CONTROLLER AND AUDITOR-GENERAL
New Zealand | Tumuaki o te Mana Arotake

Level 2, 100 Molesworth Street, Thorndon 6011
PO Box 3928, Wellington 6140, New Zealand

Email: john.ryan@oag.parliament.nz
Telephone: +64 4 917 1500

Website: www.oag.parliament.nz www.auditnz.parliament.nz

John Ryan

31 July 2020

International Accounting and Assurance Standards Board
529 5th Avenue
New York
New York 10017
United States of America

Proposed Non-Authoritative Guidance for Extended External Reporting Assurance

Thank you for the opportunity and extra time to comment on the Proposed Non-Authoritative Guidance for Extended External Reporting (EER) Assurance (the Guidance). We commend your effort to provide guidance in a challenging and wide area of reporting that we consider vitally important and evolving. Our interest in the Guidance is in relation to the audit of performance information in accordance with appropriate auditing standards and also in relation to guidance on providing assurance over different forms of EER (excluding performance reporting).

About the Auditor-General

The Auditor-General is responsible for auditing all of New Zealand's public entities. We provide the New Zealand Parliament and the public with independent assurance that public entities are operating and accounting for their performance as intended. Our annual audit work incorporates both financial and non-financial information – we refer to the latter as "performance information".

The Auditor-General has been auditing public sector performance information for more than 25 years. In the New Zealand public sector, many "public benefit entities" are required to report on their performance (what they achieved in non-financial terms) at the same time as their financial statements. This is considered critical for effective public accountability. Both the performance information and financial statements are included in an annual report to the public and are subject to audit, where required. The audit of the performance information is carried out in conjunction with, and at the same time as, the audit of the financial statements, in accordance with the Auditor-General's auditing standards.

Overall comment

Although we acknowledge that the Guidance has been prepared to address a wide-range of EER situations, the assurance of performance information in the public sector requires, in our view, taking an integrated approach to auditing the financial and performance information of an entity. The audit of performance information in the public sector fundamentally involves providing assurance on how public entities have used public money to achieve value for the public.

In New Zealand, the Auditor-General's auditing standards are based on the International Standards on Auditing (ISAs). The Auditor-General has developed a separate standard on the audit of performance information, which is integrated with the Auditor-General's other auditing standards. The standards have been configured in this way to recognise the strong connection that should exist between the audit of historical financial information and the audit of historical performance information.

Because the Guidance is based on ISAE 3000 (Revised) (the Standard), which adopts an approach to assuring EER (including performance information) in isolation and separate from the audit of financial information, we do not consider that the Guidance and Standard can be appropriately applied to the audit of public sector performance information. In a public sector context, performance information covering the activities carried out by the entity and the impact of those activities, is fundamental to public accountability and arguably more important than financial reporting. We recommend that this form of reporting not be included within the scope of the Guidance.

We also observed that there is an emerging trend towards reporting that integrates financial and performance information not only in the public sector, but in other areas as well. We therefore suggest that the International Accounting and Assurance Standards Board (IAASB) anticipate and consider developing standards and guidance that take a more integrated approach.

We also found that the proposed Guidance uses highly technical concepts, such as underlying subject matter, reporting topics, criteria, subject matter information, framework, that are difficult to understand, even for experienced practitioners. We recommend that the IAASB consider using simple and clearer concepts and terminology that professional practitioners can readily apply.

With regard to the Guidance itself, we considered that there were opportunities to improve the overall structure and to provide simpler, clearer, and more concise guidance in several places, which we discuss further in the appendices.

We hope that our comments will be helpful to you. Should you have any questions concerning our submission, please contact either myself or David Eng, Director Performance Reporting (david.eng@oag.parliament.nz).

Nāku noa, nā

John Ryan
Controller and Auditor-General

Appendix 1 – Comments on Significant Matters

1. *Performance reporting of public sector entities*

As noted in our main comments, the assurance of performance information in the public sector requires taking an integrated approach to auditing the financial and performance information of an entity. In a public sector context, performance information covering the activities carried out by the entity and the impact of those activities, is fundamental to public accountability and arguably more important than financial reporting. We recommend that the Guidance recognise this and that the assurance of performance information in the public sector therefore not be included in the scope of the Guidance.

2. *Terminology*

The Guidance and Standard use highly technical concepts that we, as experienced practitioners, found difficult to understand. Throughout the Guidance and associated documents, the concepts, such as underlying subject matter, reporting topics, criteria, subject matter information, framework, are inconsistently defined and used.

It is not clear to us whether the term "criteria" is intended to determine the underlying subject matter, reporting topic or subject matter information, or is intended to determine all of these concepts. In the Standard, "criteria" is defined as "the benchmarks used to measure or evaluate the underlying subject matter" (paragraph 12(c)). However, the Explanatory Memorandum notes that "the base, methods or standard comprising the framework used by the entity to prepare the information in the EER report are known as the "Criteria"" (paragraph 10(a)).

We also note that the Guidance uses the term "framework criteria" for established criteria (for example, see paragraph 8), but then states "The frameworks and criteria used to measure or evaluate the underlying subject matter(s) …" (paragraph 25).

In general, the examples were useful. However some examples (for example, in paragraphs 143 and 221) could more clearly explain how they demonstrate and explain the key concepts.

We recommend that the Guidance:

- use simple, plain language to explain the technical terms in the Standard;
- be reviewed (together with associated documents) to ensure that the key concepts are consistently defined and used;
- only provide definitions of new terminology and avoid repeating definitions of concepts that have already been defined in the Standard;
- clarify whether there are different kinds of criteria and how key concepts (for example, criteria, underlying subject matter, reporting topics) relate and apply to each other, using a clear end-to-end example; and
- avoid using acronyms.

3. *The Importance of Subject Matter Competence and Professional Judgment and Scepticism*

Unlike financial reporting, EER is at a developmental stage and there is no single "generally accepted framework". Providing assurance on this kind of reporting therefore does not lend itself well to a generally accepted approach. EER provides a greater opportunity for management bias and for a preparer to "cherry pick" and show themselves in a good light by not including reporting topics and/or subject matter information that disclose the negative consequences of a preparer's activities. From a practitioner's perspective, it is essential to get the right balance between guarding against management bias while enabling this area of reporting to evolve. Therefore, it is critical that practitioners have high levels of professional scepticism and judgment and access to subject matter competence to establish a set of valid independent expectations

Although the Guidance highlights the importance of these competencies, attributes, and behaviours, we recommend that their importance be strengthened at each stage of the assurance engagement.

We also recommend that the overall Guidance be reviewed and written with practitioners in mind. As discussed further below, the Guidance should be much shorter and concise and rely on simple, clear concepts and principles and focus on important topics.

4. Engagement Acceptance/Continuance

Determining if the necessary pre-conditions are in place before acceptance/continuance is the first key decision to be made. Because there is no generally accepted framework for EER, the risks of inaccurate or unbalanced reporting are significant. The Guidance should be clearer and more assertive on the matters to be considered by the practitioner in making their acceptance/continuance decision.

Before acceptance/continuance, the practitioner should ask these questions:

- Do I know enough about this organisation and the industry in which it operates to be confident I can make a reasonable assessment about factual and balanced EER?
- Do I have the competence (or can I acquire the necessary competence) to carry out the engagement?
- Is the organisation committed to factual and balanced reporting?
- Is the organisation sufficiently equipped to prepare a factual and balanced report?
- Has the preparer adequately identified the purpose of the EER report (paragraphs 230 and 231)?
- Has the preparer appropriately identified the EER report's intended users (paragraphs 232 to 238)?
- If I am not the auditor of the organisation's financial information, do I have unencumbered access to the financial auditor?

A "no" to any of the above questions should lead to an immediate decision to decline the engagement. A decision tree might be useful to illustrate the engagement acceptance/continuance process.

5. Future trends

The frameworks, measures, and information used by public sector entities are continuing to evolve, and public reporting of financial and performance information is becoming less centred on annual reports and are increasingly made available online. If EER, as well as financial information, is increasingly being reported on a continuous basis online, what does this trend mean more generally for how public reporting needs to be assured? How frequently and in what way does continuous public reporting information need to be assured?

Given these trends, we recommend that the Guidance provide clearer information about the provision of assurance of public reporting.

6. Structure

We agree that the Guidance should be structured in terms of the key stages of an EER assurance engagement. To support this kind of structure, we recommend:

- *consolidating the content of Chapters 1 and 2*: The first key stage and decision of the assurance engagement should be to determine if the necessary pre-conditions are in place. However, this stage is not discussed until Chapter 3 and as a result is not sufficiently emphasised. Consolidating Chapters 1 and 2, which would cover the necessary competencies and attributes, would better highlight that the first key stage is determining whether the pre-conditions are in place;

- *re-ordering Chapters 3 to 6:* Chapter 6 covers important content on the purpose of the EER report and the processes to identify the reporting topics and intended users, which we expected to be at the front of the Guidance, rather than the middle. Diagram 8 provided the clearest overview of the assurance engagement. We recommend that the content of Chapter 6 and Diagram 8 be moved forward in the Guidance, followed by Chapters 4 and 5; and

- *re-structuring the discussion on the suitability of criteria*: Chapters 3, 4, and 6 all discuss the suitability of criteria, which results in duplication and confusion. We recommend that this material be more clearly structured in terms of what guidance is needed to make a preliminary assessment during the acceptance phase versus a more comprehensive assessment during the planning phase.

7. Length and readability

We recognise the IAASB's response to previous feedback on the length of the Guidance, with additional contextual and background material, and more comprehensive examples, placed in Supplements A and B. However, we found the Guidance long, and separating the information across three documents made it difficult to navigate.

There are also many paragraphs and sentences that are long and difficult to understand (for example, paragraphs 10, 33, 77, 82, 113, 115, 136). Several chapters include sections that provide extensive guidance on common sense points that detract from a focus on the important information in the Guidance (for example, paragraphs 38-41, the definition of professional judgment, and paragraphs 72, 82).

We recommend that the Guidance be reviewed with a focus on rationalising all of the documents into a single succinct document, with potentially lengthier examples included in an Appendix that are clearly linked to the relevant text in the Guidance.

Appendix 2

Chapters 1 and 2

These Chapters discuss critically important issues, but serve as background to the assurance engagement. We recommend that the content of these Chapters be consolidated and streamlined. The first part of Chapter 1 was generally useful; however, we recommend that the section on *Direction, supervision and review* be reviewed and streamlined.

We also recommend that this part of the Guidance provide stronger emphasis on the importance of the practitioner's "subject matter competence" and professional scepticism and judgment on:

- making their acceptance/continuance decision; and
- developing expectations about the EER, and the suitability of the components that are used by the preparer in constructing the EER.

Chapter 3

Our comments on this chapter are included in our general comments.

Chapter 4

This Chapter covers an important topic but the language is overly technical, complex, and confusing. The term "criteria" is not easily understood, and it is defined and used in different ways throughout this Chapter and the rest of the document.

The Chapter should clarify what "criteria" means and how it applies to other concepts, such as the nature of the assurance report, underlying subject matter, reporting topic, subject matter information, or all of these. This is important as the practitioner needs to assure the information against the "applicable criteria".

The importance of the practitioner developing an independent expectation of the criteria based on subject matter competence should be strengthened to mitigate the risks of a preparer choosing criteria that are applied to the underlying subject matter and/or reporting topics to produce biased subject matter information.

In the discussion on disclosing criteria, it would be clearer to describe this in terms of disclosing the basis, method, or standards for preparing the subject matter information.

In the discussion on "Completeness" (page 92), we suggest rewording the explanation of this term to clarify that the resulting subject matter information needs to be complete and not that the criteria are required to be complete.

Chapter 5

In our experience on auditing this kind of reporting, we see risks in overplaying the importance of internal control in the context of EER and the assumption that providing assurance on internal systems and controls will lead to effective assurance over the EER. This assumption is misplaced because the important information that pertains to EER often lies outside the systems and processes. Our general concern is that an emphasis on the entity's system of internal control is simply a transfer of a financial audit methodology to a different "underlying subject matter" scenario around EER. We recommend that this Chapter follow Chapters 6 and 4.

In the case of third-party reporting, the Guidance notes that the practitioner should consider the source, scope, processes, and controls, but there is no guidance on how to assess and what degree of assurance should be sought in assessing these considerations. We recommend that the Guidance on this be strengthened.

Chapter 6

As noted earlier, a large part of this chapter should appear much earlier in the Guidance. Diagram 8 addresses the significant matter of assessing reporting bias in the EER, arguably, the most significant threat surrounding EER. Diagram 8 also provides an important overview of the assurance engagement. We recommend that this Chapter be moved to the beginning of the Guidance and draw a stronger connection with the other Chapters of the Guidance.

We also recommend reviewing the discussion on criteria in this Chapter as it seems to repeat the discussion in Chapter 4.

The content of Chapter 6 is also very technical (see paragraph 215), and we recommend that it be reviewed and re-written using simpler language.

Chapter 7

We did not have any comments on this Chapter.

Chapter 8

The content of the tables on pages 121-123 should be reviewed and better consolidated and simplified. There are several bullets in certain tables that would belong better in other tables. Relying on third-party information is a prevalent and significant issue. As noted earlier, we recommend that the Guidance provide further information on the extent to which evidence needs to be gathered when relying on third-party information.

The discussion on aggregation risk seems to understate the importance of the practitioner also needing to make a qualitative assessment of individual misstatements. It is generally not possible to add misstatements of different elements of EER reporting together, so a quantitative assessment at an aggregate level is generally not practical.

Chapter 9

This Chapter seemed overly long, often circling back around key points. We recommend that this Chapter be reviewed and made more direct and succinct.

Paragraph 315 discusses an important point about the practitioner needing to consider the fair representation of the EER report even though it contains several misstatements that individually are considered to be immaterial. This point should be emphasised and appear earlier in the Chapter.

Chapter 10

We did not have any comments on this Chapter.

Chapters 11 and 12

These Chapters provided useful and important information, but it might be more useful to incorporate this content into the earlier chapters given the relevance of these topics to each of the preceding Chapters. This might reduce the duplication and length of the overall document and make it more cohesive.