

Parliamentary Joint Committee on Corporations and Financial Services
Regulation of Auditing

Answers to questions on notice from 7 February 2020
Accounting Professional and Ethical Standards Board

2. QUESTION – Guidance on Materiality (pages 3-4 of the Hansard)

Senator WHISH-WILSON: I put to you, having worked in this industry—not in the auditing industry but in the financial industry—that the word 'material' is very subjective. It could simply be how people are remunerated within those firms. It could be their earnings' growth for a particular division within a firm. 'Material' could be defined in lots of ways, and I'd be very concerned if it was left to the company itself to decide what was material or not material. Do you have any suggestions for benchmarks or prescriptions around that?

Ms Milne: Can I suggest we give you a more detailed answer on notice?

Senator WHISH-WILSON: Okay.

Ms Milne: I think that might be of more assistance to you.

ANSWER:

Materiality in the context of financial reporting is addressed within the Framework for the Preparation and Presentation of Financial Statements, published by the Australian Accounting Standards Board.

Chapter 3 *Qualitative Characteristics of useful financial information*, states at paragraph QC11:

Information is material if omitting it or misstating it could influence decisions that users make on the basis of financial information about a specific reporting entity. In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report. Consequently, the Board cannot specify a uniform quantitative threshold for materiality or predetermine what could be material in a particular situation.

Materiality in the context of Professional and Ethical Standards is addressed at Paragraph 600.5 A3 of APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)*, which provides guidance on materiality in relation to Financial Statements. The paragraph states:

The concept of materiality in relation to an audit is addressed in Auditing and Assurance Standard [ASA 320, Materiality in Planning and Performing an Audit \(Compiled\)](#), and in relation to a review in [ASRE 2400 Review of a Financial Report Performed by an Assurance Practitioner Who is Not the Auditor of the Entity](#). The determination of materiality involves the exercise of professional judgement and is impacted by both quantitative and qualitative factors. It is also affected by perceptions of the financial information needs of users.

Additionally, the preface to the Independence Standards in APES 110 states:

With regard to the use of the words "material" and "materiality" in Parts 4A and 4B, it is not possible to provide a definition that covers all circumstances where either word is used. In assessing materiality, a Member in Public Practice or a Firm shall consider both the qualitative and quantitative aspects of the matter under consideration which might have, or be seen to have, an adverse effect on the objectivity of the Member or Firm.

ASA 320, which is issued by the Australian Auditing and Assurance Standards Board, contains an extensive discussion of materiality which commences at paragraph 2 with the statements:

Financial reporting frameworks often discuss the concept of materiality in the context of the preparation and presentation of a financial report. Although financial reporting frameworks may discuss materiality in different terms, they generally explain that:

- *Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial report;*
- *Judgements about materiality are made in light of surrounding circumstances, and are affected by the size or nature of a misstatement, or a combination of both; and*
- *Judgements about matters that are material to users of the financial report are based on a consideration of the common financial information needs of users as a group. The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered.*

It may be of interest that AASB 1031 *Materiality* contained indicative benchmarks for materiality. AASB 1031 is no longer operative; it applied to reporting periods that commenced prior to 1 July 2015.