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From: ICPAR
To: IAASB
Subject: **Comment on enhancing the value of auditor reporting: exploring options for change**

Dear Sirs,

We congratulate the IAASB for the great work that is going on to enhance the usefulness of ISAs and in particular the auditor's report. We believe this is a timely initiative and we support it.

We here by submit our comments as below:

Issues Identified

1. Do respondents have any comments about the issues identified in Section II regarding the perceptions of auditor reporting today?

Yes users of corporate financial information point to the existence of a gap between the information they believe is needed to make informed investment and fiduciary decisions, and what is available to them through the entity's audited financial statements or other publicly available information.

For example users are shocked when they read a clean audit report but in less than a year or there about, a major scandal on the said company is reported or discovered. This implies adequate information may not have been disclosed by the auditor's reports. Even with the existence of peer review, the situation hasn't been helped much.

The big issue is whether the future-based comments made by management of the organization in the Annual Report are appropriate and whether their attitude to risk is appropriate. The auditor should understand the underlying financial situation and context of the organization better than most but in the past auditing has focused on the financial statements primarily in a backward looking sense. This has fuelled the expectations gap which is a reality across the globe, especially given the financial crisis.

2. If respondents believe changes in auditor reporting are needed, what are the most critical issues to be addressed to narrow the information gap perceived by users or to improve the communicative value of auditor reporting? Which classes of users are, in the view of

respondents, most affected by these issues? Are there any classes of users that respondents believe are unaffected by these issues?

a) The most critical issues to be addressed are: i) detailed entity information, ii) entity information relevant to the audit, and information about audit scope, process and findings.

The perception is that this kind of information is important to the users however the standard audit report do not disclose it.

b) The classes of users most affected by these issues are large investors and financial analysts in particular.

c) Users perceived to be unaffected are smaller entities and public sector. For smaller entities they may have a narrower range of users that already may be able to obtain additional information about the entity through ongoing interactions with management while for public sector the scope of the audit may include lengthier and more explanatory reports in addition to the standard auditor's report. This means the auditor will have to provide more disclosure than in the case of the standard audit report for companies.

3. Do respondents believe that changes are needed for audits of all types of entities, or only for audits of listed entities?

As per (b) and (c) above mostly changes are needed for listed companies or entities with public accountability.

Clearly there will be an emphasis on listed companies and there is a balance to be struck between cost and benefit of a change in audit approach. But some improvement in many sectors is required, certainly for all those entities required to produce an Annual Report upon which others are required (these could be significant organizations – for example major public sector bodies which are of course not listed or large private companies). Probably less relevant for smaller non-listed entities where you would not want to impose excessive regulation costs.

Further it has been noted that various public entities fail to comply with certain reporting standards (IFRSs) which have material effect on the reported position and performance. There is a need to make clear disclosure of non full compliance with such standards where these have material impact on recognized amounts.

Exploring Options for Change

A. Format and Structure of the Standard Auditor's Report

4. Respondents are asked for their reactions to the options for change regarding the format and structure of the standard auditor's report described in Part A. Do respondents have comments about how the options might be reflected in the standard auditor's report in the way outlined in Appendix 1 of this Consultation Paper?

To some extent the structure and format need to be changed. What is important is the content of the report which seems to be non-communicative or inadequate in disclosing all relevant information to users.

The auditor's opinion should be:

1.Prominent so included in the body of the report

2.Free as far as possible of complex/confusing technical language that non-

auditors/accountants would not understand.

3. It would be helpful to better explain the role of management and auditor respectively for detecting fraud as this still seems to be an area of confusion

4. The auditor should include a disclosure of any material sources of estimation uncertainty as far as risk goes when the entity computes amounts recognized in the financial reports. This statement should be provided even if the entity is deemed to be a going concern and even if this disclosure has been included in the notes as part of the financial report. This disclosure keeps users on alert about possible material shifts in the near future in the status or values of amounts recognized in the report.

5. If the paragraphs in the current standard auditor's report dealing with management and the auditor's responsibilities were removed or re-positioned, might that have the unintended consequence of widening the expectations gap? Do respondents have a view regarding whether the content of these paragraphs should be expanded.

See answer to 4 above. We do not see how removing them would help the issue. If it is currently an area for confusion then how would removing references to it make it better rather than worse?

Removing them might have the impact of increasing user's expectation of the role of auditor, having them included, to some extent draws a line of separation between the role of auditor and role of management. If the content was expanded this could be communicative hence reduce the gap.

B. Other Information in Documents Containing Audited Financial Statements

6. Respondents are asked for their reactions to the possibility that the standard auditor's report could include a statement about the auditor's responsibilities regarding other information in documents containing audited financial statements. Do respondents believe that such a change would be of benefit to users?

It definitely would. An often repeated complaint about the auditor's role is that they did not spot the financial crisis coming or at least did not give any pre-warning to users of financial statements in their reports. The risks that were being assumed by management were all too often not being discussed properly in the Annual Reports and this meant that they were often in-effective in identifying the risks and the problem. Much if not all of this would be revealed in the non-financial statistics element of the report.

The management prepares the financial statements and includes management assertions, Management Discussion and Analysis (MD&A), operating and financial review (OFR) statements. The auditor is expected to express his/her opinion on all management assertions Management Discussion and Analysis (MD&A), operating and financial review (OFR) statements; whether they are in conformity with the accounts and whether they are consistent with the facts/situation on the ground. Hence the auditor has that responsibility.

7. If yes, what form should that statement take? Is it sufficient for the auditor to describe the auditor's responsibilities for other information in documents containing audited financial statements? Should there be an explicit statement as to whether the auditor has anything to report with respect to the other information?

We cannot separate financial statements from other information, much as most of other information may not be auditable for example forecasts by management, they still originate from the financial statement as the basis. Therefore there should be explicit statement for auditor to report.

We think that it is crucial that the role of the auditor is extended to include whether they have anything to report on the non financial statement element of the report. To be honest there is some rather muddle-headed thinking here. You can't split the report into discrete chunks. It forms a package and it is very difficult for users to understand which bits of the report can in the auditors view be relied upon and which cannot. This is one of the problems at the moment and it is feeding the expectations gap.

C. Auditor Commentary on Matters Significant to Users' Understanding of the Audited Financial Statements, or of the Audit

8. Respondents are asked for their views regarding the auditor providing additional information about the audit in the auditor's report on the financial statements.

If the additional information is relevant to users then the auditor should report. i.e if it influences the economic decision of users, by helping them evaluate past, present and future events or confirming, or correcting, their past evaluations.

Therefore these comments on extra information are absolutely critical. In order not to cause any confusion or ambiguity, why not keep the audit opinion as a discrete part of the auditor's report and have the comments on additional information as a separate section within it. Users of accounts are not generally uninformed or naïve; they are just confused by conflicting messages in management reports which are not picked up on by auditors.

9. Respondents are asked for their reactions to the example of use of justification of assessments in France, as a way to provide additional auditor commentary.

Justification of assessments may be more effective communication as it details significant issues that may have influenced the auditor's opinion.

The French example is interesting. If you look at the positives they relate to the usefulness of the statements to users – We would have thought that these should be the dominant feature. If you look at the negatives though I would have two comments. Most of them relate not to weaknesses with the concept but weaknesses in the application. Therefore the area to be improved and addressed is not the conceptual one but the more practical one, that those responsible for doing it are not doing it very well. This means you should address the problem of application..

The other practical point is about auditor liability. Many non auditors think that auditors have it too easy (many auditors don't agree!) in this respect. Our view is that auditors should do their work properly and conscientiously and in compliance with the ISAs they should be signing up to, then that is their best protection against liability claims.

10. Respondents are asked for their reactions to the prospect of the auditor providing insights about the entity or the quality of its financial reporting in the auditor's report.

The auditor as a watchdog of shareholders and other users at large has a responsibility and this responsibility includes providing information and part of this information is insight information. This is a good idea and one that should be adopted. One is tempted to ask, if the auditor is not doing this, who will?

D. An Enhanced Corporate Governance Model: Role of Those Charged with Governance regarding Financial Reporting and the External Audit

11. Respondents are asked for their reactions to the options for change relating to an enhanced model of corporate governance reporting, as described in Section III, Part D.

This change is welcome; there should be enhanced model of corporate governance reporting, the external auditor should as part of his responsibilities comment on the audit committees reasonableness and completeness of their work to the users of financial statements and in the same spirit audit committee reporting should be enhanced to report on external auditors oversight of financial reporting process the shareholders. This means the role of audit committees should not be restricted to reporting to management only.

A more proactive role for audit committees or equivalents in reporting to stakeholders would represent a significant strengthening of the governance structure. This is to be welcomed. It would help to ensure that the audit committee takes its role seriously and educates itself better on its own responsibilities and those also of auditors. This must be a good step and would also increase the confidence of the users of financial statements which again must be good.

We do not agree with the statement in paragraph 86 at all. If there is a lack of confidence in the audit committee or its ability to act in the interests of shareholders then you should address the problem and make it function more effectively and not give an opt-out from using this model. This inhibits true comparability internationally and also introduces the principle that if things are not working effectively then you just opts out. How will this make things better?

12. To the extent that respondents support this model, what challenges may be faced in promoting its acceptance? Also, what actions may be necessary to influence acceptance or adoption of this model, for example, by those responsible for regulating the financial reporting process?

There might be some conflict as shareholders appoints both the auditor and the management, however the audit committees is appointed by management yet on the enhanced model all are expected to report to shareholders. The management may be discontented due to the fact that they are being overshadowed or being undermined. Those responsible for regulating the

financial reporting process should initiate the process of expanding the respective responsibilities of each of the shareholders agents.

Secondly this is essentially a process of education. Regulatory bodies should be part of the consultation process if they are not already (clearly as the FRC in the UK is mentioned in the ED then it presumably is but there should be a global approach to this).

13. Do respondents believe assurance by the auditor on a report issued by those charged with governance would be appropriate?

By nature of their work i.e oversight responsibility on behalf of the shareholders whom the auditors owe the primary duty, this would be appropriate. Simply put the auditor is the person best placed to comment on this.

E. Other Assurance or Related Services on Information Not Within the Current Scope of the Financial Statement Audit

14. Respondents are asked for their reactions to the need for, or potential value of, assurance or related services on the type of information discussed in Section III, Part E.

There can be added value however this can only be possible if the scope of audit work is expanded to go beyond financial statements and internal control procedures by management and include provide assurance on, other types of subject matter that is deemed to be of value to management of the entity as well as external users.

The problem here is that, we suspect if you ask the users of financial statements they will want this extension whereas auditors won't. I feel it is important that this extension is made as it will enhance the credibility of the audit profession which has been damaged reputationally by the global crisis. This may be as much a question of perception (users expect more from auditors than has in reality and legality been required previously) than reality (auditors have been perhaps doing a reasonable job within what has been legally expected of them but users have expected something different = expectation gap) but there is considerably pressure on auditors to provide more and if the audit profession does not respond then greater external regulation and less self regulation may be the end result.

15. What actions are necessary to influence further development of such assurance or related services?

Clearly defined statements of what will be required of the auditor in the future. No ambiguities must remain which would lead to a future expectation gap. Secondly, assessments of costs benefit analysis. Are the owners able to pay for such services much as there is the added value?

Implications of Change and Potential Implementation Challenges

16. Respondents are requested to identify benefits, costs and other implications of change, or potential challenges they believe are associated with the different options explored in Section III.

Benefits will be much greater possibility of user satisfaction and consequent strengthening of credibility of the audit profession. Costs will clearly increase for the auditor and this will not be welcome but there are costs of not implementing these improvements in terms of tighter regulation. We do not agree with the argument mentioned in the French example that this results in increases of risks of liability – if the changes are clearly defined, unambiguous and properly implemented. If these three conditions are met it could actually reduce the risk of liability by removal of the expectations gap.

17. Do respondents believe the benefits, costs, potential challenges and other implications of change, are the same for all types of entity? If not, please explain how they may differ.

Clearly for larger and more complex organizations the costs will be greater. The more complex the organization, the more there is to do and therefore this will drive up costs. However there could be offsetting reductions in terms of claims against auditors if there were a clearer and more holistic view of what is required of auditors.

18. Which, if any, of the options explored in Section III, either individually or in combination, do respondents believe would be most effective in enhancing auditor reporting, keeping in mind benefits, costs, potential challenges, and other implications in each case? In this regard, do respondents believe there are opportunities for collaboration with others that the IAASB should explore, particularly with respect to the options described in Section III, Parts D and E, which envisage changes outside the scope of the existing auditor reporting model and scope of the financial statement audit?

They are all important and part of a package.

(a) Reporting by those charged with governance (or the audit committee) to the entity's shareholders (or other external stakeholders); in conjunction with

(b) Expanded reporting by the independent auditor on the report provided by those charged with governance.

19. Are there other suggestions for change to auditor reporting to narrow the information gap perceived by users or to improve the communicative value of the auditor's report?

We think the widening of scope will address many of the issues. There will undoubtedly be challenges in practical implementation though.

Yours Sincerely,

Ambrose Nzamalu,
Professional Standards Officer
For chief Executive