

The Westworth Kemp Review of 2019

Contents

Introduction	1
Key tips for auditors from our 2019 findings	2
The role of the expert witness	3
The theory	3
What we have found in practice	3
Appendix: Resources on changes to accounting standards and examples of financial statements for December 2019	5

Introduction

As I write this year’s newsletter, huge areas of Australia are being ravaged by bushfires and we



express profound gratitude for all those in our community who are facing them on the front line, working to save life and property.

We hope our newsletter finds our readers safe, in good health, refreshed from the holiday season and looking forward to a stimulating 2020.

We would also like to take this opportunity to remind clients and contacts that we moved offices in November (just down the corridor, but it

might as well have been to Mars!) and can now be found at 719/2 York Street. Telephones, email and website remain the same.

The picture on the left shows members of the team christening the new digs (minus the photographer!)

2019 has seen a return to the special purpose financial reporting debate, with different responses to small company reporting being put forward. While elegant in theory, the reporting entity concept has not worked in practice, due to its judgemental nature and a lack of resolve on the part of regulators to test it and to start to set boundaries. We have been involved in matters where special

purpose reports have been prepared and the interests of stakeholders who are less involved in day to day operations have been ignored. Greater certainty will benefit both the preparers and the users of small business reports.

Just before Christmas, the [Brydon report](#) into ways of improving the quality and effectiveness of audit was released in the UK. Its recommendations are addressed at Public Interest Entities and it recommends radical changes to the auditing profession, including separating it from other practice areas to form a new profession of “corporate auditing” with its own qualification, making the audit more informative to users by including more information about the audit in the auditor’s report and introducing the concept of suspicion, in addition to scepticism, into the attributes of an auditor, making the training of auditors more similar to that of forensic accountants. It remains to be seen how this will play out and what impact it will have around the world. Major changes in large jurisdictions overseas tend to filter through to Australia eventually.

Research into audit quality and effectiveness is needed as audit negligence continues to be a large part of our practice. While the directors and management have responsibility for what a company does, auditors are a target for two main reasons: they have to carry insurance and their work is governed by a detailed suite of standards which makes it relatively easy to challenge whether or not that work was up to standard. Furthermore within those standards there is a duty to warn management and those charged with governance of weaknesses that the auditor encounters while doing his or her work.

Key tips for auditors from our 2019 findings

Our main messages from the audit files we have reviewed in 2019 are very basic, but absolutely vital:

- Just because a test is difficult and the evidence is hard to find does not mean you do not have to perform the test. If the test is key to a significant audit area and you are unable to obtain sufficient appropriate audit evidence, you may need to have challenging conversations with the client and ultimately perhaps even modify the audit report. Retreating from the hard conversations and settling for a management letter or a point in the closing report may not be sufficient defence if the company fails. The directors may argue that they were never warned and that the auditors assured them their controls and processes were adequate.
- Merely having a chat with the client does not constitute sufficient appropriate audit evidence. For example, when the client is explaining revenue forecasts that are the basis for the fair value of an asset, is important to consider the validity of those forecasts. Do they make sense in terms of what the company can practically achieve?
- Analytical review can be a really useful test as long as you take time at the outset to carefully consider what you are expecting to find in the review so that you will know when results do not match expectations.
- Clients, particularly those who have not got an accounting background, place great emphasis on the closing report that the auditor gives to the board and/or audit and risk committee. For the recipients of these closing reports, whatever is written in the detail of the report, the

bottom line is whether or not the audit report is qualified (modified). Observations in the closing report as to weaknesses in systems and areas of difficulty in the audit are construed as interesting and instructive, but not a major problem. If the audit report is unmodified, the client is entitled to believe that whatever was found, the financial statements are nevertheless materially correct and the auditor concurred with significant accounting policy choices and estimates. We all know that the directors are responsible for the financial report at law, but non-accountants set great store by the fact that the auditor has given clearance for the accounts to be issued. This can become an area of great danger for the auditor in litigation as the closing report will invariably have touched on the controversial issues that later figure in the litigation.

The role of the expert witness

The theory

For members of the Australian accounting bodies, forensic accounting services are performed under [APES 215](#), Forensic Accounting Services, issued in December 2015 and revised in July 2019, operative from 1 January 2020.

Forensic accountants are bound by the fundamental responsibilities of their professional ethical requirements: to act in the public interest and avoid conflicts of interest, to maintain a level of professional independence commensurate with the type of service being offered, to act with professional competence and due care and to respect confidentiality.

There are two main types of expert witness services, the independent expert and the consulting expert.

- The Expert Witness is independent and is *amicus curiae* (Latin for the friend of the court) and is providing a professional opinion on matters that he or she has been asked about. He or she is not a hired gun for one side of the litigation, but must abide by Court rules and has a paramount duty to the Court which overrides any duty to the client or employer. Expert Witness services are regulated by Section 5 of APES 215.
- The role of Expert Witness must be distinguished from other forensic accounting work, including the role of the consulting expert, also known as the 'dirty' expert. The consulting expert works directly for one party in the litigation, analysing the underlying data and helping the lawyers frame the case in the case of the plaintiffs, or looking for support for the other point of view in the case of the defence.

A further role performed by accountants is that of the lay witness, but lay witnesses are generally accountants working within one of the clients involved in the litigation and are contributing their account of what actually happened in the matter, or in legal speak, evidence as to fact.

What we have found in practice

In the seven years that Westworth Kemp Pty Ltd has been providing expert opinions, we have worked for a wide variety of participants in the litigation machine:

- Regulators in Australia and New Zealand;

- A variety of defendants, including:
 - Audit firms of all sizes and their insurers;
 - Directors and their insurers; and
 - Individual auditors facing regulatory action;
- A variety of plaintiffs, including:
 - shareholder/investors in class actions;
 - finance providers; and
 - liquidators and other administrators; and
- Litigation funders exploring the merits of a potential case.

As well as matters involving audit negligence and other professional conduct, we find our skills are needed in contract disputes where the terms of accounting standards are key to interpreting the contract and also in continuous disclosure actions.

We see ourselves as a bit like a barrister – expert and independent, able to be briefed by anyone with a problem within our sphere of expertise, plaintiff, defendant or regulator. We look at each issue on its merits and analyse the relevant standards and other materials. The aspects of accounting and auditing that come to litigation are almost always highly judgemental – if the answer was obvious, there would be no need to litigate.

Much of what we do never becomes public as the vast majority of cases settle before they come to court. Sometimes a lawyer rings and asks us for our view on a situation and we never hear from them again! Sometimes we are engaged and we find ourselves in the position of being unable to argue in support of a particular behaviour or accounting choice and have to advise the client to focus on nexus and causation.

The wonderful thing about life as a forensic accountant is that we never know what the next assignment will hold and we have been privileged to work with some exceptionally talented professionals in the years that we have been in existence.

Appendix: Resources on changes to accounting standards and examples of financial statements for December 2019

There is a wealth of information freely available on various websites relating to changes in standards, in addition to the official information on the AASB's site. These updates give accountants a way in to the standard and make it easier to then apply the detail to the circumstances of their clients.

Many websites also contain specimen financial reports, again free to download, which can assist with drafting disclosures in respect of new and existing standards. While an example may not exactly fit the entity's circumstances, it provides a starting point for drafting something specifically tailored to the its needs.

As well as the international and local standards and ASIC materials which are well publicised, it is worth keeping an eye on agenda decisions of the IASB's Interpretations Committee. These are now easier to find thanks to the recent upgrade of IASB website. They can now be found at <http://www.ifrs.org/supporting-implementation/how-the-ifrs-interpretations-committee-helps-implementation/#agendadecisions> as well as the Deloitte IAS Plus site which has them hyperlinked by standard - <https://www.iasplus.com/en/projects/not-added>, and the IASB's hard copy "Green Book".

Thank you to CAANZ who compiled this hyperlinked resource on the following link <http://send.charteredaccountantsanz.com/l6JYX000uUkJ2C4650q0z0R>. A copy of the page without hyperlinks is reproduced below.

Illustrative financial reports December 2019

Where can I find illustrative financial reports for the December 2019 financial year end?

There are various illustrative financial statements available, most of which are available for free. Third party publications listed below should not be regarded as an endorsement by Chartered Accountants Australia and New Zealand.

Australia

- CA ANZ [Enhancing not-for-profit reporting](#) guide (example in Australia Part B, Chapter 4)
- [CaseWare](#)
- [Deloitte](#)
- [Grant Thornton](#)
- [IFRS System](#) (free registration required)
- [KPMG](#)
- Thomson Reuters XYZ Model Financial Accounts – either [borrow](#) from the CA ANZ Library or [purchase](#) directly

New Zealand

- [Audit New Zealand](#) (public sector PBEs)
- [BDO](#)
- [CA ANZ illustrative financial statements](#) for *A Special Purpose Financial Reporting Framework for use by For-Profit Entities*
- [Grant Thornton](#)
- [PwC](#)
- Thomson Reuters XYZ Model Financial Statements – either [borrow](#) from the CA ANZ Library or [purchase](#) directly
- XRB [templates](#) for Tier 3 and Tier 4 PBE Simple Format Reporting Standards

International

- [BDO](#)
- [Deloitte](#)
- [EY](#)
- [KPMG](#)