



Submission to the Regulation of Auditing in Australia

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On Behalf of: The Institute of Certified Management Accountants

Whilst all of the listed [Terms of Reference](#) (TOR) would make for interesting in-depth investigation, the [Institute of Certified Management Accountants](#), would like to raise issues pertaining to:

- TOR 4- on audit quality, including valuations of intangible assets;
- TOR 8- the effectiveness and appropriateness of legislation, regulation and licensing, and
- TOR 10 - the adequacy and performance of regulatory, standards, disciplinary and other bodies.

In this submission we will briefly demonstrate that these three TORs are significantly interlinked, and require urgent review by Parliament.

TOR 4, 8 and 10.

The audit report of financial statements uses the term 'true and fair' to express the condition that financial statements are truly prepared and fairly presented in accordance with the prescribed accounting standards. The problem is that it is the Auditors themselves who issue the accounting standards!

This is done by stacking the Boards of the Standard setting bodies by the auditors themselves, especially members of the Big-4, and thereby controlling the development, production and modification of accounting and auditing standards. Then they do an audit in accordance with the very standards that they issued.

Using a university analogy, it's like the Big-4 are setting the subject syllabus, preparing the exam paper, writing the answers to the exam and finally giving a grade. If there is a complaint, they are the adjudicators of the quality of their own work!

It is time for an independent body, such as Parliament, to be responsible for setting accounting standards.

A related issue is that preparing accounts based on IFRSs results in flawed financial statements and meaningless and fictitious audit reports.

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In knowledge economy companies such as Microsoft, Amazon and Google, the auditors book valuations are over 5-10 times less than market valuations. At Microsoft, this is a difference in value of US\$686 Billion in 2018! Against market values, all IFRS valuations would get a fail grade, but Auditors are certifying them as 'True and Fair'.

The outdated belief that the addition of all fair-value of individual assets (less liabilities) will give an accurate reflection of the state of affairs of the company is based on an outdated economic paradigm of a largely industrial economy, where tangible assets were the engines of growth. The IFRS based values are totally flawed in today's knowledge economy; as most intangible assets are left out, and an organisation's capability values completely ignored. Regardless, it is not necessary as this valuation can be provided by the market at any time. Asking auditors to provide a value is a costly and, ultimately, meaningless task.

Legislation should be passed to reduce the scope of the traditional statutory financial audit to only reporting if transactions are correctly recorded and that the financial statements are prepared and fairly presented in accordance with Generally Accepted Accounting Principles (GAAP).

TOR 12 - any other related matter.

If the traditional statutory audit is limited in scope by Parliament, one must consider what should replace it for proper governance of organisations. It is strongly recommended that the replacement should be a statutory audit of expected future performance and how it affects current value, and not an audit of past performance and meaningless book values. Such audits are called 'Strategic Audits'.

A strategic audit is far different from the common perception of a financial audit. It is a continuous evaluation of all the strategic functions of any success-seeking firm. Numerous components (e.g. stakeholder audit, customer satisfaction audit, etc.) make up the totality of the strategic audit, although the scope of each component audit will vary depending on the organisation. Most shareholders will want strategic auditors to perform, at a minimum: (a) stakeholder audits; (b) information security audits; (c) environmental audits; (d) corporate ethics audits, and (e) leadership audits. The skill-set strategic auditors would require will be very different from those required by those who audit the past - based on flawed accounting standards.

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References:

1. [The Silence of the Auditors](#)
2. [Auditors to the Slaughter: Why Audit Opinions are 'Untrue' and 'Unfair'](#)