

ACCOUNTANCY FUTURES

Value regained: restoring the role of audit in society

ROUND-TABLE DISCUSSIONS IN ZAMBIA, 24 MAY 2010

ABOUT ACCA

ACCA (the Association of Chartered Certified Accountants) is the global body for professional accountants. We aim to offer business-relevant, first-choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management.

Founded in 1904, ACCA has consistently held unique core values: opportunity, diversity, innovation, integrity and accountability. We believe that accountants bring value to economies at all stages of their development. We seek to develop capacity in the profession and encourage the adoption of global standards. Our values are aligned to the needs of employers in all sectors and we ensure that, through our qualifications, we prepare accountants for business. We seek to open up the profession to people of all backgrounds and remove artificial barriers, innovating our qualifications and their delivery to meet the diverse needs of trainee professionals and their employers.

We support our 140,000 members and 404,000 students in 170 countries, helping them to develop successful careers in accounting and business, based on the skills required by employers. We work through a network of 83 offices and centres and more than 8,000 Approved Employers worldwide, who provide high standards of employee learning and development. Through our public interest remit, we promote appropriate regulation of accounting and conduct relevant research to ensure accountancy continues to grow in reputation and influence.

ABOUT ACCOUNTANCY FUTURES

The economic, political and environmental climate has exposed shortcomings in the way public policy and regulation have developed in areas such as financial regulation, financial reporting, corporate transparency, climate change and assurance provision.

In response to the challenges presented to the accountancy profession by this new business environment, ACCA's *Accountancy Futures* programme has four areas of focus – access to finance, audit and society, carbon accounting, and narrative reporting. Through research, comment and events ACCA will contribute to the forward agenda of the international profession, business and society at large.

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This report summarises one of an international series of round-table discussions hosted by ACCA and designed to generate debate, new ideas and recommendations about the future of audit.

In 2010, ACCA chose 'audit and society' as one of four critical issues which it is addressing under its '*Accountancy Futures*' programme.

ACCA believes firmly that audit has a key role to play in society as a source of public confidence in financial reporting but notes that there is currently little published research which seeks to demonstrate its value. By bringing together a wide range of market participants, we hope to help establish ways in which the value of audit can be enhanced for all stakeholders.

FURTHER INFORMATION

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PURPOSE AND OBJECTIVES FOR THE ROUND TABLE

This is a report on the round-table meeting held by ACCA on 24 May 2010 in Lusaka, Zambia entitled 'The Future of Audit'. With a backdrop of ongoing global financial uncertainty, the conference covered the following themes:

- Value regained: restoring the role of audit in society
- The value and benefits of audit to national development
- Bridging the gap: is audit meeting industry and business expectations?
- Auditor independence: the key safeguards
- The role of the Zambian Institute of Chartered Accountants (ZICA) in the regulation of the accountancy profession in Zambia.

To analyse these issues, ACCA invited senior representatives from audit firms, industry, and government. The role of ZICA in regulating accountants in public practice and industry was also discussed. This supervisory role is carried out through the Accountancy Act 2008, which was passed by Parliament the same year.

The main objective of the conference was to obtain informed insights from participants about the role of audit, and to propose recommendations to enhance the value of audit in Zambia.

The conference was attended by: Helen Brand, ACCA chief executive; Chileshe Kampwepe FCCA, the deputy minister of finance and national planning; Dr Tukiya Kankasa Mabula, the deputy governor for administration of Bank of Zambia; Anna O. Chifungula, the auditor general of Zambia who sent a representative; Chansa Chiteba, the director of standards and regulations of ZICA; and representatives from audit firms, CEOs, accountants in industry and other stakeholders.

KEY OBSERVATIONS AND RECOMMENDATIONS

There is a need for the accountancy profession to address expanding the scope of audit to encompass an examination of internal controls, risk management and corporate governance. Other points made were as follows.

- The accountancy profession should consider co-opting other experts to complement their skills in the area of risk management.
- A specific report needs to be given in the audit report of a company about its business risk.
- Corporate entities should set up risk management units.
- Audit firms should invest in the training of their staff so that they can start better understanding risk management.
- Due to the continuous development in derivative products, financial services auditors will need new skills to keep pace with the advancement of new products on the market.
- There is also a need to develop different ground rules for audit in SME sector. This is because the focus of the International audit standards is very much on the audit of large companies.
- An opinion on the going concern of a firm should be included in the auditor's statement.
- External auditors should speak regularly with internal auditors and the audit committees. Management should take note of reports by the internal audit department.

- Accountants should make accounting information more understandable and user-friendly to CEOs and non-accountants.
- The key role of auditors should be to give an opinion on whether the financial statements give a true and fair view of the state of affairs of the company and whether the business is a going concern.
- Companies and audit committees should be sensitive to external perceptions that audit independence could be compromised by substantial non-audit fees. While companies should feel free to use their auditors for non-audit services, they should fully disclose the reasons for choosing incumbent auditors for non-audit services where fees are significant.
- Students should go through an article arrangement, where they will be required to gain adequate work experience before obtaining the ZICA qualification.

VALUE REGAINED: RESTORING THE ROLE OF AUDIT IN SOCIETY

Speaking under the theme 'Value Regained: Restoring the Role of Audit in Society', Helen Brand commended the government of the republic of Zambia for its good fiscal discipline and the legislative changes that have seen the introduction of audit committees in ministries, provinces and spending agencies to ensure that there is accountability and eradication of abuse of public resources.

These actions, she said, will enhance the image of Zambia as a good investment destination. ZICA and ACCA have had some involvement in this process and are keen to assist whenever asked to do so.

Helen Brand explained that, globally, the role of audit is under heightened scrutiny. The unprecedented global financial upheavals of the past three years have seen commentators in many countries question the value of auditing to companies.

Given that background, ACCA believes that it is vital for the accountancy profession to re-examine the role of audit and to question whether a sufficiently strong case is being put forward to show the benefits that audit can provide to businesses, the economy and society. Audit plays a key role in providing confidence to the public in the financial reports but currently there is little published research that demonstrates the value of auditing in promoting business trust.

The financial crisis, however, has led many commentators to ask whether the audit model is damaged. The UK's Treasury Select Committee inquiry into the banking crisis asked serious questions as to whether auditors were looking at the right things when carrying out their audits.

The view of ACCA is that the audit model is not broken. An independent audit provides investors with a high level of assurance to the credibility of the financial statements and of the underlying transactions through the audit opinion. Without the audit, confidence in the viability of major companies would disappear and their cost of capital would rocket.

This view is supported by a major recent research project carried out in Europe by Maastricht University,¹ which gathered the views of 200 market participants. It found that CFOs, and audit committee members were satisfied that the audit met their key expectations and believed it to be a useful activity. Financial analysts also said that the audit was valuable as it increased their confidence in, and reliance on, financial statements.

Similar conclusions were reached by a study carried out by ACCA for the Singapore business regulator ACRA.² Interviews with audit committee chairmen found that they valued the audit, particularly for the increased confidence it brought them that the financial statements were in good order. They also appreciated the extra insights that auditors brought them about the accounting procedures and financial processes of the company.

Under auditing standards auditors communicate with regulatory bodies where they come across information which has a bearing on their supervisory activities, and are separately required by law to disclose information on clients' affairs that they suspect may be related to financial crime.

Banks and credit reference agencies use audits as a key indicator of companies' financial strength. The audit function in its current state can be developed further in order to benefit its various stakeholders and the accountancy profession itself.

One of the lessons to be learned from the current financial crisis is the danger of focusing on a narrow measure of compliance, and failure to give the stakeholders the bigger picture.

The view that currently auditors perform their role competently and professionally does not mean that the nature of the audit function should remain as it is. There is a need for auditors to come to terms with more timely reporting as this issue has come up in several roundtable meetings that ACCA has held, internationally.

As the environment in which auditors are operating is constantly evolving it is logical and inevitable that the nature of the audit evolve with it.

The focus of the audit must remain that of giving an expert opinion on whether the 'true and fair' test is satisfied.

This opinion is arrived at following compliance with procedures specified in auditing standards. The scope of the audit must also continue to give assurance that financial statements comply with fundamental accounting principles; that the entity is a going concern; the financial statements agree with the underlying accounting records and that internal controls are adequate.

But the problem still exists of companies failing after receiving unqualified audit reports. As the UK Parliament's Treasury Select Committee said 'even if individual corporate failures do not themselves mean that audit were deficient, it does tend to suggest that the audit process can result in a sort of tunnel vision, where the big picture that shareholders want to see is lost in a sea of details and regulatory disclosures'.

ACCA suggests that, to meet stakeholders' needs, the scope of the audit could be usefully expanded to encompass an examination of internal controls, risk management and corporate governance processes. Such matters could be reported via a separate stand-alone report.

For auditors to review and comment on the assumptions underlying the company's chosen business model would be a radical addition to the range of auditors' responsibilities. The experience of the financial crisis suggests that this is a very legitimate area of interest for investors, market analysts and regulators alike – that the discipline of rigorous external review could even help to save some companies from their own miscalculations and excesses.

1. Maastricht Research Centre (MARC), *The Value of Audit*, Maastricht University, March 2010.

2. ACCA, *The Value of Audit: Views from Audit Committee Chairmen*, commissioned by the Accounting and Corporate Regulatory Authority (ACRA), Singapore, July 2010.

The expansion in the audit scope beyond the traditional template may well require auditors to acquire new skills and even co-opt experts from other fields. This will inevitably lead to an increase in audit costs. It is also important to note that this increase in scope will raise expectations of what audit involves, which will naturally cause a heightened exposure to liability on the part of the auditors should those expectations not be met.

There is also a need to develop different ground rules for audit in the SME sector. This is because the focus of the International audit standards is very much on the audit of large companies and the standards are becoming increasingly more detailed and complex in order to curb high-profile business failures. We may have to take a leaf from standard setters in the financial reporting field who have come up with separate standards for the SME sector.

Bridging the gap: is audit meeting industry and business expectation?

The deputy governor for administration of the Bank of Zambia, Dr Tukiya Kankasa Mabula, cautioned accountants and auditors that the global financial crisis which begun in late 2007 had brought them under increased public scrutiny due to the failures in governance and regulation of financial institutions. Following the global financial crisis key issues need to be addressed, including:

- whether the board of directors fully understood the business models that their companies were using, or fully appreciated the risks involved
- whether regulators failed or, worse still, if they were compromised by the excesses of industries that they were required to regulate
- whether credit rating agencies were at fault, and
- to what extent short-term performance bonuses paid to top management encouraged greed, excessive risk taking and/or creative accounting.
- Dr Mabula added a further, crucial, question: where were the auditors? The unqualified audit reports given to some of the collapsed major listed organisations represented an indication to investors that the directors' reports and financial statements reflected a "true and fair view" of the performance and state of affairs of the organisations concerned.

He said the situation was similar to that which existed in Zambia in the 1990s, where financial statements of some failed banks were issued with unqualified audit opinions, when, with the benefit of hindsight at least, danger signs should have been noticed by auditors. With this in mind, is it correct to conclude that the audit model has failed?

To counter auditing and accounting problems, there has in recent years been a range of regulatory and legislative measures taken around the world, such as the US Sarbanes–Oxley Act (2002) and the full adoption of International Financial Reporting Standards (IFRS). Zambia itself has seen enactment of the Accountants Act (2008), and establishing of the Audit Quality and Monitoring Programme under ZICA which aims at improving the quality of professional work throughout the audit profession in Zambia.

But the current crisis has shown that questions still need to be answered. To kick-start the debate Dr Mabula invited the conference to consider the following questions.

- Are auditors perceived to be more reactionary than proactive to emerging risks and challenges?
- Is the issue of fraud and illegal acts receiving sufficient audit attention?
- Have auditors' independence been compromised through excessive remuneration and audit fees?
- Has the issue of provision of non-audit services and size of these fees compared with the audit fees been fully addressed? Does this compromise auditors' independence?
- Are there constraints in the provision of audit services especially for SME's using the current auditing standards and should there be a threshold for mandatory audits of institutions?
- Delegates agreed that there had been lapses in audit work, as exemplified by unqualified opinions that were issued to banks in Zambia that subsequently collapsed. Some believed that the offering of non-audit services by auditors to audit clients had compromised their independence.

There was also a strong view expressed that fear of losing re-appointment had discouraged some auditors from qualifying the financial statements. Others, notably end-users, felt that audit fees are too high for many clients and that accounting language and financial statements were now too complex for non-experts to understand.

Placing the discussion in a wider context, Dr Mabula pointed out that the Zambian economy had performed well in the face of the global crisis. The economy grew by 6.3% in 2009 compared to 5.7% in 2008. Inflation closed the year (2009) at 9.9% (December): this was in line with the year-end prediction of 10%, compared to a high of 16.6% in 2008. The global economic crisis had though led to low international commodity prices that in turn led to a significant slowdown in the country's foreign exchange earnings. This invariably led to the depreciation of the Zambian Kwacha against major world currencies.

It is clear that if audit is to play a key role in helping the national and international economy recover by increasing confidence in business and financial statements, then the concerns raised above – whether perception or reality – need to be actively addressed by the profession.

Auditor independence: the key safeguards

The auditor general of Zambia, Ms Ana O. Chifungula, informed the participants that the independence of auditors is essentially an attitude of mind characterised by integrity and an effective approach to the audit process. The concept requires auditors to carry out their work freely and in an objective manner.

The purpose of an audit is to enhance the credibility of the financial statements by providing written reasonable assurance from an independent source that they present a true and fair view in accordance with accounting standards.

This objective will not be realised if users of the audit report believe that other parties such as managers and directors may have influenced the auditors. Apart from technical competence, auditor independence is the most important factor in establishing the credibility of the audit opinion. A number of high profile accounting scandals have negatively impacted on the public perception of audit independence.

To help ensure auditor independence, Ms Chifungula pointed to several steps that had been taken internationally and which should be addressed by Zambia.

- Independent assessment: a review of audit control procedures in audit firms could be introduced to ensure that external audits are carried out with utmost professionalism and independence at all times. In the US and Europe, such independent oversight of audit firms is obligatory.
- Audit committees: increasing numbers of countries are beginning to require listed companies to have audit committees. A group of non-executive directors from within the company are appointed to deal with the external auditors and to provide an objective view on all aspects of the audit such as internal controls and level of audit fees. In Zambia the Public Finance Act has a provision that require government ministries and quasi government organisations to have such committees.
- Conflicts of interest: in many countries legislation has been introduced which bars auditing firms holding shares in client companies.
- Professional scepticism and independent questioning are qualities and skills which should be engendered in auditors by their training. It is this that represents the true value of audit to business. Systems should also be in place which re-inforce those natural qualities and support auditor independence. It is up to the accountancy profession to ensure that it addresses these issues.

Audit practice in Zambia

Chansa Chiteba, the director, standards and regulations, of the Zambia Institute of Chartered Accountants (ZICA), gave an outline of the formation of ZICA, the accountancy profession in Zambia, public practice and the regulation of audit practice.

ZICA was established under the Accountants Act of 1982. The Accountants Act, No.13 of 2008, repealed this Act. The mandate of ZICA is as follows.

- Regulate the accountancy profession
- Regulate the education and training of accountants
- Set ethical, auditing and accounting standards
- Investigate disclosures made in the public interest.

A council headed by a president runs ZICA. The day-to-day administration work of ZICA is run by the secretary and chief executive assisted by a management team.

The Accountants Act states the requirements that a person ought to fulfil to be eligible to be employed or to practice as an accountant in Zambia. This is done by applying to ZICA in the prescribed manner and form and upon payment of the prescribed fee.

As at December 2009 the following was the composition of the accountancy profession in Zambia.

Membership

- Fellows 634
- Associates 653
- Licentiates 917
- Technicians 1,402.

Practising members

- Full audit 118
- Non-audit 26.

The Act clearly defines what an audit is, who is an auditor and what public practice is. The Act also spells out the eligibility for one to obtain a full audit certificate and a non-audit certificate.

In order to monitor the quality of work of audit firms ZICA monitors and enforces the Accountants Act by analysing practitioners' annual returns and by carrying out monitoring visits either by itself or through its appointed agents.

ACKNOWLEDGMENTS

ACCA wishes to acknowledge the valuable contributions made by the resource persons, moderators and delegates during the round-table meeting on the 'Future of Audit' held at Taj Pamodzi hotel in Lusaka, Zambia on 24 May 2010.

Resource persons

- Hon Chileshe Kapwepwe, deputy minister of finance and national planning, guest of honour
- Dr Tukiya Kankasa Mabula, deputy governor for administration, Bank of Zambia
- Anna O. Chifungula, auditor general of Zambia
- Chansa Chiteba, director of standards and regulations, ZICA

Moderators

- Chisanga Chungu, senior partner, Deloitte and Touche
- Richard Mazombwe, consultant (former senior partner, PwC)

Delegates who contributed to the discussions

- Mary Ncube, chairperson, Stanbic Bank Plc
- Chitalu Mwenya Pythias, president, Institute of Internal Auditors
- John Cruickshank, consultant
- Kiran Naik, managing partner, Mores Rowland
- Charity Lumpa, managing director, ECO Bank Zambia Ltd
- Beatrice Nkanza, director general, Lusaka Stock Exchange
- Victoria Silutongwe, chief executive officer, Institute of Directors
- Stanley Zingani Phiri, director general, NAPSA
- Hastings Mtine, senior partner, KPMG

- Bernard Kaminsa Mwela, managing partner, George Baison & Obed
- Yejju Gouthama Rao, executive director, Zambia Centre for Accountancy Studies (ZCAS)
- Richard Phiri, deputy managing director, Investrust Bank Plc
- Boniface Muswilwa Chitambala, finance director, University of Zambia
- Dev Haman, chief internal auditor, COMESA
- Wambulawae Inonge, chief internal auditor, Zambia Revenue Authority
- Andrew Sibale, deputy controller, internal audit, Ministry of Finance and National Planning
- Francis Kunda, representative, Zambia Chamber of Commerce and Industry (ZACCI)
- Nambwenga Kauseni, head of finance, Zambia Farmers Union
- George Mubipe, partner, George Baison & Obed
- Ngenda Situmbeko, partner, AIKNS Consulting Ltd
- Rodgers Nyirenda, accountant, MTN Zambia
- Edward Kabwe, director of finance and administration, Medical Stores
- Zaliwe Sali Chibeza Nyoni, member, Institute of Internal Auditors
- Malukutilla Emmanuel, senior auditor, Bank of Zambia
- Kangwa Chileshe, accountant, Cavmnot Capital Bank
- Stanley Zingani Phiri, managing director, National Pension Scheme Authority
- Peter Zulu, internal auditor, Standard Chartered Bank

- Isaac Kamwimba, accountant, Pensions and Insurance Authority
- Gabriel Banda, audit manager, Moores Rowland
- Isaac Phiri, director, Zambia Business Tuition Centre
- Rodrick Chibuye, accountant, Intermarket Banking Corporation
- Andrew Sibale, deputy controller of audits, Ministry of Finance
- Musawa Niza Gondwe, internal auditor, Standard Chartered Bank
- Kabaye Mwale, accountant, Zambia Revenue Authority
- Mambwe Kaenga, director, monitoring unit, Zambia Revenue Authority
- Gilbert Muyalwa, consultant, GSM Associates
- Kelvin Kaluba, chief internal auditor, Zambezi River Authority
- Bathel Mwiinde, accountant, Ministry of Home Affairs
- Chrispin Daka, partner, BDO Chartered Accountants
- Marsha Thurairatnam, partner, BDO Chartered Accountants
- Boniface Mwamelo, internal audit director, MTN Zambia
- Darwin Shinde, chief internal auditor, Development Bank of Zambia
- Mwila Munkanta, principal auditor, Office of the Auditor General
- Mokaya Kennedy, BDO Zambia Audit Services
- Lubemba Joseph, consultant, National Institute for Public Administration
- Felix Sinkala, finance manager, Bank of Zambia
- Mbeluko Phir, finance manager, Zambia Development Agency
- Linda Nkomo, finance director, MTN Zambia
- Ernest Sigande, internal auditor, Zambia Revenue Authority
- Jack Sievu, consultant, Corporate Services Bureau
- McDonald Chilepa, consultant, Corporate Services Bureau

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