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## **OPPORTUNITIES FOR ENHANCING INFORMATIVE VALUE OF AUDIT REPORTS**

*The question of information content of audit reports is discovered in this paper. The role of audit reports in decision-making by its users is examined in the paper. It was found that audit reports are an important source of information for the users of such statements. The need to increase the information content of audit reports and the criteria as such informative have been established. This publication considers the requirements which are brought to the Auditor's report. Attention is directed both to those charged with governance in the company and all stakeholders. An audit report should describe the responsibilities of the auditor, i.e. to identify and assess risks of material misstatements in the financial statement; to design and implement audit procedures in response to those risks and to obtain sufficient and relevant audit evidence on which the audit opinion will be based. The aim of the article is to discuss the changes in international auditing standards and auditors' liability.*

**Keywords:** *audit reports; auditors' liability; informative value of reporting.*

**Formulation of the problem.** The informative value of reporting is closely related to the role of auditors when stakeholders need to make adequate decisions. It is an expression of their social responsibility to provide an opinion about the reliability of financial statements. Therefore, opportunities for enhancing the quality of audit should be considered in terms of the impact of globalization as well as changes in audit standards and requirements to auditors who aim at ensuring that useful information which will be provided in audit reports. The underlying idea is to minimize the gap between the expectations of shareholders, investors, suppliers, and customers on one hand, and

the framework set by ISA in terms of procedures, auditors' responsibility, and the information presented in auditors' reports, on the other hand.

**Statements of the basic material.** The amendments which have been introduced [3, 2, 8], especially the requirement that an auditor's report should describe major risks of material misstatement, render it possible to provide more comprehensive and transparent information to stakeholders. These amendments are key steps towards enhancing the 'consumer value' of audits at a European level<sup>1</sup>. It is essential that auditors could meet the need for information (mainly on behalf of investors) and for more informative audit reports providing specific information about audited entities.

Minimum requirements to the contents of audit reports, such as identifying the audited financial statement and the applicable common financial reporting framework, description of the scope of audit and the need to express an unqualified, qualified or adverse audit opinion are included in the 2013 Accounting Directive [1]. In addition to those requirements, the updated text of the Audit directive provides the measures that will raise investors' awareness of the audit process.

The audit directive also provides that member states may lay down additional requirements [3] in relation to the contents of the audit report. Minimum general requirements are included in International Standard in Auditing (ISA) 700 (revised) which states that an opinion should be presented as to whether a financial statement has been prepared, in all material aspects, in compliance with the applicable financial reporting framework and whether that representation is faithful.

The major amendments to the standard include:

- An auditor's opinion should be presented in the audit report and all sections should have subtitles to improve readability and facilitate structuring of reports. Using a specific format or formulation is allowed, provided that the minimum required elements are included in the report;

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<sup>1</sup> Refer to Article 26 of the Directive and Article 9 of the Regulation

- Improved transparency; clearly defined responsibilities; a statement about compliance with independence requirements on behalf of the auditor and other ethical responsibilities; a statement of the name of the partner responsible for the commitment (only with reference to listed entities); a detailed description of the auditor's responsibilities and the key features of the audit; a description of the responsibilities of managers and the auditor in terms of the going concern assumption;

- A new section should be added to the auditor's report to give the necessary reference to other information presented with the audited financial statement;

- Disclosure of information referring to issues related to the going concern assumption when applicable.

A major amendment is the requirement that an auditor should report any material uncertainty identified that refers to the going concern assumption. An audit report should therefore provide a statement on any material uncertainty relating to the events or conditions that may cause significant doubt about the entity's ability to continue as a going concern'[3]. This disclosure should only be required when an auditor has identified such a material uncertainty.

According to ISA 570 (revised) the objectives of the auditor are:

- To obtain sufficient and appropriate audit evidence regarding, and to conclude on, the management's use of the going concern basis of accounting in the preparation of financial statement.

- To conclude, based on the audit evidence obtained, whether a material uncertainty exists related to the events or conditions that may cause significant doubt on the entity's ability to continue as a going concern.

- To report in accordance with this ISA.

When a material uncertainty relating to the going concern assumption has been adequately disclosed by the management, the audit report should include a separate section 'Material uncertainty related to the going concern assumption' without modification to the auditor's opinion. In a case if the material uncertainty has not been disclosed by the management, the auditor

has to express a qualified or adverse opinion. Should a potential danger occur in result of the events or conditions which may cause significant doubt on the ability of an entity to continue as a going concern, yet there is no material uncertainty, the auditor is required to evaluate whether the financial statement presents adequate disclosures of those events or conditions. Additional reporting is not required when no problem with the going concern assumption has been identified.

All the audit reports are required to provide a detailed description of the responsibilities of the management and the auditor related to the going concern assumption, which should include:

- Consideration whether a potential danger is the result of identified events or conditions, yet there is no material uncertainty. In such cases, the auditor is required to assess the adequacy of the disclosure of these events or conditions on behalf of the management in terms of the requirements of the applicable common financial reporting framework, *or*

- Identifying material elements of uncertainty which have not been disclosed by the management. In such cases, the auditor is required to express a qualified or adverse opinion<sup>2</sup>.

ISA 720 (revised)<sup>3</sup> includes new requirements relating to auditors' reporting. Auditors are required to read and evaluate the nature of other information<sup>4</sup>, and to take adequate measures. The report should either include a statement that the auditor has nothing to report or, if the auditor has concluded that there is an uncorrected material misstatement of the other information, the statement which describes that uncorrected material misstatement. According to the provisions of the new Regulation [3], auditors' reports about public interest entities should include:

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<sup>2</sup> Although not statutory, according to a recent decision within the framework of the programme of the IFRS Interpretations Committee, an entity's decision about the going concern assumption could meet the requirements on significant judgments in compliance with IAS 1 which should be disclosed.

<sup>3</sup> After approval from the Public Interest Oversight Board (PIOB) of the applied regulated procedure.

<sup>4</sup> Defined in ISA 720 (revised) as financial or non-financial information (different from the financial statement and the auditor's report on it) that is included in the annual report of the entity

- The description of major assessed risks of material misstatements, including assessed risks of material misstatements as a result of fraud.

- Summarized information about the procedures which the auditor has undertaken in response to those risks; and

- key remarks relating to those risks.

The auditor should also specify to what extent statutory audit is able to detect irregularities including fraud, or to confirm that the auditor opinion is consistent with the additional report to the Audit Committee. Except for this confirmation, it is not necessary to make any other references to the report to the Audit Committee. For the listed entities, auditors are required to include questions focusing on:

- Areas with a higher assessed risk of material misstatements or material risks.

- Material audit assessments relating to areas of material judgment on behalf of the management (for example, complex accounting estimates).

- The impact of major events or transactions and operation on the audit.

The auditor is not prevented from disclosing an issue which is not present in the financial statement, yet internal information should not be disclosed and professional ethics should be observed.

In terms of risks of a fraud related to material misstatements in financial statements, ISA 240 [4] provides that auditors are required to:

- identify and assess the risks of material misstatements in the financial statement because of a fraud;

- obtain sufficient and relevant audit evidence concerning assessed risks of material misstatements because of a fraud by designing and applying adequate procedures in response to those risks; and

- include appropriate disclosure in the audit report.

ISA includes requirements and more detailed instructions regarding the communication between the external auditor and

those ones charged with governance<sup>5</sup> in ISA 260 (revised) [6] and ISA 265 [7]. ISA 260 (revised) put an emphasis on the need of efficient and prompt bilateral communication. The issues which an auditor should consider in his manual include:

- The scope of auditor's responsibilities relating to audit.
- The planned scope and time for conducting the audit, including the reference to the material risks identified by the auditor.
- Major audit findings.
- Issues related to the independence of the auditor.
- Major deficiencies in internal control identified by the auditor during the audit.

EU requirements related to communication with the Audit Committee are much more specific than that ISA 260 (revised) which is primarily based on principles. Although the definite stages of communication are required, some of them may be conducted verbally. As for irregularities, the international standards on audit focus on the detection of fraud in the process of auditing the financial statement. An audit report should describe the responsibilities of the auditor, i.e. to identify and assess risks of material misstatements in the financial statement; to design and implement audit procedures in response to those risks and to obtain sufficient and relevant audit evidence on which the audit opinion will be based. According to ISA 250 [5], when auditing financial statements, an auditor must report to those charged with governance any instances of non-compliance with laws and regulations which have been identified in the audit process, except for the cases when such issues are insignificant. Should the auditor suspect that management or those ones charged with governance are involved in non-compliance, the auditor should communicate

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<sup>5</sup> This includes the Board of Directors and the Audit Committee. 'Those ones charged with governance' is a term referring to the person(s) or organization(s) (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those ones charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager. (Source ISA 260 (revised))

about the matter to the next higher level of authority at the entity or outside the entity.

**Conclusions.** Amendments in legislation have been made to meet the demand of users of audit reports for more reliable information provided by the components of financial statement and financial indicators as of the date of their preparation. In order to give a 'fair and truthful opinion', auditors need to make sure that the content of audited documents has priority over their form. It is therefore necessary to raise the awareness of users of financial and non-financial information about the constraints on the audit process as they may lead to the gap between expectations and performance and cause doubt on the quality of conducted audit.

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Наукові інтереси:

– проблеми підвищення інформативності аудиторських висновків.

Стаття надійшла до редакції 19.04.2016.