

Auditing and Assurance for Larger Registered Charities

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Presentation Outline

1. Engaging in the “Right Debate”
2. Understanding the current state of play
3. Recap on “Tentative Proposals”
4. Implications of the Proposals for the Charitable / Not For Profit Sector
5. Understanding the value / purpose of assurance
6. Understanding the difference between audit / reviews (other options for enhancing confidence in financial information)
7. Issues and Challenges facing charities / users and assurance providers
8. Implications for the NZAuASB

Engaging in the “Right Debate”

- Often, we look at the issue through the following lens:
 - What is the nature of the assurance engagement that I’m required to have (legislation / constitution / Rules)
 - Audit is an unnecessary cost on my entity, do I really need one?
 - The cost of an audit / assurance engagement is prohibitive, is there a “cheaper” alternative
- What is the “Right Debate”?
 - What level of assurance is appropriate in order to effectively discharge my entity’s public accountability / financial accountability obligations to stakeholders, users or funders
 - How can I effectively balance the level of assurance my entity’s stakeholders / funders needs with the cost associated with providing that level of assurance / comfort

Current Situation

- Many charitable organisations required to have an audit
 - Not all charitable organisations have an audit
 - Many “funders” require an audit as part of funding arrangement
- Audit = most common form of assurance engagement
- Audit suffers from an “expectation gap” issue
- Perceived lack of “value” and understanding of audit
- Range of assurance or professional engagement that could enhance or add credibility to financial information
- Increasing demand for “cheaper” review engagements
- Audit / Assurance Quality is an issue
- Quality – affected by skill and competency of practitioner

Recap on Tentative Proposals

- Registered Charities are publicly accountable, receiving significant levels of donation (\$1.2bn)
- Registered Charities impacted by new Financial Reporting requirements
- Financial reporting and / or accountability concerns
- Tentative Proposals:

OPEX < \$200k	OPEX \$200k - \$300k	OPEX > \$300k
No statutory requirement for assurance, entity may decide	Audit or Review level of assurance	Audit level of assurance

- Cost of Audit vs. Review comparisons – marginal pricing difference

Implications of Proposals

- Proposals – assurance on financial reporting
- Legislative requirement for audit if OPEX > \$300k enhances consistency where public accountability
- Charities with OPEX \$200k - \$300k – have a **choice** to make ... Audit or Review
- Charities < \$200k – no legislative requirement, but retain the **option** of having a level of assurance ... **entity choice**
- Proposals do not directly affect ability of funding agencies to obtain assurance, comfort or information
- Choices and options for charities / funders
- Challenge – making the most appropriate choice ...
Engaging in the “Right Debate”

Evaluating the Value of Assurance

Briefly Looked
at Current
Audit Market
in NFP Sector

Recap on
Tentative
Proposals

Implications of
the Proposals

Understanding
the “Value” of
Assurance

Differences
between Audits
and Reviews

Tentative
Proposals -
What are some
of the Possible
Issues &
Challenges for
Stakeholders,
Users &
Assurance
Providers

Value of Assurance Engagements

- Those charged with governance usually have an obligation, established by law or agreement to report on the results of their financial operations and position.
- Many entities publicly accountable
- Entities may be required or may elect to have an independent assurance engagement to:
 - Ensure the credibility of the financial information; and
 - Enhance users confidence that the financial information does not contain material misstatements / fairly reflect results of operation
- The increased confidence derived by an **independent and objective expert's** assurance report:
 - Assists users decision making; and
 - Improves accountability, governance and comparability

Audit vs. Review Assurance

- Appreciating the differences between an audit and review is critical to understanding the level of assurance

Audit Engagement	Review Engagement
An audit is designed to provide a reasonable level of assurance	A review is designed to provide only limited assurance
Audit Report: Opinion , expressed in positive form ... “ in our opinion , the financial statements present fairly ...”	Report: Conclusion , expressed in the negative form ... “based on the work performed, as described in the report, nothing has come to our attention , that ...”
Provides a higher but not absolute level of assurance ...	Provides a much lower level of assurance than from an audit ...
Assurance that no material errors or omission	Increased risk that assurance provider may not become aware of significant error

Expectation Gap Concerns

- Expectation gap – Arises from a misunderstanding of the role and purpose of an audit / assurance engagement:

Audit Engagement comprise:	Review Engagement comprise:
<ul style="list-style-type: none">• Performing entity risk assessments• Evaluating and testing internal control systems• Testing selected transactions• Obtaining independent confirmation or verification• Completing physical inspections and observations• Analytical procedures and comparative analysis <p>Drives a higher level of “Work Effort”</p>	<ul style="list-style-type: none">• Completion of analytical procedures and comparative analysis• Where these procedures indicate the possibility of a material misstatement may need to undertake further investigation <p>Drives a lower level of “Work Effort”</p>
<ul style="list-style-type: none">• Involves a high level of professional judgement, knowledge and experience	<ul style="list-style-type: none">• Involves a high level of professional judgement, knowledge and experience

Expectation Gap Concerns

- What an Audit (or Review) is and is not:
 - An audit or review does not relieve management or those charged with governance of their responsibility for the:
 - Preparation of the entity's financial statements
 - Judgements or estimates contained in those financial statements
 - Safeguarding the entity's assets and maintaining systems of internal control
 - Prevention and detection of fraud, errors or irregularities
 - Not an absolute level of assurance
 - Doesn't involve checking every single item in the financial statements
 - Assurance over aspects of an entity's operations that do not have an impact on the preparation of the financial statements
 - Guarantee of the future viability of the entity

Other Non-Assurance Options

- Within the charitable / not for profit sector stakeholders of users may derive confidence in financial information or regarding a matter of accountability through:
 - Assurance (audit or review) of financial statements
 - Funders / users could seek assurance, information or advice of use and application of funding provided
 - Compilation of financial statements by an appropriately qualified person against a recognised financial reporting framework
 - Other “direct” form of assurance or non-assurance (Agreed Upon Procedures) engagement
- Engaging in the Right Debate – ensuring that stakeholders and users make the most appropriate choice in respect of the matter or accountability

Proposals – Issues & Challenges

Briefly Looked
at Current
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Proposals – Issues & Challenges

■ User / Entity Perspective:

- There is already an expectation gap issue – will greater use of review engagements widen or further blur this issue
- Does an audit or review of the financial statements really give me what I am looking for (funder concept)
- How do I choose between the option of audit or a review
- Should I continue to obtain assurance if I'm not required to
- What are the compliance costs associated with the assurance engagement
- Impact of changes to financial reporting framework still need to be managed
- Confidence in quality and competency of assurance provider
- Quality of current financial reporting practices, accounting systems, accounting records and control systems

Proposals – Issues & Challenges

- Assurance Provider Perspective
 - A review is a separate / discrete professional engagement – it is not a “limited” or “restricted” audit
 - Which Standards are applied to the performance of the engagement – audit or review
 - Skills, competencies and experience required ... Is it possible for audits or reviews to be undertaken by individuals who are not trained accountants
 - Based on current international developments ... is it actually possible to perform a review engagement? ... Are the entity’s accounting systems sufficiently robust to enable a review to be performed?
 - Audit / Assurance quality remains a significant challenge / focus

Implications for the NZAuASB

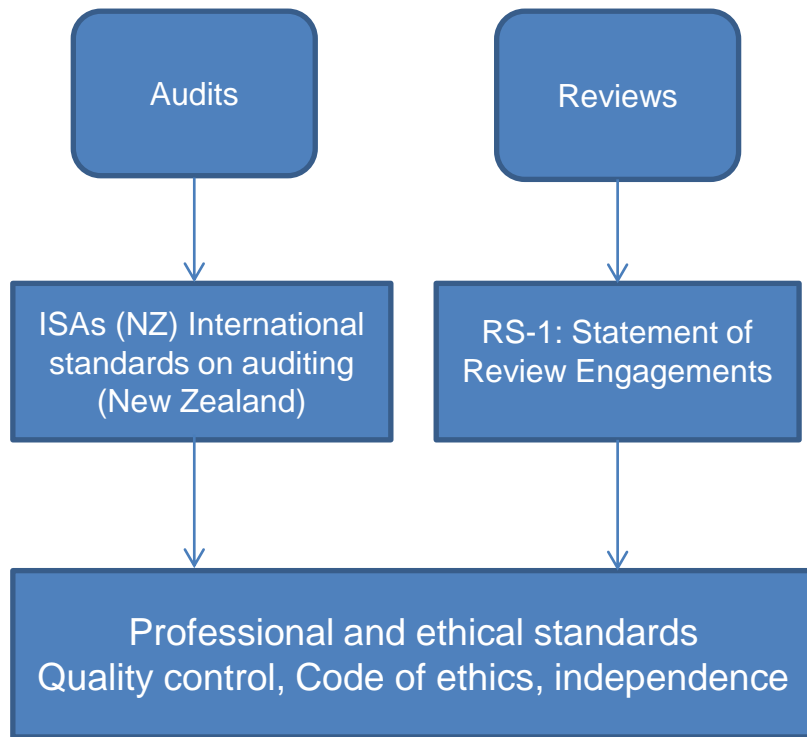
- NZAuASB has delegated authority to:

Develop and issue auditing and assurance standards for use by assurance providers where there is a requirement (statutory, professional bodies etc.) to use those standards

- Scope of NZAuASB responsibilities:
 - Auditing and Assurance Engagement Standards
 - Professional Standards (e.g. Quality Control)
 - Ethical Standards (Code of Ethics, Independence)
 - Excludes non-assurance standards (including Agreed Upon Procedures Standards)

Existing Assurance standards

- NZAuASB Standards governing audits and reviews:



- Existing standards in place for audits and reviews
- No changes required for audit engagements
- Significant international developments on future performance of review engagements

Summary

- Many entities in the charitable not for profit sector are publicly accountable and subject to new financial reporting requirements
- Some charitable entities required to have an audit or review
- Tentative proposals to require a level of assurance - designed to enhance credibility and confidence in financial reporting
- Engaging in the “Right Debate” – understanding the value of assurance and difference between audits and reviews
- “Right Debate” – broader issue around accountability

Enhancing Quality & Confidence

Enhancing the Quality, Credibility and Confidence in Financial Reporting / Public Accountability / Financial Accountability

Quality Outcomes Sought

Enhancing quality where no independent assurance provided

High Quality Compilation / Preparation or Provision of Financial Information

Agreed Upon Procedures

Engagements that provide independent assurance

Reviews

Audit

Level of Assurance Provided

“Limited” Assurance

“Reasonable” Assurance

Quality Enhancer

Qualifications / Competencies / Experience
Established Financial Reporting Frameworks / Performance Standards
Independence / Objectivity
Oversight / Monitoring / Quality Control

Questions

