



MEMO

15 September 2021

To: Mr Imran Vanker
Director Standards
Independent Regulatory Board for Auditors (IRBA)
Per email: standards@irba.co.za

From: IoDSA's Audit Committee Forum

AUDIT COMMITTEE FORUM: COMMENTS ON THE CONSULTATION PAPER 'ENHANCING DISCLOSURES IN THE AUDITOR'S REPORTS IN SOUTH AFRICA: ADDRESSING THE NEEDS OF USERS OF FINANCIAL STATEMENTS'.

The **Audit Committee Forum** (ACF), is a formal forum of The Institute of Directors in South Africa (IoDSA) that provides valuable information to assist audit committee members to be effective in their role on audit committees through sharing knowledge with their peers, disseminating relevant information and focusing on key performance areas, thereby contributing to the effective governance and sustainability of their organisations and enhancing the economic environment of South Africa.

The Independent Regulatory Board for Auditors' (IRBA) – through its committee - A Committee for Auditing Standards (CFAS) - approved and issued the consultation paper: *Enhancing Disclosures in the Auditor's Reports in South Africa: Addressing the Needs of Users of Financial Statements*.

The purpose of the paper is for CFAS to gather perspectives from stakeholders about the need and options for additional disclosures in the independent auditor's report for an audit of financial statements.

Overall Comments:

On **21 July 2021**, the IRBA, made presentations at the ACF's quarterly meeting. Below, we document, some key points that came from the overall discussion.

- A question was posed as to the objective of the proposed additional disclosures. Is it to enhance trust in the financial statements, or trust in the auditor's process? If enhancing trust in financial statements is the primary objective, a question needs to be answered as to whether the independent auditor's report is the most appropriate tool to do so.
- Information that can be adequately covered in the financials and the notes should not be included in the audit report too. Consideration should also be given that material issues should be addressed in the audit committee's report, and in the notes to the financial statements, ahead of them being required to be disclosed in the auditor's report.
- There is a risk that the auditor's report will be further burdened with too much information, making it harder for the users to read and understand.
- Careful consideration would need to be made on whether additional details supporting current year unadjusted differences should be provided. By definition, these are amounts that together or in aggregate are not material. Should uncorrected differences be disclosed, further disclosure around how these were deliberated, understood and decisions reached would also be required. The value of

this is questionable, and if sufficient context is not provided, this could expose companies and auditors to unnecessarily increased risk.

- A consideration should be made, as to whether these enhancements, could give rise to audit committees and boards concluding that some of their responsibilities have been abdicated to the independent auditor. These enhancements would have to be accompanied, by a clarification of roles and responsibilities.
- The regulator should engage with actual users of the financial statements e.g. fund managers, to ensure their understanding of the purpose of an audit report and their views on the value of the various suggestions.
- An important test for the value of the recommendations being made by IRBA will be to evaluate whether these incremental disclosures would have avoided or prevented any of the known recent corporate or financial reporting collapses. This is a useful means of assessing the purpose of the suggested areas of enhanced disclosure.

Specific comments made by the members of the forum to the IRBA, addressing direct questions posed in the discussion paper have been incorporated in the individual responses, below.

Question 1

Do you believe that additional disclosures in the auditor's report about the scope of the audit would be useful in enhancing the understanding of the audit that was performed?					
	Very useful	Useful	Somewhat useful	Not useful	No particular view
Scope of the audit. Refer to section A	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<p><i>Please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.</i></p> <ul style="list-style-type: none"> ▪ At present, an expectation gap exists between the defined scope of an audit and the expectations of the users of financial statements. This is despite the enhancements of the revised <i>Auditor Reporting Standards</i> which became effective on or after 15 December 2016. ▪ Therefore, additional disclosures on scope, could be useful in enhancing the understanding of the audit that was performed. However: <ul style="list-style-type: none"> ○ The detail would need to be crisp, and focused, so as not to overwhelm the users of financial statements. It is difficult to see how a comprehensive analysis of the scope of the audit could be achieved in a sufficiently succinct manner for the general user of financial statements. 					

Question 2

Do you believe that disclosing the **materiality threshold applied**, and an explanation of significant judgements made by the auditor in determining materiality for the audit in the auditor's report, would be useful in enhancing the understanding of the audit that was performed?

	Very useful	Useful	Somewhat useful	Not useful	No particular view
Materiality threshold applied, and an explanation of significant judgements made by the auditor in determining materiality for the audit. Refer to section A	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.

- An understanding of materiality thresholds and determination thereof may add enhanced the reader's understanding the audit process by making more specific the size of errors or misstatements that would not be considered by the auditor.
- However, materiality is not a simple concept and explaining the various ways in which materiality thresholds are set and applied within an audit could cause further confusion.
- There is real danger that, this disclosure, without a background as to how this relates to matters identified, could be taken out of context by users of financial statements.

Question 3

Do you believe that the **disclosure of performance materiality** in the auditor's report would be useful in enhancing the understanding of the audit that was performed?

	Very useful	Useful	Somewhat useful	Not useful	No particular view
Performance materiality. Refer to section A	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>

Please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.

- See comments under question 2.
- Most users will not have a good understanding of the process to compute, performance materiality and a whole education process would need to be embarked on.
- There is a risk that disclosing this amount could be taken out of context and expose the auditors to increased risk.

Question 4

Do you believe that additional disclosures in the auditor's report that explain the extent to which **the audit was considered capable of detecting irregularities, including fraud**, would be useful in enhancing the understanding of the audit that was performed?

	Very useful	Useful	Somewhat useful	Not useful	No particular view
Explanation of the extent to which the audit was considered capable of detecting irregularities, including fraud. Refer to section B	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as any suggestions you may have.

- The ambit of the audit committee's report should include enhanced disclosures around the organisations ability to detect or prevent fraud. Inclusion in the independent auditor's report would be very cumbersome and unwieldy. At best, enhanced disclosure about the nature of the procedures followed by the auditor in this regard could be expected. The question of how 'capable of detecting fraud' the audit is, is likely to simply be further boilerplate disclosure linked to the current auditing standards. Any significant changes to the auditors' responsibility around fraud should be handled in new standards rather than in the audit report.
- If disclosed, it could be useful to split the disclosure into two separate disclosures - **1)** audit effort related to irregularities, and **2)** audit effort related to fraud.

Question 5

Do you believe that disclosures in the auditor's report about how the auditor evaluated management's assessment of the entity's ability **to continue as a going concern** and, where relevant, key observations arising with respect to that evaluation would be useful in enhancing the understanding of the audit that was performed?

	Very useful	Useful	Somewhat useful	Not useful	No particular view
How the auditor evaluated management's assessment of the entity's ability to continue as a going concern and, where relevant, key observations. Refer to section C	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Please provide your reasons and indicate where applicable, what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.

- Enhanced disclosures about the organisation's ability to continue as a going concern should first be included in the financial statements themselves. This level of information would unduly burden the audit report.
- However, enhanced disclosures about the audit procedures followed in this regard, could be useful. Again, however, these disclosures are likely to be very boiler plate and simply make reference to the auditing standards.
- Again, if additional work is expected by the auditors on going concern or resilience, this should be addressed through revising the auditing standards themselves – and only after commensurate increased procedures and disclosure by the reporting entity

Question 6

Do you believe that a conclusion (i.e. a positive statement) that management's use of the going concern basis of accounting in the preparation of the entity's financial statements is appropriate should be included in the auditor's report?

	Yes	Maybe	No	No particular view
Conclusion (i.e. a positive statement) that management's use of the going concern basis of accounting is appropriate. Refer to section C	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.

- In order to give their opinion, auditors already make an assessment of going concern, whether significant indicators exist or not. By issuing an unmodified audit opinion, the auditors already make a positive statement. An explicit positive statement in the audit report may add marginal value to the user, but is not too onerous a requirement on the auditors

Question 7

Where there is a material uncertainty related to going concern, do you believe that procedures specific to the auditor's response to the material uncertainty related to going concern should be disclosed in the auditor's report?

	Yes	Maybe	No	No particular view

Procedures specific to the auditor's response to a material uncertainty related to going concern. Refer to section C	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
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please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.

- This would highlight what the issues are and add valuable insight. So, enhanced disclosure would add value.
- However, there is a risk that the auditors may be unduly cautious and result in negative outcomes for a company if users do not fully understand it. These are matters that could have significant unintended consequences for the reporting entity and for the auditors.

Question 8

Where the auditor concludes that no material uncertainty related to going concern has been identified, would a statement that the auditor has not identified a material uncertainty related to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern for a period of at least 12 months from when the financial statements are authorised for issue be useful to you as a user?					
	Very useful	Useful	Somewhat useful	Not useful	No particular view
A statement that the auditor has not identified a material uncertainty related to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern for a period of at least 12 months from when the financial statements are authorised for issue. Refer to section C	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>

please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.

- There is a risk that, too much reliance will be placed on the auditors and users will stop applying themselves to the going concern principles.
- The auditors assess going concern and if material uncertainty exists, the auditor modifies an audit opinion and requires the entity to provide detailed disclosures in the financial statements. There is no reason to highlight where the auditor has concluded that there is no material uncertainty.

Question 9

Are there any other matters related to going concern that you believe should be disclosed in the auditor's report?				
	Yes	Maybe	No	No particular view
Any other matters related to going concern that you believe should be disclosed in the auditor's report. Refer to section C	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	✓
<p><u>Please provide the details and where applicable, the benefits and drawbacks of disclosure of such matters, as well as any suggestions you may have.</u></p> <ul style="list-style-type: none"> ▪ Going concern disclosure should be dealt in the notes to the financial statements not in the auditor's report. ▪ Again, there is a risk that disclosure of matters like going concern considerations by the auditor, without the proper context, could expose auditors to increased risk and the reporting entity to unintended consequences 				

Question 10

Do you believe that auditor's reports, other than on listed entities and where law or regulation requires the application of ISA 701, should disclose KAMs?				
	Other PIEs	All Entities	No	No particular view
KAMs in auditor's reports other than on listed entities and where law or regulation requires the application of ISA 701. Refer to section D	✓	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<p><u>please explain your reasons for the answer to this question and where applicable, specify the type of entity for which you believe the auditor's reports should disclose KAMs, as well as any suggestions you may have.</u></p> <p>Even though KAM's have tended to become fairly boiler plate, it is useful disclosure, and it would be a good idea to extend this to include other Public Interest Entities.</p>				

Question 11

In your view, are descriptions of the outcome of audit procedures or key observations with respect to Key Audit Matters useful in understanding the KAM?					
	Very useful	Useful	Somewhat useful	Not useful	No particular view
Descriptions of the outcome of audit procedures or key observations with respect to Key Audit Matters. Refer to section D	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<p><i>please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.</i></p> <ul style="list-style-type: none"> A KAM outcome provides additional colour and focus if done properly but have tended to become very boiler plate. 					

Question 12

Do you believe it is beneficial to stakeholders to have visibility of the professional relationships between an audit firm and the audit client for audits of entities that are not PIEs?				
	Yes	Maybe	No	No particular view
Visibility of the professional relationships between an audit firm and the audit client for audits of entities that are not PIEs. Refer to section E.	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<p><i>Please provide your reasons. Where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder and specify for which types of entities should the disclosure of such professional relationships be. Also indicate any suggestions you may have.</i></p> <p>All auditors are required to be 'independent' and visibility of the relationship is beneficial. However, again it is unlikely that this should be handled through the audit report.</p>				

Question 13

If the answer to question 12 is "yes" or "maybe", do you believe this should be disclosed in the auditor's report?				
	Yes	Maybe	No	No particular view

Disclosure of professional relationships in the auditor's report. Refer to section E.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
<p><i>Please provide your reasons. Where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder or provide alternative mechanisms for such disclosure</i></p> <ul style="list-style-type: none"> There is a balance between what can be disclosed in the audit report, versus that which should be disclosed in the audit committee report. 				

Question 14

Do you believe the auditor's report is an appropriate mechanism to disclose the matters described in (a), (b), (c) and (d) in paragraph 65 in relation to fees?				
	Yes	Maybe	No	No particular view
Auditor's report an appropriate mechanism to disclose the matters described in (a), (b), (c) and (d) in paragraph 65. Refer to section E	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
<p><i>please provide your reasons. Where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder or provide suggestions on other possible mechanisms to achieve such disclosure, including the benefits and the drawbacks.</i></p> <ul style="list-style-type: none"> No this should be disclosed in the annual report or audit committee report if material. 				

Question 15

Do you believe the auditor's report is an appropriate mechanism to disclose whether an entity has been classified as a PIE or not?				
	Yes	Maybe	No	No particular view
Disclosure of whether an entity has been classified as a PIE or not in the auditor's report. Refer to section F	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<p><i>please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.</i></p> <ul style="list-style-type: none"> It is not clear, what material bearing this disclosure would have. The user would know this if it was important to them. 				
<p><i>If not, please provide reasons and suggestions on other appropriate mechanisms:</i></p>				

Question 16

Do you believe that when prior period financial statements that are misstated have not been amended and an auditor's report has not been reissued, but the corresponding figures have been properly restated or appropriate disclosures have been made in the current period financial statements, the matter should in all cases be described in the auditor's report?				
	Yes	Maybe	No	No particular view
Description in the auditor's report when prior period financial statements that are misstated have not been amended and an auditor's report has not been reissued, but the corresponding figures have been properly restated or appropriate disclosures have been made in the current period financial statements. Refer to section G	<input type="checkbox"/>		✓	<input type="checkbox"/>
<p><i>Please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.</i></p> <ul style="list-style-type: none"> Disclosure of the prior year misstatement is made in the financial statements. There is no additional benefit, to overwhelming the audit report with a huge amount of detail, which has already been disclosed in the financial statements. 				

Question 17

Where such disclosure is made in the auditor's report, whether mandated or not, do you believe that tailored descriptions of the audit procedures performed, and key observations made by the auditor regarding prior year material misstatements, would be useful in enhancing the understanding of how the auditor addressed the matter?					
	Very useful	Useful	Somewhat useful	Not useful	No particular view
Tailored descriptions of the audit procedures performed, and key observations made by the auditor regarding prior year material misstatements. Refer to section G	<input type="checkbox"/>	<input type="checkbox"/>	✓	<input type="checkbox"/>	<input type="checkbox"/>
<p><i>please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.</i></p>					

- There is value to understanding how a prior material misstatement was not addressed appropriately by the auditors (and the reporting entity)
- There is however a risk, that this gets used against the audit firm whereas, there is joint accountability between auditors, management, and the Board.
- Entities would need to carefully consider details supporting, prior year misstatements and the current year unadjusted differences. How these were deliberated, understood and decisions reached. If sufficient context is not provided, this could expose companies to increased risk.
- There is a need to guard against creating the impression that the auditors are the ultimate custodians of giving comfort to investors.
- This would also be too cumbersome to include in the audit report itself.

Question 18

Do you believe the disclosure of the threshold of unadjusted misstatements in the auditor's report would be useful in further enhancing transparency by auditors?

	Very useful	Useful	Somewhat useful	Not useful	No particular view
Do you believe the disclosure of the threshold of unadjusted misstatements in the auditor's report would be useful in further enhancing transparency by auditors? Refer to section H	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>

Please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.

- This needs to be addressed by the Audit Committee and adjusted if necessary. Not all identified issues by the auditor are simply easy to adjust – specifically extrapolated audit differences or areas of significant estimation or judgement.
- Entities would need to carefully consider details supporting, prior year misstatements and the current year unadjusted differences. How these were deliberated, understood and decisions reached. If sufficient context is not provided, this could expose companies to increased risk.
- The audit report would seem to be too cumbersome a place to include these disclosures though.

Question 19

In relation to the matters described in sections A, B, C, G and H in the Consultation Paper, if applicable, would you please indicate for which types of entities these disclosures should be made? Your response should be in the format set out below (tick where appropriate and provide your reasons, including benefits and drawbacks, in the comment box).

Details	All entities	PIEs only	Listed entities only	Other (Please explain)	Disclosure should not be made at all (Please explain)
Extending the disclosures of the audit scope <i>Refer to section A</i>	X				
<u>Comments:</u> 					
Materiality <i>Refer to section A</i>	X				
<u>Comments:</u> 					
Performance materiality <i>Refer to section A</i>					X
<u>Comments:</u> This would add no value to the users of financial statements and would create confusion and expose the auditors to unnecessary risk. There is a lot of judgement applied in determining materiality and users with no context of the audit process may be confused by this.					
Enhancing the disclosure of the audit effort related to irregularities, including fraud <i>Refer to section B</i>	X				
<u>Comments:</u> 					
Enhancing the disclosure of the audit effort related to going concern <i>Refer to section C</i>	X				
<u>Comments:</u> 					
Auditor's report disclosures arising from prior year misstatements <i>Refer to section G</i>	X				
<u>Comments:</u> 					

Disclosure of the reporting threshold unadjusted misstatements <i>Refer to section H</i>	X				
	<u>Comments:</u>				

Please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.

- Also refer to the comments from the overall Audit Committee Forum meeting held in July 2021

Question 20

Other than those proposals discussed in sections A to I in the Consultation Paper, are there more matters that can be disclosed by auditors in the auditor's report for an audit of financial statements?

	Yes	Maybe	No	No particular view
More matters that can be disclosed by auditors in the auditor's report.	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Please provide your reasons and where applicable, indicate what the benefits and drawbacks would be to you as a stakeholder, as well as any suggestions you may have.

- We would like to re-iterate the concern that the audit report might become so cluttered and contain so much detail that the users are not able to see the wood for the trees.
- Users will then just stop reading it. The Audit Committee needs to deal many of the above issues and if necessary, include their decision-making in their report.
- We also refer you to the overall comments on this paper, where the IRBA back testing the value of their suggestions against known cases of corporate or reporting failure – would be valuable

Question 21

Should there be prescribed standards or a rule that will mandate additional disclosures in the auditor's report? If not, please provide your reasons.

	Yes	Maybe	No	No particular view
Prescribed standards or a rule that will mandate additional disclosures in the auditor's report.	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Please provide your reasons and where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder, as well as any suggestions you may have.

- Any required or enhanced disclosures would necessarily have to be included in prescribed standards to ensure consistency of application.

Question 22

Is there a need to develop a structure or framework within which to accommodate currently envisaged but also future changes to auditor's report contents?

	Yes	Maybe	No	No particular view
A need to develop a structure or framework within which to accommodate currently envisaged but also future changes to auditor's report contents.	✓	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Please provide your reasons. Where applicable, indicate what the benefits and drawbacks of such disclosures would be to you as a stakeholder and explain what the elements of such a framework would be. Also provide any suggestions you may have.

- Yes, including guidance and education for the users. To ensure that the enhanced disclosures are not taken out of context or simply ignored.