

Writing effective legislation for annual reporting

Executive summary

What does this paper cover?

This paper provides an explanation of terminology which can be used when:

- Setting financial reporting requirements
- Setting assurance requirements
- Setting qualification requirements for the practitioner

It also explains what assurance services are and why it is important to use consistent and appropriate terminology.

Who is this for?

This document is intended to assist regulators, government departments and other entities who wish to include audit or other assurance requirements in relation to historical financial information or other information in legislation, regulations or contracts such as grant agreements.

Why is this paper necessary?

It is important that financial reporting and assurance requirements are drafted in a way that allows users to receive consistent, useful information and those carrying out the assurance services can provide high quality, efficient engagements while complying with their professional and ethical obligations.

Recent research into Australia's state, territory and federal legislation reveal a wide variety of language being used. For example, over 136 unique terms describing the information subject to audit and 101 unique descriptions for the auditor and their qualification. This lack of consistency results in confusion and is a clear burden on Australian business.

It is vital that Australian legislation uses consistent, clear and accurate wording in prescribing these requirements to ensure that business is able to operate efficiently and trust in reported information is well placed.

How can this be achieved?

Steps	Recommended wording in relation to a full financial report	Recommended wording in relation to a statement of income and expenditure
1. Decide what information is required (using the explanation in this guidance of the different types of financial information and its uses)	At the end of the financial year, the [entity] must prepare a financial report that consists of the financial statements, the notes to the financial statements and a [governing body's] declaration. The financial report must comply with Australian Accounting Standards.	At the end of the financial year, the [entity] must prepare a statement of income and expenditure. The statement must be prepared in accordance with [state preferred basis of preparation].
2. Decide what level of assurance is required (using the explanation in this guidance of the different types of assurance and its uses)	The financial report must be audited. [A time limit may also be included].	The statement of income and expenditure must be audited. [A time limit may also be included].
3. Decide who can perform the assurance engagement (using the explanation in this guidance of different types of qualifications)	The auditor must be a member of Chartered Accountants Australia and New Zealand, CPA Australia or the Institute of Public Accountants who holds a certificate of public practice.	The auditor must be a member of Chartered Accountants Australia and New Zealand, CPA Australia or the Institute of Public Accountants who holds a certificate of public practice.

The process for developing financial reporting and assurance requirements

Step 1: Decide what information is required

Things to consider:

- Who are the users of the information?
- Do the users need a full financial report?
- Do they need a single statement?
- Do they need a statement with some notes?

When deciding what would be helpful, the requirement will need to state that clearly using consistent and appropriate terminology. Appendix 1 sets out key concepts for accounting terminology.

When setting the legislative requirements, the drafting also needs to address the basis of preparation and the period the statement is intended to cover. For example; a statement of

financial position, a statement of trust monies held, and a statement of assets are prepared as at a point in time. In contrast, a statement of income and expenditure, a statement of profit or loss, and a statement of cash flows cover a specified period of time.

Problematic terms

Terms such as “books and records”, “accounts” and “trust records” have historically been used as previously there were no recognised formats for financial information. These terms do not have a defined meaning under the Australian Accounting Standards so they are no longer appropriate to use.

Example of a clear description of requirements

“At the end of the financial year, the association must prepare a financial report consisting of the financial statements, the notes to the financial statements and a Committee’s declaration for the financial year which is prepared in accordance with Australian Accounting Standards”

Where the situation is complex or assistance is needed in determining the appropriate requirements or terminology consider consulting with the Australian Accounting Standards Board (AASB) or having professionals with appropriate accounting experience involved in the drafting process.

Step 2: Decide what level of assurance is required

Things to consider:

- What is the objective of requiring assurance?
- What type of information is to be assured?
- Is more than one kind of information being assured?
- Do you want to prescribe a format for the report?

Understanding the objective you are trying to achieve will help determine what level of assurance is required. You may even identify that you have multiple objectives that need more than one assurance engagement, for example; assurance on compliance with regulations and financial information. See Appendix 2 for the different assurance services and when each may be suitable.

The Australian auditing and assurance standards contain mandatory requirements for the contents of assurance reports therefore specifying that the engagement is to be performed in accordance with these standards will ensure that consistent reporting is obtained. If a prescribed report is desired then consultation with the Australian Auditing and Assurance Standards Board (AUASB) should be undertaken to avoid prescribing a report that does not comply with the requirements of the Australian auditing and assurance standards.

Problematic terms

Use of terms that are not defined under the AUASB Framework results in uncertainty as to what the practitioner is required to do. This requires the practitioner to interpret the requirements, this subjectivity can result in inconsistency in what is provided to the users which may be misleading. In particular, use of the terms “certify”, “confirm” and “correct” should be avoided as they imply absolute assurance which cannot be provided by any assurance service.

Where verification of factual information is required, an agreed-upon procedures engagement may be appropriate. It may be that there is a very low or zero tolerance for error due to the nature of the information. An audit or review cannot provide absolute assurance

(guarantee there are no errors) and these terms should not be used when requiring certainty.

Similarly, when dealing with assurance of information, the use of the terms “audit”, “auditor”, “review” and “reviewer” should only be used in accordance with their defined meanings under the Australian auditing and assurance standards. The use of the word “review” in other circumstances is acceptable only when it is clear the term is not being used to mean a limited assurance engagement.

Example of a clear description of requirements

See Appendix 3 for types of assurance engagements along with illustrative report wording. Where the situation is complex or assistance is needed in determining the appropriate requirements or terminology consider consulting with the AUASB or involving professionals with appropriate audit experience involved in the drafting process. More complex areas may be non-financial information or prospective financial information.

Step 3: Decide who can perform the assurance engagement

Things to consider:

- Is the description clear and unambiguous?
- Is the description in line with professional standards?
- Does the description allow for an appropriate qualification?
- Does the prescribed qualification ensure independence?

In Australia, there are four choices when considering who can perform the assurance engagement.

1. A registered company auditor (RCA) - The RCA designation is highly respected and a sign of quality. However it was developed for the purpose of specific audits, primarily historical financial statement audits for Corporations Act entities required under the Corporations Act. While much of the foundation knowledge, skills and experience necessary to undertake a financial statement audit under the Corporations Act may be relevant to undertake other assurance engagements, it is not the only appropriate auditor qualification that should be imposed in all circumstances. Most assurance engagements prescribed by Australian legislation should not impose this requirement.
2. The Auditor-General of the relevant jurisdiction. Usually appropriate for public sector entities.
3. A member of Chartered Accountants Australia and New Zealand, CPA Australia or the Institute of Public Accountants who holds a certificate of public practice. These members are subject to initial and continuing professional development, ongoing monitoring and disciplinary regimes which all promote quality. In addition, these members must comply with professional and ethical standards, this prevents them from accepting engagements which they do not believe they are competent to perform. Therefore a member of one of these professional bodies will have the appropriate skills and expertise. The holding of a public practice certificate will also ensure that the practitioner has appropriate professional indemnity insurance. We believe this is an appropriate level of qualification to specify for a range of circumstances.
4. Anyone else. Where the qualification is not specified in detail, for example; “a person” or “a qualified person” then the user is not protected by the standards and education which a member of a professional accounting body is held to. It also removes the protection of

professional indemnity insurance. We do not recommend that such broad clauses be used.

Why reference a professional accounting body?

It is important that those designated to undertake the role of assurance practitioner have achieved a high level of competence and conduct and carry out the engagement professionally and diligently.

Members of Chartered Accountants Australia and New Zealand and the other professional accounting bodies in Australia must comply with the Australian Accounting Standards issued by the AASB and the auditing and assurance standards issued by the AUASB. The AASB and AUASB are both government bodies and are responsible for ensuring that there are high quality accounting standards and audit and assurance standards respectively in Australia. The use of terminology that is consistent with the frameworks issued by the AASB and AUASB is vital to ensuring that:

- The information being provided to the users is prepared in a reliable and consistent manner and provided under an agreed framework.
- The assurance provided on that information is high quality and provided under an agreed framework.

These will allow users to be comfortable that the information provided to them is reliable and not misleading.

Independence and ethics

Independence is one of the key attributes of an assurance engagement. The independence of the practitioner adds credibility to their assurance report and allows the practitioner to maintain their integrity and objectivity. In relation to assurance engagements independence requires:

- (i) Independence of mind – the state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity, and exercise objectivity and professional scepticism; and
- (ii) Independence in appearance – the avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude, that a firm's, or a member of the audit and assurance team's, integrity, objectivity or professional scepticism has been compromised.

In Australia, members of the professional accounting bodies must comply with APES 110 *Code of Ethics for Professional Accountants* as well as other professional and ethical standards issued by the Australian Professional and Ethical Standards Board (APESB). APES 110 deals with the five fundamental principles of professional ethics; integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

Recommended description of qualification requirements

We recommend that the wording used for the majority of situations where it is not imperative that the Auditor-General or an RCA perform the work should be; "The auditor must be a member of Chartered Accountants Australia and New Zealand, CPA Australia or the Institute of Public Accountants who holds a certificate of public practice".

APPENDIX 1: Key concepts – accounting terminology

Regulators or others may recommend particular types of reporting, which may be financial or non-financial information. Financial information should use the terminology and concepts set by the AASB where possible. Non-financial information may either be prepared in accordance with an external framework established by a regulator or other body or in accordance with criteria established by the entity. As these engagements are less common, this document will focus on terminology for historical financial information (financial information).

Basis of preparation	This is the framework under which the financial information is prepared. In order for the information received by users to be consistent, it is important to specify an agreed framework for the preparation of the financial information. This may be a cash basis of accounting, an accruals basis of accounting or compliance with the accounting standards issued by the AASB.
Financial report	A financial report is a set of financial statements; a statement of financial position (commonly known as a balance sheet), a statement of financial performance (commonly known as a profit or loss), a statement of cash flows (not always required) and the notes that accompany those statements to explain their contents in more detail. A financial report is prepared in accordance with a basis of preparation.
General purpose financial report	A general purpose report is “a financial report intended to meet the information needs common to users who are unable to command the preparation of reports tailored so as to satisfy, specifically, all of their information needs” (SAC 2, Objective of General Purpose Financial Reporting). Reporting entities (SAC 1, Definition of the Reporting Entity) are entities where it is reasonable to expect that users exist who are dependent on general purpose financial reports. Reporting entities must prepare general purpose financial reports. In Australia, a report prepared in accordance with the Australian Accounting Standards is a general purpose financial report.
Special purpose financial report	Non-reporting entities may prepare special purpose financial reports. These are designed to meet the information needs of specific users. In Australia, special purpose financial reports do not comply with all requirements of the Australian Accounting Standards. Some regulators, such as the Australian Securities and Investments Commission (ASIC), set minimum requirements in relation to which aspects of the Australian Accounting Standards must be applied by entities preparing special purpose reports for lodgement with that regulator.

Other types of financial information

Where a full financial report is not required, it is important to be specific about what financial information is required and what basis of preparation is to be used to ensure consistent reporting to users. For example “a statement of income and expenditure in accordance with the accruals basis of accounting” or “a statement of financial position prepared in accordance with Australian Accounting Standards”. If a basis of preparation is not specified then an accompanying note to the financial information setting out the basis of preparation should be requested so that the users can understand the information being presented to them.

APPENDIX 2: Key concepts – assurance terminology

<p>Audit</p>	<p>An audit is a type of assurance engagement (see below for definition) that is designed to provide a higher degree of confidence in the information than a review (see below for definition). It is also known as a reasonable assurance engagement as it provides a reasonable level of assurance. It does not provide absolute assurance. An audit involves a systematic process of obtaining and evaluating evidence about the information to determine if it has been prepared in accordance with suitable criteria. For financial information these criteria may be the Australian Accounting Standards or another framework such as a cash or accruals basis of accounting as circumstances warrant. An audit results in the auditor expressing an opinion on the information to the users that based on their audit, they believe the information is not material misstated. “Audit” is a strictly defined term under the standards issued by the AUASB and should only be used where a reasonable level of assurance is desired.</p> <p>The AUASB Glossary defines an audit or reasonable assurance engagement as “an assurance engagement where the assurance practitioner’s objective is a reduction in assurance engagement risk to an acceptably low level in the circumstances of the assurance engagement as the basis for a positive form of expression of the assurance practitioner’s conclusion”.</p>
<p>Assurance engagement</p>	<p>This is an engagement where the assurance practitioner undertakes a range of processes in order to be able to provide an opinion that the information being provided to users does not contain material errors.</p> <p>The AUASB Glossary defines an assurance engagement as “an engagement in which an assurance practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria”.</p>
<p>Review</p>	<p>A review is another type of assurance engagement that is designed to provide a level of confidence that is lower than an audit. It is also known as a limited assurance engagement as it provides a limited level of assurance. A review also involves a systematic process of obtaining and evaluating evidence about the information however the procedures carried out are generally limited to making enquiries of those involved in preparing the information and applying analytical and other review procedures. After a review, the reviewer expresses a conclusion about whether or not anything has come to their attention that would make them believe that the information is materially misstated. For information that is lower risk, a review may be appropriate and should be specified.</p> <p>The AUASB Glossary defines a review or limited assurance engagement as “an assurance engagement where the assurance practitioner’s objective is a reduction in assurance engagement risk to a level that is acceptable in the circumstances of the assurance engagement but where that risk is a greater than for a reasonable assurance engagement, as the basis for a negative form of expression of the assurance practitioner’s conclusion”.</p>

Compliance engagement	<p>A compliance engagement is one in which the assurance practitioner provides reasonable or limited assurance in relation to an entity's compliance with a set of requirements.</p> <p>An engagement which requires assurance on both financial information and other elements such as compliance with certain legislation is a multi-scope engagement.</p>
Other engagements	<p>The AUASB framework also includes agreed-upon procedures engagements. These engagements are where the entity specifies certain procedures that they wish to have carried out in relation to the information. The practitioner performs the procedures and reports the factual results of the procedures. No assurance is provided, the entity must draw their own conclusions from the factual results of the procedures.</p> <p>The AUASB Glossary defines an agreed-upon procedures engagement as “an engagement in which an auditor is engaged to carry out those procedures of an audit nature to which the auditor and the entity and any appropriate third parties have agreed and to report on factual findings. The recipients of the report form their own conclusions from the report by the auditor. The report is restricted to those parties that have agreed to the procedures to be performed since others, unaware of the reasons for the procedures may misinterpret the results”.</p>
Auditor	<p>A person performing an audit or reasonable assurance engagement in accordance with the standards issued by the AUASB. The term “assurance practitioner” is generally used when the subject matter is non-historical financial information.</p>
Reviewer	<p>A person performing a review or limited assurance engagement in accordance with the standards issued by the AUASB. The term “assurance practitioner” is generally used when the subject matter is non-historical financial information.</p>
Assurance practitioner	<p>A person who provides professional assurance services.</p>

APPENDIX 3: Engagement types and sample opinion wording

Engagement type	Sample opinion
Audit of a general purpose financial report prepared in accordance with the Australian Accounting Standards	In our opinion the financial report presents fairly, in all material respects, the financial position of ABC Entity as at 30 June 20XX and its financial performance and cash flows for the year then ended in accordance with Australian Accounting Standards. (For more examples and full report wording refer to ASA 700 or ASA 800 for special purpose financial reports).
Review of a general purpose financial report prepared in accordance with the Australian Accounting Standards	Based on our review, which is not an audit, nothing has come to our attention that causes us to believe that these financial statements do not present fairly, in all material respects, the financial position of ABC Entity as at 30 June 20XX and its financial performance and cash flows for the year then ended in accordance with Australian Accounting Standards. (For more examples and full report wording refer to ASRE 2400/2410).
Audit of a statement of income and expenditure prepared in accordance with cash receipts and disbursements basis of preparation as determined by management	In our opinion the statement of income and expenditure presents fairly, in all material respects, the income and expenditure of ABC Entity for the year ended 30 September 20XX in accordance with the cash receipts and disbursements basis of accounting as described in Note X. (For more examples and full report wording refer to ASA 805).
Review of a schedule of accounts receivable prepared in accordance with accounting policies	Based on our review, which is not an audit, nothing has come to our attention which causes us to believe that the schedule of accounts receivable of ABC Entity at 31 March 20XX is not prepared, in all material respects, in accordance with the accounting policies as set out in Note X. (For more examples and full report wording refer to ASRE 2405).
Reasonable assurance compliance engagement on compliance with legislation in relation to the operation of a trust account	In our opinion, ABC Entity has complied, in all material respects, with the requirements of the XYZ Act in relation to the operation of their trust account for the year ended 31 December 20XX. (For more examples and full report wording refer to ASAE 3100).
Agreed-upon procedures engagement (in relation to accounts payable)	The procedures were performed solely to assist you in evaluating the accuracy of accounts payable. The procedures performed and the factual findings obtained are as follows: [Table of procedures, factual findings and errors or exceptions identified would follow, for example; We compared [xx] to [yy]. The amounts were the same. We requested confirmation from x% of balances. We received confirmations from all. [zz] disputed the amounts listed].

APPENDIX 4: Additional information

To understand these matters in more detail, you should refer to the standards and frameworks issued by the AASB, AUASB and APESB. If in doubt, you should seek advice from these bodies or one of the professional accounting bodies. Specific documents to refer to include, but are not limited to, the following:

AASB documents (available at aasb.gov.au)

- SAC 1 Definition of the Reporting Entity
- SAC 2 Objective of General Purpose Financial Reporting
- AASB 101 Presentation of Financial Statements

AUASB documents (available at auasb.gov.au)

- AUASB Glossary
- Framework for Assurance Engagements
- Understanding Financial Statement Audits: A Guide for Financial Statement Users
- ASA 210 Agreeing the Terms of Audit Engagements
- ASA 700 Forming an Opinion and Reporting on a Financial Report
- ASA 800 Special Considerations – Audits of Financial Reports Prepared in Accordance with Special Purpose Frameworks
- ASA 805 Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement
- ASRE 2400 Review of a Financial Report Performed by an Assurance Practitioner Who is Not the Auditor of the Entity
- ASRE 2405 Review of Historical Financial Information Other than a Financial Report
- ASRE 2410 Review of a Financial Report Performed by the Independent Auditor of the Entity
- ASAE 3000 Assurance Engagements Other than Audits and Reviews of Historical Financial Information
- ASAE 3100 Compliance Engagements
- ASRS 4400 Agreed-Upon Procedures Engagements to Report Factual Findings
- GS 022 Grant Acquittals and Multi-scope Engagements

APESB documents (available at apesb.org.au)

- APES 110 Code of Ethics for Professional Accountants
- APES 205 Conformity with Accounting Standards
- APES 210 Conformity with Auditing Standards

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