EXTENDED AUDITOR REPORTING - SUMMARY

The FRC has reported on the results of its second survey, “Extended auditor’s reports: A further review of experience”. The report covers developments in auditor reporting covering c.80% of the premium listed FTSE 350 companies in the UK. We have taken account of feedback from investors in order to identify those areas of best current practice and those where there is scope for further improvement.

Auditors are required to describe in their reports, their assessed risks of material misstatement, materiality and the scope of their audit. These high-level requirements are supported by enhancements to the UK Corporate Governance Code, including more detailed annual reporting by audit committees. They were designed to enhance the level of investor confidence in audit, by providing greater insight and understanding from the work of auditors.

Key findings include:

- Investors welcome the information included in extended auditor’s reports, and particularly for smaller companies where there tends to be less independent information available;
- In general, auditors have continued to move away from generic language and descriptions of risk, making their reports more relevant and insightful;
- The reports which have earned the greatest praise from investors tend to be well structured, signposting key information and often make innovative use of graphics, diagrams and colour.

Many investors feel that more could be done to enhance auditor’s reports, including:

- Providing more complete information about the sensitivity ranges used in audit testing;
- Giving greater insight into the auditor’s assessment of the quality of an entity’s internal controls informing their significant risk assessment;
- Being more explicit about the auditor’s view on the appropriateness of management estimates.

Overall, investors prefer greater transparency about assumptions made by management and the benchmarks used by auditors in making key judgements. The FRC recognises that this has to be balanced against the potentially competing demands for auditor’s reports to demonstrate clarity and conciseness, as well as preserving the importance of reading an overall true and fair opinion.

Areas where auditor’s reports could be further enhanced include:

- More frequent inclusion of commentary about what the auditor found as a result of the work done on risks of misstatement;
- Explanations of changes to the audit approach, materiality or risk assessment over time;
- More auditor’s to include information about ‘performance materiality’ – how it is derived and how it impacts on the audit.