap in relation to going concern.

Evolution gap

The AUASB agrees that user expectations have evolved and is supportive of further consideration by all parties in the financial reporting ecosystem as to whether the current reporting requirements in the Accounting Standards and other corporate reporting requirements in relation to going concern are fit for purpose, or whether further reporting would be beneficial.

In relation to the time period for going concern assessments, in Australia we have already extended this to approximately 12 months from the date of the auditor's current report to the expected date of the next auditor's report, which is greater than the time period in ISA 570. The AUASB do not support further extending the time period for going concern assessments beyond our localised position due to the inherent difficulty in obtaining sufficient appropriate audit evidence that provides reasonable assurance on management's assessment and plans over a longer time period. Additionally, extending the relevant period that the auditor needs to assess going concern would also risk increasing the knowledge gap associated with users' understanding of the auditor's responsibilities in this area. And the longer the relevant period after the date of the auditor's report, the higher the likelihood other factors that alter an entity's going concern assessment may occur, such as unanticipated changes in economic conditions or market activity.

The AUASB considers that reporting by entities on other concepts of resilience and longer-term viability should be explored further. Now is an appropriate time to consider if reporting by entities on longer term viability would be of more value than the current going concern assessments alone. Then there should be a careful consideration as to the auditor's responsibility to provide a level of assurance or read and consider (other information) on this type of reporting.

Canadian Auditing and Assurance Standards Board (AASB)

Going concern

Like the views expressed for fraud, stakeholders acknowledged that there was a lack of understanding by users of the role of each party within the financial reporting ecosystem.

Stakeholders emphasized that the role of certain parties in the financial reporting ecosystem, specifically the entity and its management, cannot be ignored. They expressed a view that management's role and responsibilities need to evolve before more can be expected of the auditor.

As it relates to the role of the auditor, they believed that limited revisions to audit standards are needed, and such revisions would mainly be responsive to changes in management's role and responsibilities, and changes to requirements in accounting frameworks.

In our view, there is no one main cause of the expectation gap, but rather, several inter-connected factors/causes.

This view is evidenced by the fact that our stakeholders did not agree on a main cause, expressing varying views. The only item our stakeholders all agreed on was that it is not just the auditor that needs to implement actions to narrow the expectation gap.

Our stakeholders cautioned against putting too much emphasis on any one sub-component of the expectation gap. In their opinion, some actions focused on narrowing the evolution gap may result in an increase in the knowledge gap. For example, expanding the involvement of forensic specialists may result in users having heightened expectations of the audit which may widen the expectation gap.

We used the Discussion Paper's breakdown of the expectation gap by sub-components (i.e., knowledge, performance, evolution etc.) when engaging with our stakeholders during consultations. However, we did not find the sub-components helpful in developing our views and recommendations. The sub-components were interpreted by stakeholders based on their understanding of the role of each party in the financial reporting ecosystem and therefore lacked consistency.

Compagnie Nationale des Commissaires aux Comptes (CNCC) and the Conseil Supérieur de l'Ordre des Experts-Comptables (CSOEC)

Expectation gap relation to going concern

Assessing an entity's ability to continue as a going concern has its inherent limitations which cannot be eliminated. This is due to the fact that no one can predict future events with certainty. A number of recent corporate failures where their financial statements had an audit report with a clean opinion may increase the expectation gap relating to going concern in an audit of financial statements. We consider that the main causes of such expectation gap could be explained as follows:

There is no requirement for Management to disclose in the Financial statements its assessment of the going concern of the entity (i.e. what are the assumptions that have enabled management to assess the entity as a going concern). Unless there is a material uncertainty on the going concern, Management simply states in the notes to the financial statements that they have been prepared on a going concern basis.

There is no clear definition of the going concern concept and no explicit statement from management regarding going concern in the financial statements. It thus seems important to improve external reporting in relation to going concern and the role of all relevant parties (entities and auditors) to narrow the expectation gap relating to going concern.

There are different interpretations on the reference period (time horizon) of the going concern

Going concern is an economic and accounting term used to describe a company which is assumed to be financially stable enough to continue to operate for the foreseeable future, even if there is a material uncertainty about its ability to continue to do so. In accounting terms, financial statement information is considered material if its misstatement, including an omission, would influence users' economic decisions. The notion of "Foreseeable future" is apprehended differently according to the financial reporting framework. It is usually regarded as being at least 12 months from the company's year-end date or the date of auditor's report (depending on the financial reporting framework that the company follows or the country is located in).

Concomitance between bankruptcies and certified accounts with a clean opinion

Stakeholders note a significant number of bankruptcies even though the accounts had an audit report with a "clean" opinion. Users of financial statements expect the auditors to have issued a qualified opinion, as a kind or warning, before a company goes bankrupt, when in fact it can be perfectly appropriate to issue a clean opinion on a set of financial statements that points out to a material uncertainty on the going concern.

In addition, users of financial statements are not aware of the work performed by the auditors in terms of prevention and alert with regard to going concern. As a matter of fact, French law provides for specific reporting responsibilities on the part of the statutory auditors with respect to prevention and alert in terms of going concern, i.e. a specific legal procedure in case of going concern uncertainties (procedure d'alerte, "early warning procedure"), review of specific documents required by French law for certain entities above certain thresholds relating to the prevention of difficulties and going concern.

Hong Kong Institute of Certified Public Accountants (HKICPA)

The expectation gap is mainly due to the general public and financial statement users not fully understanding the work performed by auditors during an audit, referred to in the DP as the knowledge gap.

Based on our outreach to stakeholders, we believe that the expectation gap is mainly a combination of the knowledge gap and the evolution gap. For the knowledge gap, it is observed that the general public and audit report users may not have a thorough understanding or knowledge of the role of auditors and the approaches used and procedures carried out by auditors under the current auditing standards. Hence, the public may over-expect what auditors actually do during an audit of financial statements.

Though we believe the extant auditing standards remain robust and fit for purpose, stakeholders who are preparers of financial statements expressed observations that the current auditing standards may not have kept up with the rapid changes in financial markets and technological advancements. This lag in the development of new standards is identified as the evolution gap.

Institut der Wirtschaftspruefer in Deutschland e.V. (IDW)

Based on our understanding of the issues as described below, we surmise that the knowledge and reasonableness gaps together form the largest portion of the expectations gap.

We are convinced that there will only be at most marginal reductions in the performance gap for fraud and going concern issues if the IAASB improves the clarity of its standards and adds more guidance to support implementation. Other causes of the performance gap (see (b) below), which may be more significant, can only be addressed by other participants in the audit environment.

In relation to the evolution gap, we note that, if asked, users of financial statements and auditors' reports will always want more and better information and therefore seek to have audits evolve further. However, simply seeking to be responsive to these desires without considering that audits and any other additional engagements must be completed within a reasonable time to be relevant to users and at reasonable cost (which is a public policy issue on the proportion of GDP that a society wishes to expend on audits and additional engagements) does not adequately deal with consideration of the societal costs and benefits involved. In line with our comments in the body of the letter, unless the scope of financial reporting frameworks is generally extended worldwide, to the extent that the evolution gap involves seeking to satisfy stakeholder desires (e.g., future viability) beyond an audit opinion on the financial statements and communication of the auditor's findings thereon, such required scope extensions of the audit are beyond the remit of the ISAs and hence the IAASB for financial statement audits.

Adding very robust or enhanced procedures, to improve audits of financial statements, that ultimately cause the costs of audits to increase by orders of magnitude, or incrementally augmenting standards that costs substantially less but only marginally improves audit performance, is not likely to satisfy stakeholders either way: it is unlikely that, given the history of changes made to ISAs 240 and 570 over the last twenty-two years, the IAASB will miraculously discover previously undiscovered "significant quick wins" that substantially increase audit performance for fraud and going concern issues at reasonable cost. Furthermore, as the discussion on KAM when drafting ISA 701 showed, the need, due to independence requirements, to retain audit as an attestation, rather than direct engagement, which implies that original information about the entity ought to be provided by management rather than the auditor, and the related legal confidentiality requirements that the ISAs cannot overcome, mean that improving the transparency of auditor communication to users of the financial statements beyond ISA 701 may be difficult.

The knowledge gap and the reasonableness gap both reflect severe information asymmetry between parties knowledgeable about audits (e.g., auditors, auditing standard setters and knowledgeable regulators) and parties with comparatively little knowledge about audits (e.g., legislators, the media, users, less knowledgeable regulators, and the public). Given the available literature on auditing, including, but not limited to, introductory auditing textbooks, and the content of the auditor's responsibility section of the auditor's report (which was expanded for both going concern and fraud in 2015), lack of interest or diligence appears to be the only explanation for the knowledge gap for those parties supposedly interested in audits but that lack the knowledge to understand what auditors do and are required to do.

While the knowledge gap is severe on its own, the reasonableness gap is a more serious and intractable problem because it relates to public expectations that can never be fulfilled due to the inherent limitations of audits. With the exception of a FEE Paper from 2007 that deals systematically with the inherent limitations of audits, both auditing standards and literature only address this issue in cursory fashion which means that even if parties sought to improve their knowledge about audits in this respect, they would have great difficulty doing so.

Contributing to the reasonableness gap is the problem that for the uninitiated, auditing, like accounting, also suffers from what is often called "numeracy bias" or "precision bias" – that is, the belief that since financial accounting involves numbers and auditing involves examining the veracity of those numbers, properly audited numbers must be "right". The undersigned have encountered numerous instances in which otherwise highly educated representatives of the media, legislators and regulators (often with prestigious law degrees), and members of the public react with disbelief (they appear to believe that the auditing profession is "just being defensive") when the judgmental nature of accounting (recognition, measurement, classification, presentation and disclosures) and auditing and other assurance engagements (e.g., the persuasiveness of evidence) is explained to them.

This is all the more surprising for those with a legal education, since even they recognize that with the power of the courts to gather evidence from entities other than the entity whose financial statements are being audited, search for and seize documents, force the disgorgement of evidence, and subject individuals to interrogation or cross-examination under oath, the prosecution may not be able to obtain the conclusive evidence needed to prove in a court the guilt of a supposed perpetrator of a financial crime beyond any reasonable doubt even when there is virtually no doubt that a crime has been committed. These inherent limitations apply even more so to auditors of financial statements, who do not have these powers and where much of the evidence obtainable is persuasive rather than conclusive. As noted above and in relative contrast to court proceedings, to be relevant audits must be completed within a reasonable time and society expects audits to be performed at a reasonable cost, which represent real inherent limitations to audits beyond the inability to force the disgorgement of evidence, etc.

We believe that auditing standard setters and the auditing profession have exacerbated the information asymmetry versus

other stakeholders about the reasonableness gap by not engaging in a frank dialogue with other stakeholders about this gap for fear of appearing "defensive".

Korean Institute of Certified Public Accountants (KICPA)

(KICPA response) The gap between what the general public expects from audit and what the auditor actually provides is mostly about the knowledge gap, and the gap is mostly associated with the hindsight gap, a gap between expects of stakeholders on auditors prior to a negative event and those after that event occurs, due to the lack of understanding on the inherent limitations of audits, thereby giving rise to the overestimation of the government, regulators and media about the extent to which audit services could provide, which could mislead investors, consumers and other financial statement users about the limitation of auditors' responsibilities.

In addition, auditing standards and practical guidance relating to fraud and going concern issues have difficulties with providing clear guidelines fit for each case. Therefore, in most of the parts, these standards and guidance require that the auditor exercise "professional judgment" throughout the audit procedures, thereby bring about differences in their understanding and application. While the public expectation level and fraud scheme, in particular, have continuously evolved, driven by technological transformation, specified audit methodologies have not advanced in a timely manner, in response to the public expectation and fraud scheme changes, but lagged behind the changes, all of which have resulted in the expectation gap.

New Zealand Auditing and Assurance Standards Board (NZAuASB).pdf

At our roundtable event, 57% of participants identified the knowledge gap as the main cause of the expectation gap relating to going concern. 10% of participants consider that the performance gap was the main cause, 13% considered the evolution gap the main cause. 20% of participants considered that the knowledge gap, the performance gap and the evolution gap apply equally.

Royal Netherlands Institute of Chartered Accountants (NBA)

The various components of the expectation gap each play a role. Regarding the knowledge gap, we should not act defensive as auditors, but see what we can contribute ourselves to improve in this area. We believe that the main reason for the expectation gap is that auditors are insufficiently transparent in their communication and that auditors should report more clearly and specifically about the audit procedures performed and the outcomes thereof.

Furthermore, the performance gap also plays a role. Both the complexity of the standards including interpretation thereof as well as appropriate application thereof are causing

difficulties in practice, the latter being the most important.

Finally, the evolution gap is also relevant. The public expects that technology such as data analytics is used to further improve the audit.

4. Accounting Firms

Deloitte (DTTL).pdf

DTTL believes that elements of the knowledge gap, performance gap, and evolution gap (as described in the discussion paper) all contribute to what has been described as the "expectation gap" (our recommendations on specific steps to address the knowledge gap, performance gap, and evolution gap are included in our response to Question 1b). However, we have specific concerns about the knowledge gap, as outlined below.

Knowledge gap - Lack of public understanding of the responsibilities of all constituents in the financial ecosystem.

The "expectation gap" that has been described and discussed for many years is not limited to the difference between the perceived role of the auditor vs. their actual responsibilities. There is a lack of common public understanding:

that the primary responsibility for the prevention, detection, and communication of matters related to fraud and going concern lies with both management and those charged with governance (TCWG), which includes company directors and others who oversee the strategic direction and obligations related to the accountability of the entity;

of the importance of internal controls over performing an evaluation of the entity's ability to continue as a going concern; and

of the importance of internal control over financial reporting and the part it plays in supporting strong capital markets, fraud prevention, and management accountability.

Entity management, TCWG, and auditors all have a distinct part to play in providing the public with robust financial reporting worthy of trust—and DTTL believes the public's misunderstanding of these shared roles has perpetuated the expectation gap.

Knowledge gap - Lack of understanding of the inherent limitations of an audit.

In addition to the lack of understanding of the responsibilities of management and TCWG, the repeated question, "Where were the auditors?" in each instance of a company's financial demise demonstrates that the public doesn't fully appreciate the inherent limitations of an audit.

By definition, an audit of the financial statements provides reasonable, not absolute, assurance, and there will always be a risk that some material misstatements may not be detected by the auditor, even if the audit was properly planned and performed in accordance with professional auditing standards. The risk of not detecting a material misstatement due to fraud is even higher than not detecting one caused by an error because of the potential for sophisticated fraud schemes designed to hide fraud from detection during the audit, intentional misrepresentation to the auditor, and collusion between employees, or even management and TCWG.

Related to going concern, there is an obvious limitation to predicting future events and conditions. The auditor evaluates management's assessment of the entity's ability to continue as a going concern based on information known at the time and reasonable assumptions made on such information. The occurrence of unexpected or unlikely circumstances could have a significant detrimental effect on the information and assumptions used, resulting in unforeseen challenges to the financial viability of an entity in the short term.

Ernst and Young (EY)

Going concern

We believe that the "Knowledge Gap" and the "Evolution Gap" as outlined in the Discussion Paper are the main contributors to the expectation gap relating to going concern in an audit of financial statements.

The expectations of the users of the financial statements have clearly evolved. Users expect greater transparency to better enable them to understand how management performed their going concern assessment and the relevant events, conditions and assumptions that were included. This has become increasingly clear over the past year. During this period, regulators have stressed the need for entities to be transparent in their corporate reporting, including financial statement disclosures, about the effects of COVID-19 on their business and its future viability. This past year has stress-tested current accounting requirements around going concern and, in our view, has evidenced the need for formal consideration of whether accounting and auditing frameworks remain fit-for-purpose as they relate to addressing and assessing an entity's ability to continue as a going concern.

We believe there is an underlying knowledge gap about the accounting requirements for going concern that is a strong contributor to the knowledge gap that exists with respect to the auditor's responsibilities for going concern.

KPMG

We agree with the IAASB that there has long been an 'expectation gap' in terms of a difference between what users of financial statements and the auditor's report thereon expect from auditors and the financial statement audit and what an audit actually is, in particular, in relation to the critical areas of fraud and going concern. We believe the analysis in the DP, which breaks the expectation gap down into the constituent parts of ‘knowledge gap’, ‘performance gap’ and ‘evolution gap’ is helpful in supporting further exploration of the underlying issues. We consider that all three of these aspects contribute to the expectation gap in respect of fraud and going concern.

Evolution Gap – Fraud and Going Concern

We recognise that there is a significant evolution gap in respect of both fraud and going concern. The UK Brydon Report identified these as being the two areas that stakeholders want more information and clarity about – which we summarise as being whether the company is ‘honestly’ run and whether the company is ‘resilient’, i.e. whether it is likely to survive for a reasonable length of time. We believe it likely that stakeholders would call for certain key aspects of this information to be independently assured. Please refer to our responses to questions 2a) and 3a) for further information and our recommendations to address this aspect of the expectation gap.

In respect of going concern, we note that the purpose of management’s going concern assessment may not be fully understood by all stakeholders of an entity, i.e. there is a significant knowledge gap. In the context of a financial statement audit, management makes a ‘going concern’ assessment to determine the underlying basis of accounting used to prepare the financial statements. This includes determining whether it is appropriate to prepare the financial statements on a going concern basis, or whether this would be inappropriate, and the financial statements should be prepared on a ‘non-going concern’ basis. Material uncertainties relating to the events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern are required to be disclosed but do not change the basis of accounting. Accordingly, the ‘threshold’ at which such a going concern basis of accounting is inappropriate is high – i.e. an entity’s financial statements are prepared on a going concern basis unless management either intends to liquidate the entity or to cease operations or has no realistic alternative but to do so. However, this may not be clearly understood by all stakeholders more broadly, who may view ‘going concern’ conceptually not through the lens of being a fundamental assumption underlying an accounting basis of preparation of financial statements but rather as whether the company as a whole is ‘viable’ or ‘resilient’ in the longer-term.

We also note that terms such as ‘entity’ (i.e. whether this refers to the legal entity or the underlying business), ‘intends’, ‘liquidate’ ‘cease operations’ and ‘realistic’ are not defined and therefore subject to differing interpretations, and, furthermore, there is a lack of clarity as to how these terms apply across the spectrum of business models that currently exist, e.g. start-ups, exploration entities with a limited lifespan, research and development entities, dormant entities etc.

We believe the current concept of going concern in relation to a basis of preparation of financial statements remains appropriate for financial statements and the audit thereon. We recommend the exploration of provision of more information regarding the longer-term viability of an entity, which we believe would be best placed within the annual report, outside the financial statements themselves, and we suggest that the IAASB explore the provision of separate assurance that is not part of the financial statement audit over such information. Please see our response to Question 3a) for further information.

We also consider there is a performance gap in respect of going concern, as there is a lack of clarity regarding certain ISA concepts and terminology, including the term ‘going concern’ itself, as well as regarding material uncertainty relating to going concern (MUGC). We also highlight that there is potential misalignment between ISA 570 (Revised), Going Concern and financial reporting frameworks, including IFRS Standards. We set out further details regarding these areas and our recommendations as to how these issues may be addressed in our response to Question 3a).

The purpose of management's 'Going concern' assessment may not be fully understood by users of financial statements, and this lack of understanding likely contributes to the expectation gap. In the context of a financial statement audit, management makes a 'going concern' assessment to determine the underlying basis of accounting used to prepare the financial statements. This includes determining whether it is appropriate to prepare the financial statements on a going concern basis or whether this would be inappropriate, and the financial statements should be prepared on a 'non-going concern' basis. Material uncertainties relating to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern are required to be disclosed but do not change the basis of accounting. Accordingly, the 'threshold' at which it is inappropriate to apply a going concern basis of accounting is high, i.e. an entity's financial statements are prepared on a going concern basis unless management either intends to liquidate the entity, or to cease operations, or has no realistic alternative but to do so (with 'realistic' also representing a high bar). However, this may not be clearly understood by all stakeholders more broadly, who may view the 'going concern' assessment not through the lens of being a fundamental assumption underlying an accounting basis of preparation of financial statements, but rather as whether the company itself is 'resilient/viable' in the longer-term.

This may lead to a fundamental misunderstanding of the role of the auditor (as well as of management/ those charged with governance), which we do not believe is capable of being addressed by making changes to the ISAs, or indeed to other standards, including financial reporting standards.

We also note that there is an evolution gap, which we describe in more detail below under Evolution Gap – Fraud and Going Concern.

MHA Macintyre Hudson (MHA)

Similarly, the Going Concern gap relates to a greater or lesser degree in all three aspects of the gap. The expectation gap relating to what users/the public think the auditor does and reports on compared to the expectations on auditors set out in standards. In our view, issues around going concern are linked to the current limitations on auditor's responsibilities, i.e., how much more auditors can do or should do in relation to going concern.

Regarding the Performance Gap, there are examples of auditor's not sufficiently challenging management's assessment of going concern. It should be noted that management does not always perform the assessment to the standard required. Furthermore, there is an evolutionary gap as more expectation is placed on the assessment of going concern and wider auditor consideration of disclosures and qualitative information, including the impacts of climate change, sustainability, ESG and one-off events like the current pandemics.

MNP LLP (MNP)

We are of the view that the three components of the expectation gap, as stated in a May 2019 publication by the Association of Chartered Certified Accounts (ACCA): knowledge gap, performance gap and evolution gap, are all causes of the expectation gap relating to fraud and going concern in an audit of financial statements. In the context of the IAASB's workplan, we have focussed our comments on the knowledge gap and evolution gap.

As stated in the DP, some users of the financial statements do not understand what an audit entails and may have unreasonable expectations of what an auditor ought to do in comparison to what they are reasonably capable of doing due to the inherent limitations of an audit. That is, such investors may believe that the role of the auditor is to detect fraud, material or otherwise, and conflate resilience statements with the going concern concept.

In contemplating amendments to audit standards and broader deployment of newer audit techniques, we are conscious of their impact on cost-effective timely financial information. We are mindful of the ability of emerging growth public companies and small and medium sized enterprises (SMEs) to support such audit changes. In Canada, this would represent an extremely significant portion of the marketplace. Moreover, certain changes may deepen the expectation gap. For example, audit tools that test the internal integrity of 100% of a client's transactions may still not connect to external evidence nor necessarily detect fraud or management bias, despite a potential undue reliance by financial statement users on these technologies

Moore (MGN)

We do not believe that there is one 'main cause' for any of the disconnects which exist, including for any universally agreed 'expectation gap'. In particular, we do not necessarily believe that the gaps in expectation (and other factors) arising in relation to fraud and going concern are the same or have identical causes (although there may be similarities both between the various disconnects and the reasons for those disconnects).

In our view a key to resolving disconnects is to recognise not just that they are nuanced but that there can be no meaningfully effective solution that does not address and include all the members of the ecosystem. Nevertheless, we appreciate that IAASB has the role of determining audit standards and therefore will primarily be addressing issues relevant to the auditor piece – but this should be considered in the context of the nature and circumstances of the issues as a whole.

With regard to going concern, some stakeholders appear to expect auditors to be able to predict with certainty an entity's financial and economic viability and resilience. Some of these expectations are reasonable, to an extent, many are not.

PKF International Limited (PKF)

The expectation gap relating to fraud and going concern in an audit of financial statements is caused by a combination of two factors:

users of financial statements not having an accurate understanding of how the audit is conducted; and

ineffective communication from auditors to the users of financial statements on how the audit is conducted.

The expectation gap is further widened where users of financial statements desire, and believe they receive, a greater level of assurance from the audit than the reasonable assurance that the audit opinion provides.

The expectation gap comes under increased public scrutiny for each high-profile corporate failure. In light of current global conditions and the economic outlook for the medium-term, it is probable that more situations will arise which will provoke further debate on this topic.

PricewaterhouseCoopers (PWC)

We believe that the components described in the Discussion Paper (DP) – Knowledge Gap, Performance Gap and Evolution Gap – are a reasonable way to articulate the expectation gap.

It is not always clear which of these components is the main driver of the expectation gap relating to fraud and going concern in an audit of financial statements. In reality, it is often a combination thereof.

In addition, perceptions of the expectation gap at any point in time are likely to vary depending on recent events or conditions as well as contextual factors including the local jurisdictional legal and regulatory regime, and the corporate reporting and governance model in place. This complicates finding solutions that are applicable and equally effective globally.

5. Public Sector Organizations

Auditor General of South Africa (AGSA)

The main cause in our view is the lack of understanding by users of the financial statements as to what the objective of an audit and the responsibilities of an auditor are. Users and the public at large do not understand what reasonable assurance means or that there are inherent limitations within an audit. The general public may also not understand that there is a difference between a regularity and forensic audit and what the key differences are.

Unfortunately there is also an element of incorrect application of the audit standards on fraud and going concern, partly due to the complexity of the standards and partly due to the limited application of professional scepticism by the auditors. Furthermore the general public may not be regarded as a primary user of the financial statements resulting in the information needs of the public not really being considered when planning the audit approach for fraud and going concern.

Australasian Council of Auditors General (ACAG)

We noted the following as the main causes of the expectation gap:

The ongoing misunderstanding by users of the financial report of:

-the scope of a reasonable assurance engagement (with linkages to fee pressure)

- the period that the audit report covers; historical not forecasts

New Zealand Auditor General (NZAG)

We consider that a knowledge gap and a performance gap exists in respect of going concern. In our view, this gap arises because of a misunderstanding amongst preparers, auditors and users about what “going concern” actually means in the context of an entity’s financial statements. Preparers are required to assess if the entity is entitled to use the “going concern basis of accounting”.

For practical purposes the use of the “going concern basis of accounting” is often interpreted as the ability of the entity to survive 1 year from its balance date, or 1 year from the date of the auditor’s report on the financial statements for a particular balance date. This is a very narrow concept of going concern and the users of the financial statements often look at various other indicators to consider an entity’s performance. The general understanding of going concern often does not take into account other factors or external developments that could provide an indication that the entity’s business model may be unsustainable.

The requirement to consider other external factors will increasingly become important in audits of sustainability and climate-related information where the timeframes for the information involved are likely to span more than 12 months.

In our view, the requirements placed on preparers to justify their use of the “going concern basis of accounting” as the basis for preparing their financial statements needs to be very clear. For example, the “resiliency statement” prepared by certain entities in the United Kingdom places greater demands on entity management and governors when asserting an entity is a going concern in the context of preparing the financial statements of the entity.

If a clear understanding is reached on what going concern means, in the context of an entity's financial statements, the entity will need to provide evidence (supported by suitable disclosures in the financial statements) that it is justified in asserting it is a going concern. This in turn provides the auditor with an appropriate platform from which to assess management's use of the going concern assumption.

6. Professional Accountancy and Other Professional Organizations

American Institute of Certified Public Accountants (AICPA)

We agree that the differences between what the public thinks auditors do and what auditors actually do, or the "knowledge gap" as described in the Discussion Paper, likely contributes to the expectation gap and believe it may be best addressed through education of the users of the auditor's report. We note that in some instances auditors may not properly implement the requirements in the auditing standards, however we believe further outreach and research are warranted to assess the extent to which that is a function of the standards being overly complex or unclear, or of auditors not exercising due professional care in interpreting or adhering to the requirements. Such outreach and research would inform decisions regarding allocation of resources to enhance auditor education and instruction and standard setting. A better understanding of the causes of an expectation gap will be helpful to determining what actions will be most effective in reducing the gap.

Center for Audit Quality (CAQ)

Of the three components outlined in the Discussion Paper, we believe that the "Knowledge Gap", or the difference between what the public thinks auditors do and what auditors actually do with respect to fraud and going concern, is the component that is most often responsible for the expectation gap.

With respect to going concern, we believe that in addition to the "Knowledge Gap", the "Evolution Gap" also contributes to the expectation gap. Considering the related accounting and auditing standards together with the modernization of business and user needs could address the "Evolution Gap".

CFO Forum

In addition to the knowledge gap we also believe that the expectation gap results from an evolution gap and a performance gap. An evolution gap represents the fact that the planning of an audit does not always sufficiently evolve over time to appropriately consider all the developments within an environment and industry that an audit client operates in. A performance gap relates to audit procedures (or a lack thereof) that may not always fully comply with audit quality requirements.

A performance gap may, for example, result from audit engagement team members not having sufficient and appropriate knowledge and/or understanding of the business environment, operations and the related business risks of the audit client in order to design appropriate audit procedures to address the relevant audit risks. This can also manifest in the inconsistent application of audit standard requirements where there is little guidance and/or supporting material to assist with the effective application thereof. A lack of "professional skepticism" or "suspicious mindset" further affects this performance gap.

The CFO Forum believes that the expectation gap arises directly from a knowledge gap where the users of financial statements may either not fully understand or have unrealistic expectations of what an audit entails; as well as from a performance gap where there is a shortfall in the quality of the audit work performed.

The knowledge gap effectively represents the difference in knowledge between what the public assumes an auditor does during the performance of an audit together with the related level of assurance that the audit report provides, versus what auditors actually do and the level of assurance provided. This mismatch therefore stems from the public perception pertaining to the role of auditors.

Chartered Accountants Australia and NZ and ACCA - Joint (CAANZ-ACCA)

From our outreach, we believe that the main causes of the expectation gap in relation to fraud and going concern are the knowledge gap and the evolution gap. There were limited areas where performance gap issues were considered as a main cause compared to the other gaps.

1. In regard to the expectation gap (see Section I):

(a) What do you think is the main cause of the expectation gap relating to fraud and going concern in an audit of financial statements?

According to feedback received in our outreach for this DP, there was a wide recognition that the expectation gap is a wider financial reporting ecosystem issue with all relevant stakeholders having a role in narrowing it, as noted in the DP. The views we've heard regarding the main cause of the expectation gap relating to fraud and going concern were mixed, with most stakeholders referring to the knowledge and evolution gaps. Some feedback was also provided for the performance gap but to at a lesser extent.

Knowledge gap

We consider that there is still a lack of understanding by the general public regarding the purpose of an audit and what the respective responsibilities of auditors and those charged with governance are, in relation to the management of risks, the preparation of financial statements and the provision of assurance over those financial statements. In the case of going concern, this is exacerbated by the lack of clarity over the concept of going concern used in the accounting standards which drive preparers' responsibilities versus the auditor's responsibilities established in the auditing standards. There is also the fundamental issue that, at heart, users would like there to be no corporate failures or fraud even if this is not achievable in our current markets, regardless of how much regulation is put in place.

Furthermore, some of the feedback received emphasised that there is a general lack of knowledge regarding fraud and a confusion as to what fraud means in the context of an audit of financial statements. Recommendations suggest audit firms need to place more emphasis in educating their staff via training regarding fraud, if they are to be in a better position to detect and report fraud when it occurs and/or properly investigate suspicions.

Evolution gap

Based on the feedback received, the other primary cause of the expectation gap relates to the evolution gap. During our outreach a large majority of the stakeholders expressed the view that, for auditors, there is more room for evolution in the area of fraud than for going concern.

Some stakeholders also suggest that the focus should only be on the evolution gap and how the profession can evolve to satisfy users' expectations rather than keep focusing on the knowledge gap as one that will always exist. Businesses continue to increase in complexity and, in response, users' expectations of what they require from assurance changes over time.

Performance gap

Although according to the feedback received, fewer stakeholders identified the performance gap as one of the main causes of the expectation gap, some stakeholders, other than audit practitioners, consider that the expectation gap is caused either by auditors not following the requirements of ISA 240 or because the requirements of ISA 240 are not robust enough.

We note that in respect of the performance gap, in the UK as per the Brydon report it was noted that ISA (UK) 240, the equivalent UK standard on fraud, 'appears to be a balancing act between managing, or possibly lowering, expectations whilst seeking to avoid going so far as to affect significantly users' perceptions as to the value of audit. The messaging in this standard is therefore somewhat ambiguous, in Brydon's view'. Similar points were raised by regulators during our outreach, more specifically, regarding para 5 of IAASB's ISA 240 which states that 'while the audit may be properly planned and performed, some material misstatements may not be detected' who are of the view that such statements undermine the auditor's responsibility in detecting and reporting fraud. As a result, the UK Financial Reporting Council (FRC) is currently consulting on certain revisions to ISA (UK) 240, to address some of the concerns raised in the Brydon report. In our view, the feedback received by the FRC on these revisions will be very relevant for the IAASB's consideration.

CPA Australia (CPAA)

The entity collapses or enters into some form of administration without warning signs which, had warnings been available, may have enabled a more timely response or could have put stakeholders on notice of the risks and uncertainty faced by the entity (knowledge, performance and evolution gaps).

We consider that the main causes of the expectation gap in relation to fraud and going concern are explored and articulated well in the DP. The DP describes the expectation gap as comprising knowledge, performance and evolution gaps. However the components are categorized, in essence they arise when:

Federacion Argentina de Consejos Profesionales de Ciencias (FACP)

Knowledge gap: We understand that this is the main cause of the expectation gap.

Evolution gap: respect going concern the auditor frequently uses professional judgment, it is also possible that the latest technological tools available for detecting the risk of fraud in financial statement audits are not used, for these reasons it is convenient that some procedures used by the auditors are reviewed.

Institute of Certified Public Accountants of Uganda (ICPAU)

Some users don't appreciate that the primary role of the auditor is to express an opinion whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. Relatedly, as technological competencies take centre stage in the main business world, the aspects of fraud and going concern become vital and very sensitive. This tends to refocus the public expectation in terms of what the auditors should do if the expectation gap is to be narrowed.

ICPAU believes that the key components of the expectation gap including the knowledge, performance and evolution gaps, require equal effort in demystifying the difference between what users expect from the auditor and the actual obligations of the auditor in an audit of financial statements. The expectation gap is generally due to the difference resulting from misconstruing and or misapplication or neglect of changes taking place world over to suit the current provisions of the auditing standards.

Institute of Directors in South Africa's Audit Committee Forum (IoDSA ACF)

The ACF Forum believes that the expectation gap arises directly from the combination of two specific gaps – the knowledge gap and the delivery gap.

The knowledge gap arises when the level of assurance with regards to the work performed by the auditor is assumed to be at a level higher than actually expected of the auditor under the current auditing standards.

The delivery gap arises when the work delivered by the audit team does not adequately meet even the current auditing standards relating to fraud and going concern. The delivery gap is a matter that both audit committees and audit regulators can pay increased attention to, in measuring whether auditors are compliant with current (and future) auditing standards on fraud and going concern.

Kriton (KNL)

In our opinion, the cause is a complex of factors, as was also mentioned in the discussion paper. None of these factors can be considered the main cause of the expectation gap.

In our opinion, the following factors play a role in the expectation gap around the use of the going-concern assumption:

Wishful thinking by management (and where applicable, those charged with governance): signals of potential problems - which are sometimes obvious - are, consciously or not, ignored in the preparation of the financial statements. This may be related to pressure resulting, for example, from expectations raised by stakeholders, the remuneration structure, financing conditions or the feeling of having failed as an entrepreneur.

A lack of objectivity, professional competence and/or professional scepticism on the part of the auditor: the interest of the client (painting a positive picture) consciously or unconsciously prevails over the public interest (fair reporting), signals of any problems are overlooked during the audit or not evaluated critically enough and investigated further.

Reluctance on the part of management (and the auditor) with regard to disclosure about a possible uncertainty about the continuity of the entity: this could be a self-fulfilling prophecy, because financiers, suppliers and customers, for example, are deterred.

Unfamiliarity among users of financial statements and auditor’s opinions with the actual meaning of using the going-concern assumption when preparing the financial statements: what period does it concern, how should the certainty or uncertainty about the going-concern assumption be interpreted and what is the scope of the reports by management and the auditor on this?

In a number of recent disciplinary rulings in the Netherlands about presumed audit failures in relation to the bankruptcies of audited entities, the factors mentioned in the first two bullets play a role to a greater or lesser extent.

Malaysian Institute of Certified Public Accountants (MICPA)

The components described in the Discussion Paper (Knowledge Gap, Performance Gap and Evolution Gap) are a reasonable way to articulate the expectation gap. However, it is not always clear which of these components are the main driver of the expectation gap as it is often a combination thereof.

Mexican Institute of Public Accountants (IMCP)

Going concern

Users of audited financial statements know the risks of their decisions, however if those risks materialize, then what was assumed as a risk may become a claim.

There can be other causes of the gap between expectations and reality regarding the entity's ability to continue as a going concern, such as auditors' work not complying with professional standards or regulatory requirements, or financial statements preparers not disclosing in conformity with the applicable financial reporting framework. But the main cause of that gap is the out of proportion users' expectation about the auditor's work on this matter.

Even though the entity's management has assessed and determined its capacity to continue as a going concern, and the auditor has obtained sufficient evidence supporting such determination, as of the date of the financial statements and the date of the auditor's report, if the entity ultimately cannot continue as a going concern, users of the entity's audited financial statements will ask: "why did the auditors not disclose it in their audit report?"

This approach involves a combination of the knowledge gap and the evolution gap. Occurs both by: 1) an expectation based on the needs of users, regardless of whether the auditors' professional and legal requirements are sufficient for their purposes; and 2) an incomplete response to this expectation, given the nature and scope of an audit of financial statements, and what the financial statements themselves present and disclose, in accordance with the applicable financial reporting framework.

Users expect a high degree of protection for the results of decisions they make based on audited financial statements. The auditor cannot assume the role of provider of that protection.

Despite the existing literature on auditing matters, many users of audited financial statements still do not have a whole understanding of the nature, scope and limitations of an audit of financial statements, nor the responsibilities of external auditors. Consequently, users' expectations exceed the corresponding professional standards and regulatory requirements.

South African Institute of Chartered Accountants (SAICA)

Similarly with going concern, auditors may find management's assumptions and basis for conclusion on the use of the going concern basis of accounting appropriate and a corporate failure may occur at the same company a few months down the line. This contributes to the widening of the expectation gap, particularly as it relates to the knowledge gap. In making the determination on the appropriateness of the going concern basis of accounting, auditors often make use of historical financial information to predict future trends. In addressing the evolution gap, there is a need to relook at the examples of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern provided in paragraph A3 of ISA 570, Going Concern. For example, negative analysts' reports on the future of a company could be an example of an event or condition that may need to be considered by the auditor. Some of the trends identified in the recent corporate failures should be incorporated in these examples. Furthermore, technology and data analytics could provide the auditor with useful trends, including industry specific trends that may allow for more appropriate conclusions on going concern to be made.

One of the reasons for the expectation gap is that there appears to be a lack of understanding of what the needs of the public are in relation to an audit of financial statements. This could be due to the fact that there are no mechanisms for dialogue between the public and the auditors resulting in a lack of understanding in terms of what auditors are expected to deliver. The term 'public' is undefined and often used loosely without clarity as to which stakeholder groups represent the public's views with regard to the audit process. These stakeholder groups may vary from one jurisdiction to the other but it is critical that they are identified and for formal mechanisms to be implemented in order to identify how best to solicit their views on the expectations of an audit of financial statements. The stakeholder groups may also vary as a result of differences in complexities, size, laws and regulations and the regulators who oversee the entities being audited. Some of the traditional stakeholder groups include regulatory authorities such as audit regulators, stock exchanges and large institutional investors that may have a direct interest in the audit process. However, there is a need to move beyond the traditional stakeholder groups to allow for a more inclusive process.

Users of financial statements have evolved from being predominantly individuals with financial backgrounds to individuals from various other careers. This has led to a lack of understanding over audit concepts such as materiality, the responsibilities of management with respect to fraud and going concern, and the concept of reasonable rather than absolute assurance.

It can be argued that a significant contributor to the expectation gap is the information contained in media reports and other information reported on informal platforms such as social media, which may contain misleading information that adds to widening the knowledge gap. There is a need for appropriate structures to be created to address the expectation gap in appropriately responding to media reports and ultimately educating the public on the roles and responsibilities of the auditor.

The distinction between the knowledge, performance and evolution gap as defined in the Discussion Paper is useful. Any changes to the International Standards of Auditing (ISAs) that the IAASB may propose will only address the performance gap in clarifying the requirements and the evolution gap in responding to the changing needs of the general public demands, but other action is required to address the knowledge gap. This is probably the reason why, although the ISAs have been updated and revised over the years, the issue of the expectation gap remains unabated. The importance of educating and having a continuous dialogue with the appropriate stakeholder groups in an effort to close the knowledge gap cannot be emphasised enough. This should not be the responsibility of the IAASB alone but of everyone involved in the wider financial reporting ecosystem. It is SAICA's view that the knowledge gap is the main contributor to the expectation gap as this is beyond the profession's control. The mere fact that auditors are also called "watch dogs" might be an indication on what the public expects from auditors, compared to what they really do.

The complexities of business and the very stringent reporting deadlines imposed by regulators and management, together with the ever-reducing number of auditors have increased the workload and pressure and due to this, the appropriate composition of the audit teams may be lacking. This contributes to widening the evolution and performance gaps.

<u>9. Individuals and Others</u>

Christian Minarriz (CM)

Regarding performance gap for going concern, I think there is some lack of understanding and/or difficulty to apply the ISA 570 requirements in practice, especially regarding the required work to evaluate the feasibility of management plans, the work to be done regarding assumptions for cash flow projections (and if ISA 540 also applies) and how to evaluate if there is “material uncertainty” or just a “close call”. The lack of guidance in accounting standards (including IFRS) about the required disclosures also generates some issues.

Regarding knowledge gap for going concern, I think many people have the idea that auditors are able to guarantee the ability of an entity to continue as a going concern but fail to understand that auditors cannot predict the future. This is further enhanced by the increasingly volatile economic environment (especially in some jurisdictions).

Regarding evolution gap for going concern, I do not see other issue than the expectation of more explicit auditor statements about the future viability of the audited company.

Following the ACCA´s component classification of “expectation gap”, I think that the 2 major components are knowledge gap and performance gap, while evolution gap has some impact in fraud but a relatively smaller impact in going concern.

Q1a-2.2 - Evolution Gap

N/A

Q1a-2.3 - Knowledge Gap

<u>2. Regulators and Audit Oversight Authorities</u>

Botswana Accountancy Oversight Authority (BAOA)

In regard to the expectation gap (Section 1):

What do you think is the main cause of the expectation gap relating to fraud and going concern in an audit of financial statements?

Users of financial statements, not knowing exactly what the Auditors responsibilities are in relation to fraud and going concern. General expectation is that the responsibility for detection of fraud and assessment of going concern lies with the Auditor. This, however, is not the case as per the International Standards on Auditing (ISAs).

The Auditors responsibilities as defined by the ISAs viewed to be not as robust to detect or identify fraud and going concern matters.

ISA 200 requires the Auditor to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatements, whether due to FRAUD or error. When an audit opinion has been given to that effect, and later on there is a corporate collapse, stakeholder start asking questions such as, ‘Where were the Auditors’. Ideally a reasonable assurance is expected to be supported by sufficient appropriate audit evidence, in this case such evidence is assumed to cover fraud.

Canadian Securities Administrators (CSA)

We think the expectation gap relating to going concern is largely due to the knowledge gap resulting from the unclear wording in the auditor’s report relating to going concern in conjunction with an emphasis of matter paragraph. The wording, “when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern," is vague and in some cases, not understood by users of the financial statements. The term "going concern" itself may not be well understood by users. We think the existing auditor responsibilities with respect to going concern are clear; however, the auditor's report does not highlight that the auditor does not make a positive assessment of going concern.

3. National Audit Standard Setters

Malaysian Institute of Accountants (MIA)

The public may not fully understand the technical terms used in auditing standards and the various conclusions conveyed in the auditor's report. A qualification in the audit opinion still appears to be the only commonly understood deviation from a clean audit report. The public may not understand that, in the absence of any reference to a material uncertainty related to going concern (MUGC), an auditor's report cannot be viewed as a guarantee on the entity's ability to continue as a going concern.

The public expects the auditors to raise the red flag before an entity has a going concern issue. However, this expectation is inconsistent with the auditor's role under ISA 570 Going Concern where an auditor is required to conclude, based on the audit evidence obtained, whether a material uncertainty exists about the management assessment about the entity's ability to continue as a going concern.

Unlike the auditing standard (ISA 570) which is quite comprehensive, there are minimal requirements in the accounting standard (IAS 1 Presentation of Financial Statements) to govern the management's assessment and disclosures relating to going concern.

The management's assessment of an entity's ability to continue as a going concern involves making judgment, at a particular point in time, about uncertain future outcomes of events or conditions. Subsequent events may also result in outcomes that are inconsistent with judgments that were reasonable at the time they were made. Sometimes, the public may fail to understand this matter and do not take into consideration the period of assessment covered by the management and auditor in the going concern assessment.

The expectations of users of financial statements have evolved over time. Users expect greater transparency to better enable them to understand how management had performed their going concern assessment. As a result, there is an information gap between the information that an entity discloses about its going concern assessment and the information stakeholders need to understand the viability of an entity.

In addition to knowledge gap, we also believe that performance gap and evolution gap are also causes of the expectation gap, as stated below:

Performance gap

Auditors may have omitted certain audit procedures as required under the auditing standards due to the complexity and unclear requirements of certain standards.

Evolution gap

Audits may not have evolved to meet changing expectations due to changing business landscape and developments in the environment such as the use of technology by both reporting entities and auditors. Standard setters should recognise that the use of technology by reporting entities creates different opportunities and fraud risks within an organisation, particularly when those entities are implementing new technology applications at an increasing pace. On the flipside, the auditor's use of technology is equally important to address fraud risks and to identify potential misstatements due to fraud.

The public is looking for enhanced procedures in relation to fraud and going concern that is not currently provided by the requirements of the auditing standards and is getting more demanding that the financial reports should be more predictive rather than merely reporting on historical numbers.

Due to increasing disclosure requirements in the financial statements, sometimes the public may tend to ignore certain general information such as auditors' responsibilities for the audit of financial statements. This may widen the expectation gap.

In your view, wh

We are of the view that knowledge gap is the main cause of the expectation gap relating to fraud and going concern in an audit of financial statements whereby the public misunderstands the role and responsibilities of auditors relating to fraud and going concern, as stated below:

4. Accounting Firms

BDO International Limited (BDO)

Discussions within our network indicated that the largest factor which had resulted in an expectation gap was the knowledge gap - particularly amongst those stakeholders who are not as closely involved in the audit process – such as investors, shareholders, the public.

Taken as a whole, we also recognize that the expectation gap is not just 'someone else's problem' and that, as a profession, auditors should not be complacent. We may have a key role to play through (1) steps to evolve what and how we perform our procedures, (2) better communication of what we have done, and (3) improved or clearer performance of our procedures.

It is important to note that in our discussions, we perceived there to be:

A difference in the expectation gap relating to fraud and going concern – while they may be linked, the expectations of users for each may differ (and the causal factors may be different too).

When a material fraud has occurred at some point in the past and the nature of an auditor's work is to review to what has already happened (i.e., to look back retrospectively), there is an expectation that auditors should be able to identify that material fraud.

For going concern, stakeholders have a more realistic understanding that auditors are not able to predict the future especially as the 'future' is being set out by management's assessment of going concern. So, in general, there appears to be less of an expectation gap in this particular area.

Differences in the relative importance of the knowledge, performance and evolution gaps for fraud and going concern respectively; also, the extent to which these 'gaps' were dependent on each national jurisdiction (for example, a number of colleagues cited innovations in financial reporting ecosystems that had been implemented to improve reporting on fraud or going concern matters, through additional procedures or controls testing).

Potential causes of the knowledge gap included:

Communication challenges – whereby components of the financial reporting ecosystem and those outside the system, such as the media and public, may not have a sufficient understanding of what the scope of an audit entails and specifically the standards' requirements for auditors in relation to fraud and going concern. Conversely, we received feedback that:

Auditors may need to do a better job of communicating what has been done (through improved transparency, greater focus on certain areas, etc.).

There may also be a role for regulatory and professional bodies to aid consumption of financial statements information (and an understanding of what it is to be audited), and to better explain how different parts of the financial reporting ecosystem operate.

Expectations about the extent of an audit – there may be a perception that being audited means that everything has been checked which contrasts with ISA concepts of:

Materiality

Adopting a risk-based set of procedures to address assessed risks

Obtaining reasonable (but not absolute) assurance that the financial statements are not materially misstated.

Nature of fraud and going concern – another factor contributing to the knowledge gap is that despite the procedures performed by auditors, there remains an element of risk that is unaddressed, essentially because:

Fraud is, by its very nature, designed to be concealed, making it difficult to detect, particularly when accompanied by collusion and/or extending over a longer period of time;

Going concern includes an element of unpredictability as it is based on future events and, as we have seen in recent recessions and the COVID-19 pandemic, facts and circumstances can and often change quickly and without warning.

Other suggestions we received during our discussions, included:

Variations in laws and regulations at the national level which may mean there are different requirements when reporting on fraud in the auditor's report (which has already started to emerge in certain jurisdictions) or regarding the reporting timeframes being considered in respect of going concern (whether from reporting date, financial statement date, auditor's report date, etc.).

A failure to communicate to TCWG (or, in the case of small owner-managed businesses, directly to management) what procedures we have performed around fraud and, to a more limited extent, going concern.

A perceived failure by auditors to use forensics or fraud experts as part of their audit strategy and planned approach, particularly where facts and circumstances, with hindsight, may seem to suggest that it would have been prudent to do so.

Crowe (CG)

The main cause of the expectation gap relating to fraud and going concern in an audit of financial statements are perceptions by some groups of stakeholders that the audit is an exercise in "fraud discovery" and that auditors have a greater responsibility for forming an opinion on going concern than is actually the case.

GTI

In our view, the main cause of the expectations gap relating to fraud and going concern in an audit of financial statements is the knowledge gap – described in the Discussion Paper as the difference between what the public thinks auditors do and what auditors actually do. This can also be somewhat exacerbated by the media focus on the auditor when frauds or going concern issues are uncovered subsequent to the completion of the audit and the issuance of the auditor's report, especially when this results in the failure of the business. Media focus, in general, is naturally biased towards coverage of such issues and the perceived failures of the auditor, rather than providing more balanced reporting that also reports instances where the auditor has been instrumental in identifying issues or have even prevented a fraud from being perpetrated just through the performance of an effective audit.

HLB International (HLB)

We acknowledge that the performance gap is also a contributing cause to the expectation gap. In particular, consideration of fraud and going concern in an audit of financial statements should be an area lead and completed by partners and managers, with junior staff observing for training and education purposes.

We believe that the main cause of the expectation gap relating to fraud and going concern in an audit of financial statements is a knowledge gap, a difference between what the public thinks is provided by an audit engagement and what an audit engagement is actually intended to do. In particular, there is a knowledge gap regarding the concept of reasonable assurance (as required by the ISAs) versus absolute assurance, as is sometimes expected by the public.

Mazars (MAZ)

Going concern

We think that the main reason for the expectation gap regarding going concern is that there are "Differences of view as to the meaning and implication of material uncertainties and the going concern concept" which creates a knowledge gap.

The expectation gap is split in the paper between knowledge, performance, and evolution gaps and we believe all are valid.

We do not believe that the evolution gap is a significant contributor to the expectation gap at this time.

The knowledge gap has historically, and continues to be, a significant cause of the expectation gap. This is in part due to the expectations of stakeholders, many of whom are not necessarily concerned with understanding the role and responsibilities of the auditor. Clearly there is a need to engage all financial statement users in having a common understanding of the relevant roles and responsibilities for addressing fraud and going concern among the auditors and the Management and TCWG.

Even though we believe it is not the main reason, the expectation gap may be also linked to the performance gap as described in the discussion paper.

Also impacting the knowledge gap is the frequent lack of clear disclosure of management's key assumption around the going concern analysis. While we recognize that it is outside of the purview of the IAASB, having stronger disclosures regarding the key assumptions and data used in assessing going concern assumption, as well as the time period considered, would benefit users.

Mazars USA (MAZUSA)

Response: We believe the knowledge gap is the main cause of the expectation gap. We recognize there are performance and evolution gap factors as well, but to a much lesser degree, therefore our focus is on closing the knowledge gap.

Nexia International (NI)

There is also an expectation gap regarding going concern. Here the gap lies in user's reliance on the auditors to tell the story of a company's strategic and operational plans to continue as a going concern. In the past, too much emphasis is placed on the auditor as it relates to this topic. Much of what is provided by management to support going concern assumptions are related to future or projected events and transactions. Management is in a better position to tell users this story than the auditor. The expectation can simply not be that the auditor is responsible for the viability of a company's operations.

The directors do not guarantee an entity is a going concern, and there is no basis for the auditor, who is not responsible for the management or operation of the entity, to be held to a higher threshold.

RSM International Limited (RSM)

Given the responsibilities of auditors, management and those charged with governance under the current auditing standards, in our view the main cause of the expectation gap which exists at the present time is the "knowledge gap".

However, we also acknowledge the findings of the recent report in the UK by Sir Donald Brydon "Report of the Independent Review into the Quality and Effectiveness of Audit", which was clear that auditors cannot solely blame this expectation gap on a lack of user knowledge. The profession has been attempting for decades to help users to better understand the nature and limitations of the audit, yet the expectation gap persists, so we suggest that a change of approach should be considered.

High-profile instances of audit failures in several, though not all, jurisdictions make it difficult to avoid the conclusion that there is also a "delivery gap" in the performance of audits that needs to be addressed. While this may be partly attributable to failures to follow the current ISAs, a "performance gap", we believe there is also a need to assess whether the ISAs in these areas are fit for the purpose of meeting users' reasonable expectations; an "evolution gap." Therefore, we welcome the IAASB's discussion paper on these critical audit areas and support a review into whether these current responsibilities remain appropriate.

5. Public Sector Organizations

US Government Accountability Office (GAO)

We generally believe that the expectation gap exists because financial statement users may not understand financial statement auditing standard requirements and related scope of financial audits. As noted in the discussion paper, auditing standards require auditors to obtain reasonable assurance rather than absolute assurance. Also, audits focus on material misstatements rather than all misstatements. In our view, financial statement users' misunderstanding of auditing standards is the main cause of the expectation gap relating to fraud and going concern.

6. Professional Accountancy and Other Professional Organizations

Botswana Institute of Chartered Accountants (BICA)

The main contributor to the expectation gap is the knowledge gap. More often the public, including those charged with governance, lack the basic principle of what financial statements audit entails. In most cases the expectation is that the auditor has the responsibility of detecting fraud and assessing an entity's going concern. For this reason, investors often attempt to take action against the auditors when things go wrong for any period for which the auditor issued an unmodified report.

Institute of Chartered Accountants of Scotland (ICAS)

From the model used by the IAASB, the main cause in our view is the "knowledge gap", i.e. the difference between what the public thinks auditors do and what auditors actually do. This recognises that the public may misunderstand the role of auditors and the requirements of the auditing standards. We do need to be careful here, however, as to regards what constitutes "the public". Given the inherent complexities associated with business, and indeed financial reporting, it is questionable whether it would be possible for an average member of the public to properly understand the purpose and objectives of an audit. Therefore, we believe that closing the perceptions gap has to be targeted at a particular group, e.g. an informed investor or equivalent in relation to the audits of public interest entities to have any real hope of closing this gap.

International Federation of Accountants (IFAC).pdf

The IAASB's reference to the ACCA's description of three components of the expectation gap: the "knowledge gap," "performance gap" and "evolution gap" is helpful. The significance of the gap is likely to vary internationally, and measuring its extent objectively is inherently challenging as there are many different expectation gaps, even between those in the same stakeholder groups. We agree that some users of financial statements and other stakeholders may misunderstand the role of auditors and requirements of the ISAs in relation to others in the financial reporting ecosystem. In addition, there can be a lack of understanding that management and those charged with governance have the primary responsibility for the prevention and detection of fraud and assessing the entity's ability to continue as a going concern. One of the factors contributing to the expectation gap is a failure to understand the situation auditors face in reporting on matters such as going concern in the absence of adequate reporting to investors and employees by directors, which may also lead to calls for auditors to address issues that are unreasonable (i.e., an unreasonableness gap).

The role of the audit is to test the veracity of management's assertions as presented in the financial statements, which means that the auditor cannot be the original source of information about a company. Client confidentiality regulations also generally prohibit this. If the auditor finds that a company has presented information incorrectly, including its omission, such that the financial statements are materially misstated the auditor cannot form a so-called clean opinion, whereas if the auditor considers the impact of a misstatement to be immaterial a clean opinion can be expressed. Understanding the difference between material and immaterial in this context is likely to be a challenging part of the expectations gap.

We believe that a key issue with the expectation gap is around education of external users/stakeholders to have an appropriate understanding of audit and assurance engagements (the "knowledge gap").

New York State Society of CPAs (NYSSCPA)

The material extracted from an Association of Chartered Certified Accountants (ACCA) publication and included in the Discussion Paper on page 11 succinctly identifies the components of the expectation gap, currently identified as relating to fraud and going concern, as the knowledge gap, performance gap, and evolution gap. Each component significantly contributes to the expectation gap, with each component being interdependent of the other. With that said, the core of the issue lies in the public's perception of the audit, the auditors, and the auditing standards. This perception is skewed by the idea that all audits are performed in the same prescribed manner, following the same "rule book." The public may not fully understand the goal of the audit and the meaning of "reasonable assurance," and the gap widens as advances in technology enable more transactions to be looked at and more procedures to be performed. This technological expansion is (perhaps mistakenly) perceived to increase the auditor's ability to identify fraud and going concern issues.

Pan African Federation of Accountants (PAFA)

The three components (knowledge, performance and evolution gaps) detailed in the Discussion Paper aptly describe contributors to the audit expectation gap with a greater emphasis towards the knowledge gap.

REA Auditores - Consejo General de Economistas (REA)

We understand that the main cause of the expectations gap is due to the difference between what the general public thinks that the auditors do and what the auditors actually do, which implies that the users of the audit report can misinterpreting the role of auditors or confusing their professional activity. And we believe that this is due, fundamentally, to the lack of knowledge of a good part of the users of the audit reports of what is the objective of the audit of accounts of financial statements and the requirements of the technical auditing standards (NIA).

Although the DP mentions three components of the "Audit expectation gap", according to an ACCA publication of May 2019, we consider that the expectation gap, in general terms, is the difference between what users expect from the auditor of audit accounts of financial statements, and the reality of what an audit is defined in its regulations.

The Institute for the Accountancy Profession in Sweden (FAR)

We think that the description of the expectation gap in three components: the knowledge gap, the performance gap and the evolution gap is relevant to explain the expectation gap. Concerning fraud and going concern we believe that there primarily is a knowledge gap. There is a lack of common understanding that the responsibility for identifying and providing users with information and disclosures related to fraud and going concern begins first and foremost with the management and those charged with governance. However, we also believe that there is a difference between what auditors do and what the public thinks auditors do.

Union of Chambers of Certified Public Accountants of Turkey (TURMOB)

Lack of sufficient understanding of the scope and purpose of an audit of financial statements, and the extent of responsibilities of the auditor regarding fraud and going concern while conducting an audit and issuing an auditors' opinion.

Wirtschaftspruferkammer (WPK)

Whereas the public image of the professionals seems to be one of well-paid, well-trained specialists with comprehensive expertise in various economic and business-related disciplines (e.g. tax, financial reporting, controlling, valuation services, forensic). This image may be reinforced by financial news in the media and self-presentation of the firms (image brochures, recruiting conventions, social media). In case of large corporate failures, like Wirecard, the media coverage swiftly reports about alleged duties and failures of the auditor and others even though legal investigations are still ongoing, thereby creating a potentially distorted picture of the role, responsibilities and capabilities of the parties involved.

Considering the evolution gap expectations in the digital expectations might be that technologies enable the auditor to perform 100% audits, resulting in absolute assurance auditor's reports.

We see the main cause of the expectation gap in the general public's misunderstanding of the role and the legal task of the auditor, including the inherent limitations of the audit ("knowledge gap"). The informational value of the auditor's opinion is accordingly overestimated and falsely rather considered as a guarantee for flawlessness of the financial statements and future viability of the audited company by a trustworthy, external party.

The number of professionals conducting statutory audits is small, at least in Germany, and regarding the audit of financial statements they operate rather unobserved by the public due to the trusting relationship with its clients and discretion obligations. The audit itself is conducted on the basis of a comprehensive set of rules (laws and statutes, standards, codes) containing complex requirements and concepts that are hard to understand for people outside the profession. These include amongst others concepts like reasonable assurance, materiality with all its different forms, or the elaborated allocation of responsibilities between auditor and management with regard to the going concern ability of the audited company. Knowledge of and interest in the conduct of a financial statement audit of the general public is accordingly limited.

7. Investors and Analysts

Corporate Reporting Users Forum (CRUF)

We think that the expectation gap is primarily derived from the knowledge gap which is the difference between what users think is expected of the auditor and the actual role and authority of auditors.

For example, it was challenging for users to grasp the concept and impact on audit practice of the recent fundamental revisions to the conceptual ISAs such as ISA540, ISA315, IAS 220 and ISA 600 and ISQMs. We hope that users of financial statements will be provided with a comprehensive and easy-to-understand explanation of these new standards in tandem with local auditing standard setters to help narrow the knowledge gap.

Also, as is the case with IFRSs, translation into languages other than English will facilitate non-English-speaking users' participation in the discussion during the development of standards. While there may be resource constraints, we would like the IAASB to cooperate with local auditing standard setters to achieve this.

The knowledge gap could also be derived from differences in the perspectives of users, such as investors and analysts, and auditors. Investors and analysts place importance on information that affects stock prices and ratings, but auditors place the highest priority on whether financial statements are free from material misstatements. It is possible therefore that auditors are not familiar with the information that investors and analysts place importance on, such as the future prospects of the company's products and services, industry trends, and the economic and market environment, or auditors might have a different view on the company and industry than users. We would expect auditors to proactively gather information on the audited company and its industry, including points and perspectives that investors and analysts place importance on.

Key Audit Matters (KAMs), plus the addition of Critical Audit Matters (CAMs) in the USA, may include the auditor's explanation with respect to the company's system for preventing frauds which may lead to material misstatements. We expect the IAASB to analyze such descriptions to a wider extent in cooperation with local accounting bodies.

We believe also that the expectation gap arises from the performance gap, where the performance of an audit is not up to a high enough quality. Regarding the performance gap, the CRUF would like the IAASB to continue its efforts to clarify the ambiguity of the standards as the discussion paper mentioned. We also expect the IAASB to encourage countries to take appropriate actions including enactment of laws and regulations in alliance with IOSCO and/or ICGN for tight deadline issues. We expect auditing firms to improve their governance through ISQM1 implementation to reduce concerns that auditing firms might not develop clear guidelines and procedures regarding audit quality. We are concerned about whether accountants effectively execute professional skepticism in the current audit environment. Any fraud could affect a company's financial statements through negative impacts from fines, damage claims and impairment of reputation. Auditors are expected to confront the risk of fraud with this in mind. Some CRUF UK Members indicate that an example of removing ambiguity from standards may be seen in the proposed revisions to ISA (UK) 240 and their consultation on this by the Financial Reporting Council in the UK.

We agree with the discussion paper that there is insufficient provision of information from auditors to shareholders on their procedures performed and outcomes. We recognize that the IAASB has expanded initiatives for auditors' disclosure, such as transparency reports of audit firms, however we would like such efforts to be accelerated. As discussions during the development of ISQM1 did not always go positively in this area, we expect the IAASB to be more proactive in addressing this. One way to do this is to ensure that audit standards' changes and developments are consumer rather than producer led with the IAASB listening more to what the users of audits and audited financial statements are looking for.

During an audit, auditors should understand the actual state of the company's governance, including whether those charged with governance are independent from management (in mind, as well as in appearance, possess necessary knowledge, skill and authority, and align with internal audit functions), and are committed to their duty. Auditors should know who is the right contact of those charged with governance, its subordinates and others within the company who are responsible for dealing with allegations of fraud raised by employees or other parties, in case management is reluctant to identify and respond to fraud. In addition, we expect auditors to assist management and those charged with governance to regularly reinforce their knowledge of GAAP and GAAS. Furthermore, auditors should understand the company's culture well. If similar, even insignificant frauds occur repeatedly or with the involvement of management, it indicates a company culture that creates or overlooks frauds leading to material misstatements. Auditors should request companies to identify the root cause of the frauds and remedy internal control weaknesses and assist companies in cultivating a culture that does not permit any frauds.

Auditing standards should focus more on reliance of audits on internal financial controls and how these may indicate the possibility of material misstatements in financial statements arising from fraud.

<u>8. Academics</u>

Auditing Standards Committee of the Auditing Section of the American Accounting Association (ASC)

A recent review of the expectation gap literature by Quick (2020) suggests that a primary cause of the expectation gap likely results from differences in understanding auditors' responsibilities. In their review of the academic literature related to the auditor's report, Church, Davis, and McCracken (2008, 81) reached a similar conclusion, that although communications to financial statement users have been enhanced over time, "users do not appear to fully understand the auditor's responsibility, the extent of work performed in an audit, and the level of assurance provided by the auditor's report."

Research highlights the value placed on management's representations relating to going concern and the auditor's opinion on those representations. With a few exceptions, research generally shows that auditor reporting on going concern uncertainty provides useful information (see Carson, Fargher, Geiger, Lennox, Raghunandan, and Wilkens (2013) and Geiger, Gold, and Wallage (2019) for reviews of the literature and Czerney, Schmidt, and Thompson (2019), Bédard, Brousseau, and Vanstraelen (2019), and Gutierrez, Krupa, Minutti-Meza, and Vulcheva (2020) for recent studies). It is, however, difficult to disentangle the unique contribution of an auditor's reporting on going concern uncertainties versus other information reported at the same time. In this regard, Myers, Shipman, Swanquist, and Whited (2018) find that the unique information content associated with auditor reporting on going concern uncertainty may not be as pronounced as previously thought. This does not discount the importance of the auditor reporting on going concern uncertainties, as independent assurance helps drive the quality of accounting information (see DeFond and Zhang (2014) for a review). Rather, this highlights the importance of all stakeholders in the financial reporting ecosystem, as noted in the Discussion Paper.

Criticism is often levelled at auditors when entities fail (often spectacularly), in that there is a perception that auditors should have forewarned market participants of the impending collapse. Unease around the issue of going concern focuses on circumstances where there is uncertainty as to the entity's continued viability. While the interest in instances when auditors report on going concern uncertainty and the client remains viable (referred to in the literature as a Type I error) and when auditors do not report on going concern uncertainty and the client subsequently fails (referred to in the literature as a Type II error) is understandable, this should not be the benchmark against which auditor performance is evaluated, nor a reason in itself to modify auditor requirements. Although the auditor's reporting on going concern uncertainty may be perceived as a salient and simple shortcut when predicting failure, current requirements in International Standards on Auditing do not conceive of auditor reporting on going concern uncertainty as serving this purpose. Rather, as explained in ISA 570 (IAASB 2015a, para. 6), the auditor's responsibilities extend to concluding on the appropriateness of management's use of the going concern basis of accounting and whether a material uncertainty exists about the entity's ability to continue as a going concern. ISA 570 paragraph 18 explains a material uncertainty in terms of the impact and likelihood of events or conditions that may cast doubt on the ability of the entity to continue as a going concern. Even if the events or conditions identified eventuate, the standard does not envisage that failure necessarily follows. Improved auditor performance in reporting on going concern uncertainty, therefore, centers on the auditor's ability to identity the events or conditions that may be associated with the entity's ability to continue as a going concern, and to evaluate the likelihood and impact for the entity's future viability. Below we note, with reference to the extant literature, opportunities for the IAASB to help auditors in this regard.

A considerable amount of the research we draw on in our submission was undertaken at a time when explanatory language relating to going concern uncertainties was reported in 'Emphasis of Matter' paragraphs, rather than, as is presently the case, in a dedicated 'Material Uncertainty Related to Going Concern' section or a Key Audit Matter. Also, much of the extant literature is often situated in a U.S. setting in which there are nuanced differences from the requirements of the International Standards on Auditing (e.g., significant doubt vs. substantial doubt). We believe that the views we express are not dependent on the time the research was undertaken nor the jurisdiction within which the research was situated.

In advance of addressing the specific questions, we note that going-concern disclosures are the domain of accounting standard setters, and that International Standards on Auditing should be framework neutral and should not extend requirements beyond those which are expected of management in the accounting standards. We encourage the IAASB to work closely with the IASB on this project. We note above the role of auditing in improving the quality of accounting information (see DeFond and Zhang 2014), but is assurance improving the quality of the right / best information? This is a question for the IASB, and we do not comment further on matters that are within the remit of the IASB, except when they are also within the purview of the IAASB.

Several studies examine perceptions of different stakeholder groups and highlight persistent differences in what the various stakeholders think auditors do and what auditors actually do (i.e., the knowledge gap). These studies focus on fraud-related responsibilities, perhaps because the expectation gap is widest on that aspect of the auditor's work. For example, Baron, Johnson, Searfoss, and Smith (1977) find that non-auditors perceive higher auditor responsibility for detecting and disclosing corporate irregularities and illegal acts than auditors perceive. Similarly, Lowe (1994) and Frank, Lowe, and Smith (2001) find significant perceptual differences between auditors and judges/jurors, particularly in relation to the auditor's role in fraud detection. Epstein and Geiger (1994) noted 71 percent of investors wanted absolute assurance that financial statements are free of material misstatements due to fraud, which is also similar to findings of McEnroe and Martens (2001) who compare expectations of audit partners to investors.

As noted in Quick's (2020) recent review of the expectation gap literature, recent studies suggest that these differences in perceptions still persist between different stakeholder groups across many countries. For example, studies have been conducted in China (Lin and Chen 2004), Barbados (Alleyne and Howard 2005), Egypt (Dixon, Woodhead, and Sohliman 2006), Australia (Schelluch and Gay 2006), Lebanon (Sidani 2007), Saudi Arabia (Haniffa and Hudaib 2007), Netherlands (Hassink, Bollen, Meuwissen, and De Vries 2009; Litjens, van Buuren, and Vergoossen 2015), Bangladesh (Siddiqui, Nasreen, and Choudhury-Lema 2009), Iran (Noghondari and Foong 2013), UK/New Zealand (Porter, Ó hÓgartaigh, and Baskerville 2012), Germany (Ruhnke and Schmidt 2014), and the USA (DiGabriele 2016), with the majority of these studies noting specific differences in how various stakeholders view the auditor's role in detecting fraud.

While much of the research examines the auditor's role in detecting fraud, there are also differences in perceptions as to going concern. Campbell and Mutchler (1988) find that lending officers believe auditors issue a going concern opinion because it is their duty to provide a signal of financial distress to financial statement users, while auditors issue a going concern opinion because they believe there is risk that assets will not be recoverable. A similarly disparate understanding of financial statement audits was reported by Frank et al. (2001), who find that jurors perceive auditors' role as a public watchdog (in addition to expecting auditors to search for the smallest of frauds as noted above).

Other research compares perceptions of auditors and investors related to terminology in the audit report and on auditors' responsibilities involving various dimensions of the attest function including going concern and fraud. McEnroe and Martens (2001, 356) conclude that investors do "not want auditors to issue an unqualified opinion unless: every item of importance to investors and creditors has been reported or disclosed, auditors have been 'public watchdogs,' the internal controls are effective, the financial statements are free of misstatements resulting from management fraud, the financial statements are free of misstatements intended to hide employee fraud, and the firm has not engaged in illegal operations."

Gray, Turner, Coram and Mock (2011, 661) conduct focus groups research with "financial statement preparers (CFOs), users (bankers, analysts, and non-professional investors), and external auditors." They find that those in the "users" group frequently misinterpret common terms that are included in the audit report, such as reasonable assurance, materiality, and sampling. In addition, they report that non-professional investors indicated that they use secondary sources for financial data and do not search for the auditor's report, suggesting that attempts to address the knowledge gap via enhanced communications in the auditor's report may not be effective. However, a more recent study by Kachelmeier, Rimkus, Schmidt, and Valentine (2020) examines critical audit matter disclosures and finds that such disclosures prompted participants (MBA students, financial analysts, and lawyers) to recognize measurement uncertainty and lower their assessments of auditor responsibility for subsequent misstatements related to the critical audit matter. These findings suggest that key audit matters in the updated auditor's report might be able to reduce the expectation gap by lowering users' perceptions of audit assurance and auditors' responsibilities.

It is interesting to note that findings reported in the above studies echo observations by the Commission on Auditors' Responsibilities from the 1970s (see the Cohen Commission 1978). That Commission found that "many users appeared to misunderstand the nature of the attest function, especially in the context of an unqualified opinion. For example, some users believed that an unqualified opinion means that the entity is financially sound. Others felt that the auditor should not only provide an audit opinion, but also interpret the financial statements in such a manner that the user could evaluate whether to invest in the entity" (McEnroe and Martens 2001, 347).

Some of the more notable conclusions reached by Quick (2020) were that the expectation gap differed between countries; stakeholders had widely varying expectations about what the audit should achieve; and that two of the most promising avenues for reducing the expectations gap are education of stakeholders and revised reporting standards like the expanded reporting via key audit matters (KAMs).

Q1a-2.4 - Performance Gap

<u>6. Professional Accountancy and Other Professional Organizations</u>

Accountancy Europe (AE)

Going Concern

Causes of the expectation gap

We believe that there is a specific expectation gap linked to going concern about where to put the cursor in case of a 'close call' when it is not straightforward whether management's mitigating plans will be sufficient, but on balance, after much work during the audit, it is concluded they are just about sufficient. Another reason for the expectation gap is the different interpretations of going concern and material uncertainty concepts, since accounting frameworks do not always define these in the same way. The difference between corporate governance requirements in various jurisdictions may also create different expectations for international investors.

It is also important to emphasise the two different purposes in making the going concern assessment. The first is about concluding whether the going concern basis of accounting is appropriate for the financial statements in accordance with the period defined in the accounting framework (i.e. prevention aspect). The second is about providing information to stakeholders about the economic and financial viability of the entity, as well as potentially its resilience (i.e., transparency aspect). Although there is an overlap, the auditor's role would be different for each of these purposes. The fact that both are referred to by the same words “going concern” is significant in creating the expectation gap.

Institute of Singapore Chartered Accountants (ISCA)

Choice of Audit Strategy

The alignment of choice of audit strategy to audit quality is another important component towards achieving high audit quality.

The ISAs generally provide flexibility in the choice of audit strategy. For instance, paragraph A4 of ISA 330 The Auditor’s Responses to Assessed Risks allows the auditor to determine that only substantive procedures are performed (fully substantive strategy) if the auditor finds testing of controls to be inefficient and therefore does not intend to rely on the operating effectiveness of controls. We note that the above allows the auditor to adopt an audit strategy based on efficiency, which may not always equate with audit quality. While we understand that the intention behind the flexibility may be to allow for scalability and application of the auditor’s judgment, we notice that it may potentially lead to audit teams determining audit strategy based on factors such as resources, fees or time pressure, instead of audit quality.

Audit quality should be a key determination factor when the auditor decides on the audit strategy. A fully substantive strategy would not be able to highlight any lapses in key internal controls over financial reporting. Where there are such lapses, the risk of fraud in the financial statements would increase.

With efficiency in mind, audit teams might be inclined to adopt a fully substantive strategy. However, there may be situations where substantive procedures may not by themselves provide sufficient appropriate audit evidence, such as when checking the completeness of revenue.

In this regard, tests of controls may be more effective as the auditor might be able to identify lapses in key internal controls over financial reporting which might have led to fictitious or fraudulent transactions.

Firm culture

We agree with the DP that firm culture is a key component of audit quality and a lack of clear firm policies and procedures with regard to audit quality is a cause for poor audit quality. While standards can endeavour to influence mindset and behaviour, firm culture plays a critical role in driving behaviour that impact audit quality.

Lack of professional skepticism/professional judgment

Professional skepticism, which is critical to audit quality, is defined in the ISAs as an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence.

Professional judgment, on the other hand, is defined as the application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement.

We are concerned with audits that are performed using a “checklist” approach, which potentially reduces professional skepticism and professional judgment. This is consistent with the findings reported in the UK Financial Reporting Council’s Annual Enforcement Review (2020), that an overwhelming majority of cases of audit failures have involved a failure by the auditors to exercise professional skepticism when assessing the decisions and judgments made by management.

One of the reasons for the lack of professional skepticism is an insufficient focus on the importance of understanding the audited entity and its environment. When such understanding is lacking, auditors would not have the right frame of mind to exercise professional skepticism or professional judgment.

Understanding the entity and its environment is a critical process, especially in this day and age where transactions and business models of companies are becoming increasingly complex. If this process is not performed in a robust manner, auditors would not have an appreciation of the business rationale behind transactions made that would help them pick up irregularities.

Inter-American Accounting Association (IAA).pdf

We also believe that another of the main causes of the Expectation gap related to fraud and going concern in an audit of financial statements is based on the diversity of entities that are subject to audit in different environments from one country to another and in changing situations, in this way it is difficult to raise a common approach since it must be approached in a flexible way completely made and designed tailored to the needs of each entity and in the c ontext of the country in which it is carried out.

Q1a-2.5 - Other Cause

<u>4. Accounting Firms</u>

CohnReznick (CR)

We believe a number of factors contribute to the expectation gap relating to fraud and going concern. Some of this expectation gap is perpetuated by litigators and regulators looking to assign blame for a perceived shortcoming, such as a high-profile restatement.

<u>5. Public Sector Organizations</u>

Office of the Auditor General of Canada (OAGC)

While it is difficult to identify one single cause, broadly speaking the main cause of the current expectation gap relating to fraud and going concern in an audit of financial statements is likely sourced from the ease of access to markets by investors and the scope and pace of information impacting financial market valuations. While market valuations and traditional financial reporting include in their scope fraud and going concern impacts, the information used in each is not identical in terms of timing and scope, and impacts to market valuations may be inconsistent with accounting presentation and disclosure judgments. Traditional audits, performed at regular intervals, as at a point in time, have at best an indirect link to today's fast paced market valuations – yet their presence is seen as more directly linked. More investor/user awareness of audit limitations/scope may be needed.

<u>9. Individuals and Others</u>

Constantine Cotsilinis (CC)

Going concern

I believe the expectation gap relating to going concern relates primarily to time – for how long will the enterprise be a going concern? I have read many financial statements which contain very detailed descriptions of the matters considered when management has assessed going concern. However, nowhere do they mention "for how long".

It is generally accepted that when discussing going concern, we are talking about at least the following 12 months. 12 months from the end of the reporting period or twelve months from the date of the directors' report and the approval of the financial statements. Or it can be more than twelve months if the matters considered will not reach conclusion in the next twelve months.

Why don't we state clearly to what time period we are referring?

Dmitrii Timofeev (DT)

The perceived gap between auditor's responsibilities and financial information user's expectations is a classic principal-agent problem. Auditors profit from their services and consequently incentivized to preserve client-oriented relations with an auditee. Users may disagree with the financial reporting but that knowledge usually remains private and there is no formal way to provide relevant feedback and to pressure the auditors and organizations. Here are some real-life examples.

According to a decision by the government, ownership of a state-owned enterprise (SOE-1) was transferred to another holding SOE. The following year SOE-1 restored some of the previous write-downs of inventories leading to the increase in profit. Both SOEs reported the new management's success, as SOE-1 turned "operating profitable". Company restored inventory write-downs the next year with the same magnitude. It looks very like to a deliberate shift of the profits between years. Write-downs and reversals were hidden in the cost of the sales line in the income statement of the SOE-1.

The government pursues a policy of 50% dividend payout of profit for all SOEs. One electric power generating SOE routinely impairs value of newly installed capacities referring to non-economic tariffs on heat and electricity. Impairments decrease profits and, consequently, the dividends. For the purpose of fair value estimation of cash generating units company applied an unjustifiably high pre-tax discount rate of 15 - 17% (inflation target in the country is 4%, profit tax rate is 20%). At the same time, comparable SOEs with regulated tariffs apply 10-11% pre-tax rate. Significant impairment expenses were included in one number together with costs of sales in the Income statement.

One socially significant enterprise reported "assets for sale" combined in single big lump line in the Balance sheet supposedly for concealing a significant part of its cash. The assets for sales were impaired using a very high discount rate, and the corresponding costs were aggregated in the costs of sales in the Income statement. Finally, the enterprise applied for the government support justifying the claim with its overstated net debt and understated profits.

In all cases, relevant material information was buried in footnotes, and auditors were silent on the ways of calculation and presentation. As the government employs IFRS in the dividends' policy and for distribution of subsidies, for setting key performance indicators and management remuneration, one can find incentives to game the figures. Auditors have to safeguard fair representation, respecting materiality principle, and express opinion on doubtful revaluations. All discretionary accounting decisions (tangible and intangible asset write-downs, reserve creations, etc.) have to be scrutinized by the auditor. The presentation has to be strictly according to materiality principle. I believe it is more important than going concern and outright fraud issues. Going concern is a credit analysis, and appears to be the responsibility of investors and creditors. Fraudsters sometimes will find a way to defraud, and the auditors may be deceived.

This highlights a need for establishment of a feedback mechanism to fill the gap between user's expectations and the auditors work. This has to be an institutionalized and public way for the users to complain with subsequent assessment of the audit quality, be it some "court" or peer-auditors review.

The Unlimited (TU)

The expectation gap generally explains the difference between what the public expects of auditors and what the responsibilities of auditors are in terms of the International Standards on Auditing (ISAs).

However, it must first be determined whether auditors are performing audits in terms of the ISAs or not.

1. Professional skepticism

The ISAs require the application of professional skepticism. Professionnal skepticism is defined in the IRBA professional skepticism guide as "An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of evidence."

The extent to which audit firms currently do not have robust processes to document the questions asked, the conditions that they were alerted of as well as a critical assessment of evidence needs to be assessed. Audit firms have been known to

generally complacent and accepting of information provided by the client, often with pressing deadlines that leaves little time for questioning. Audits are also notorious for "ticking up" being the act of mindlessly quickly checking supporting documents in order to complete audit procedures and mark working papers as complete. Again, due to time constraints.

This creates a huge gap between the auditor and their responsibilities.

2. Nature of audit evidence

In terms of ISA 500, audit evidence should be obtained by third parties wherever possible.

An example of where this is not applied is in the audit of Revenue. A financial statement caption that has an inherent significant risk of fraud, is audited primarily by agreeing line items in the general ledger to invoices. A source of evidence that is generated by the auditee and due technology it is the invoice that generates when the general ledger item is captured and therefore provides no evidence of the existence of that revenue.

Herein lies another gap between the audit and the auditor's responsibilities.

3. The decline of audit quality

The media is bombarded with articles of fines being imposed on audit firms in the UK and South Africa for failing to comply with the audit standards. While these fines on its own indicates that audits are not being performed to the relevant standards, it also highlights that there is a gap between the standards and the auditors responsibilities. If the auditor is not fulfilling their responsibility, there will definitely be an expectation of the public to the profession.

4. Audit opinion

The unqualified audit opinion provides the users of the financial statements with "reasonable assurance that the financial statements are free from material error whether due to fraud or error".

When fraud does occur, auditors quickly turn around and say that it is not their responsibility to detect fraud.

However it is the responsibility of the auditor to ensure that the audit is planned and performed to obtain reasonable assurance that the financial

statements are free from material misstatement whether caused by fraud or error.

These instances highlight the need to consider whether, if the auditing standards were adhered to, would there be as big of an expectation gap as there is?

Q1a-2.6 - Disagree That There is an Expectation Gap

<u>3. National Audit Standard Setters</u>

Japanese Institute of Certified Public Accountants (JICPA)

We are aware of cases overseas where the entities went bankrupt in the accounting period immediately after the audit report was issued without any reference to going concern, triggering discussions as to whether the audit was properly conducted.

On the other hand, we are not aware of any significant issues in Japan that require consideration regarding audit procedures of a going concern.

First of all, for Japanese entities that publish annual securities reports (listed entities, etc.), if events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern are identified but there is no material uncertainty related to them, it is required by laws and regulations (Cabinet Office Ordinance on Disclosure of Corporate Affairs, etc.) for the entity to disclose the information in its annual report outside of financial statements as business risks. In addition, when management is aware of material uncertainties, the entity shall disclose those uncertainties in its financial statements. In either case, it is required respectively by the Financial Instruments and Exchange Act for the entities to properly disclose the information and for the auditors to perform appropriate procedures on the disclosure. With regard to auditor reporting, the Japanese Auditing Standards have been revised in response to IAASB's New and Revised Auditor Reporting Standards issued in 2015. In addition, Auditing Standards Committee Research Report No. 6, "Q&A in regard to Audit Reports," which is a guidance document issued by the JICPA in 2019, explains the details of considerations required for the auditors in light of the above-mentioned Japanese disclosure system. Furthermore, in Japan, the preparation of quarterly financial statements and a quarterly review by auditors of those reports are required for listed entities. Therefore, an entity's ability to continue as a going concern is assessed by management and examined by auditors every three months, and the information is disclosed in a timely manner when a new event occurs.

In addition, as described in the Discussion Paper, many of the going concern issues should primarily be addressed by the financial reporting framework.

As such, currently we are not aware of any significant expectation gap with respect to going concern or the need to enhance requirements. Although there is a possibility that an entity might suddenly go bankrupt when fraud is discovered, we believe that this should be considered as a response to fraud rather than going concern.

<u>6. Professional Accountancy and Other Professional Organizations</u>

PIRC

The central premise of this consultation is incorrect because there is no 'expectation gap' under the law of many countries including the UK and other jurisdictions. In the UK, both the Judiciary and Parliament are clear on this.

Disappointingly, this IFAC-IAASB consultation spreads misinformation. We request that it is withdrawn by 21 February 2021, and we will also be asking accounting firms in the UK and the Financial Reporting Council to repudiate it.

The Business, Energy and Industrial Strategy Committee of the UK Parliament ('The Parliamentary Committee') determined that there was not an expectation gap under UK law. We are copying this to the UK Parliament and other parties.

The legal position is that fraud may cause a company (and a group of companies) not to be a going concern and the auditors can be responsible for it if they have missed it.

The Parliamentary Committee described the evidence of the largest accounting firms given to it as "blatant" and concluded that the problem was not the public's expectation of auditors being wrong, the problem was a 'delivery gap' by the auditors, The Committee concluded:-

"We were both surprised and disappointed to hear the view from audit firms that because fraud is difficult to detect, the public should not expect auditors to find it. The most blatant example came from Grant Thornton's CEO, David Dunckley:

"We are not looking for fraud. We are not looking at the future. We are not giving a statement that the accounts are correct. We are saying they are reasonable. We are looking in the past and we are not set up to look for fraud."

"We do not accept the attempts of auditors—particularly the Big Four and Grant Thornton—to underplay the role or scope of audit, nor to implicitly blame the public for failing to understand the purpose of audit. Rather, the firms should focus on the poor quality of their audits, and on how they are falling short of what audits are for within the current framework."

A High Court case settled in the middle of the hearing, Asset Co vs Grant Thornton, which involved a fraud. Not only was Grant Thornton held to be accountable for the illegal dividends, as a result of missing the fraud which led to the company not being a going concern (it had failed the capital maintenance requirements of the Companies Act) but Grant Thornton was also accountable for the misinvestment that this had caused the company to undertake.

We therefore had the "Alice in Wonderland" situation where:-

Grant Thornton admitted in court what the profession to Parliament, and this consultation, denies. Paragraph 2 of the Appeal Court decision states:-

"GT admitted that it had in important respects carried out the audits in breach of its duty of care and that it had failed in its duty to identify management fraud, particularly dishonest representations and evidence provided to it by senior management in the course of the audits."

Grant Thornton told Parliament the opposite:-

"We are not looking for fraud. We are not looking at the future. We are not giving a statement that the accounts are correct. We are saying they are reasonable. We are looking in the past and we are not set up to look for fraud.

The consultation cites the position of the Certified Public Accountants of the USA. The USA itself has a framework of law and governance such that there may be different positions from US courts depending on the interaction of duties in state law and federal law. Indeed the legal responsibilities in the UK (and jurisdictions with similar law) exceed what most people would envisage given the consistent message from the auditors misleading people.

We needed to go no further than the introductory letter from the IAASB's Chair, to see the strategy at play here.

The IFAC-IAASB is attempting to initiate a debate on the false premise that there is an expectation gap and that the

auditor's role needs to be expanded. Under the guise of offering an 'upgrade' the consultation is tilted towards a downgrade.

Mr Seidenstein's - the IFAC-IAASB Chair – introduction states [our underlines].

"Our specific focus is on the auditor's responsibilities and whether they should be expanded with regard to these topics in the context of an audit of financial statements. We will also consider whether such enhanced responsibilities are needed in all audits, or only in some circumstances. Our efforts will necessarily require us to work with others in the financial reporting ecosystem, because the effectiveness of any potential changes may depend partly on the actions of other stakeholders.

The suggestion too that parties other than auditors have a role is a buck pass. Mr Seidenstein's introduction also states:-

"Companies, those charged with their governance, investors, regulators, and others have an important role in improving external reporting in relation to fraud and going concern. The respective responsibilities of the various stakeholders support and reinforce one another."

Problems with false assertions about an 'expectations gap' also flow through to the accounting standards regime, as some accounting treatments under IFRS are also inconsistent with the going concern position.

The overstatement of assets and understatement of liabilities permitted and required by the IFRS system, may in fact achieve similar outcomes to fraud and false accounting, by masking whether a company or group of companies is a going concern or not.

The situation is so serious that PIRC is minded to recommend that shareholders vote against any accounting firm that does not publicly repudiate the assertions in this document by 28 February 2021, as audits conducted on that basis would be in breach of duties and contract.

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Q1a-2.7 - No Comment

<u>1. Monitoring Group</u>

International Association of Insurance Supervisors (IAIS)

International Forum of Independent Audit Regulators (IFIAR)

<u>2. Regulators and Audit Oversight Authorities</u>

Canadian Public Accountability Board (CPAB)

<u>4. Accounting Firms</u>

SRA

The note on page 11 of the Discussion Paper states, that situations where auditors fail to do what standards or regulations require are not discussed in the Paper. Also referring to the remark, made above, under point 2, regarding the lack of analysis in the Paper, we feel that these situations might be an important cause of failures and scandals also in the non-public interest segment of the audit market. We therefore do not understand the exclusion of these situations in the Paper, as these situations might require other measures, than those suggested in the Paper.

<u>6. Professional Accountancy and Other Professional Organizations</u>

Belgian Institute of Registered Auditors (IBR-IRE)

Belgian National Chapter of Transparency International (BNCTI)

Confederation of Indian Industry (CII)

The discussion paper has a robust analysis of the expectation gap and the ACCA has appropriately classified causes into - knowledge, performance and evolution. There is clearly an increasing expectation amongst stakeholders for a higher level of assurance on the absence of material misstatement due to fraud than has been historically provided and accepted. Rapid developments in technology and availability of significant data and external evidence enable auditors to better meet those expectations.

In many corporate failures, fraud has led to concealment of factors that may lead to challenge of the 'going concern' assumption. In our view, this does not reflect on adequacy of the auditing standard on going concern but more on the audit procedures addressing the risk of fraud.

European Audit Committee Leadership Network (EACLN)

Tapestry Networks

Institute of Chartered Accountants in England and Wales (ICAEW)

Expectation gaps relating to fraud and going concern are long-standing and not straightforward. They are linked because it is not uncommon for the failure of large businesses shortly after an unqualified audit report has been issued to be associated with fraud. Something needs to be done. But we are not convinced that analysing these gaps, or even seeking to address them, is the right starting point. Repeated analyses of expectations gaps over many years have borne little fruit.

Expectation gaps are more a symptom of an underlying problem, which is that more needs to be done by everyone concerned. IAASB's focus should be less on managing expectations, and more on helping all stakeholders, including auditors, enhance their ability to prevent, detect and report fraud, and to challenge management and report more effectively on going concern.

International Air Transport Association (IATA)

<u>9. Individuals and Others</u>

Ahmed Al-Qawasmi (AAQ)

Alvaro Fonseca Vivas (AFV)

Michael Bradbury (MB)