

No choice but to move with the times

Audit profession risks losing its relevance if it fails to embrace the looming changes for the auditor's report

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THE financial statements of most companies in Singapore are audited annually by their auditors who would then opine on whether these statements give a true and fair reflection of the financial health and performance of the companies.

Such opinions are given in the form of an auditor's report. The current format of such reports reveals only the end results of an audit, along with the boilerplate disclosures on the scope of the auditor's work, his responsibility and the management's responsibility, among others.

This format has been in existence for the longest time, with some tweaks made over the years. And for the longest time, the usefulness of such standardised reports has been questioned time and again. It was not until 2011 that standard-setters put their foot down and set the wheels of change in motion – and this time, fast. The auditing profession should know that if it sits back and does nothing, it risks losing its relevance.

The research commissioned by the global standard-setter in 2006 found that users – particularly institutional investors and financial analysts – did not find a traditional auditor's report to contain information that they want to see. They want auditors to tell them more about the company and the audit itself.

In their minds, surely after weeks – if not months – of inquiries of management and ploughing the records of the company, the auditors could tell more in their report? Calls for more information in the auditor's report intensified in Europe and the United States after the 2008 financial crisis, especially with the collapse of conglomerates which had passed the audit, at least on paper.

A formal proposal to improve the auditor's report was finally released by the global standard-setter last June, and the public was invited to provide feedback. It attracted a lot of feedback. As many as 165 different stakeholders around the world provided their views on the proposal.

Whatever views were received, there is no turning back for the global standard-setter. The draft standard on the improved auditor's report is expected to be released within the next two months for final feedback after which the standard in its final form is expected to be released in June 2014.

In case anyone is wondering, yes, the auditors' reports of Singapore companies will be affected by the changes as well, given that Singapore follows global best practices. An audi-



Adding up: The current format of an auditor's report reveals only the end results of an audit, along with the boilerplate disclosures on the scope of the auditor's work, his responsibility and the management's responsibility. FILE PHOTO

tor's report of a Singapore company is expected to get its new look in 2015.

Not all stakeholders happily embrace the proposed changes. Some proposed changes have attracted a fair amount of concern over potential disagreement with the management and liability risk. The requirement to include a section in the report for the auditor to comment on important accounting and audit matters of the company has attracted mixed views.

It is meant to help users better navigate the increasingly thick financial reports so that sharper focus can be given to matters likely to impact their decision-making. This requirement could be contentious as the company may not agree with what the auditor writes in this section. The company is also worried that its auditor might reveal too much, causing it to run into the risk of attracting too much unnecessary attention to its financial reports.

Another major change will be the requirement for the auditor to conclude as to whether or not the company is likely to continue to operate and will not go out of business. This requirement does not end here. The con-

clusion is to be followed by an explicit statement to be made by the auditor on whether or not significant uncertainties in relation to the financial well-being of the company have been identified.

This change has been considered by some to be relevant and important in view of the recent global financial crisis which had affected many companies, where even conglomerates were not spared. The dilemma here is whether auditors are capable of making this conclusion given their less than intimate involvement in the affairs of companies that they audit.

The board of directors is the steward of the company, and the management is intimately involved in the day-to-day operations of the company and should therefore make such conclusion and explicit statement – but the auditor? The reason that the auditor is being made to give this conclusion and statement is that he is an independent party and can therefore be trusted to give objective views.

Similar to the proposal to highlight important matters, the company and the auditor may have different views on the financial well-being of the company, and they could therefore be em-

broiled in protracted debates over whose view is correct.

What if the auditor's negative conclusion or statement leads to its financiers pulling the plug, thereby causing its downfall? We suppose that one would not dispel the possibility of the auditor being sued in this scenario – which might not be too remote after all.

The traditional auditor's report is simple and safe. However, the auditing profession cannot ignore the fact that its value and relevance will come under intense scrutiny if it rejects calls for change. There will no doubt be challenges along the way but these are not insurmountable.

Moreover, there is no sign of the global standard-setter engaging in reverse gear on this front. It seems like there is no other way out for the profession but to step out of its comfort zone and move with the times.

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Proposed key improvements to the auditor's report

◆ **Auditor commentary:** This new section in the auditor's report will contain additional information on matters that, in the auditor's professional judgment, are likely to be most important to users' understanding of the audited financial statements or the audit.

◆ **Auditor conclusion on going concern:** The report will include the auditor's conclusion on the appropriateness of management's use of the going concern assumption. In addition, there will be an explicit statement as to whether material uncertainties in relation to being going concern have been identified.

◆ **Auditor statement on inconsistencies:** The report will include a statement as to whether the auditor has identified any material inconsistencies between the audited financial statements and other information in the document containing the financial statements, and specific identification of that other information.

◆ **Placement of information:** The auditor's opinion and other company-specific information will be more prominently located in the report.

◆ **Transparency and clarification:** The auditor's report will provide transparency about the audit itself, and clarify the respective responsibilities of the auditor, management and the parties responsible for governance.