KPMG

Key Audit Matters

Auditor's report snapshot

8 September 2017

June 2017 was the third significant period end where NZX listed entities had to issue new style audit reports including Key Audit Matters (KAMs). This snapshot provides insights into those KAMs and emerging trends in the new style reporting. Below are the themes from the 49 audit reports for listed entities which were available at the time of the publication.

Reports by industry

Energy & Natural Resources 7

Financial Services 6

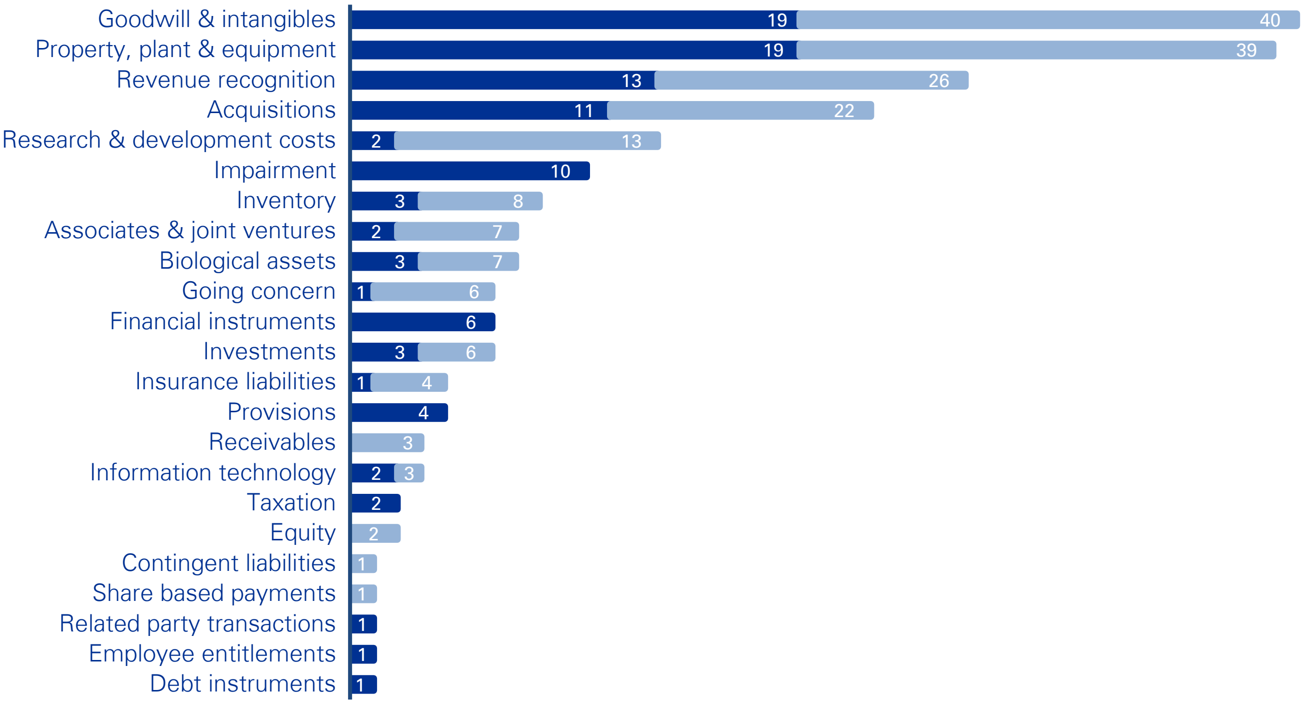
Technology, Media & Telecommunications 7

Corporates 16

Agribusiness 7

Infrastructure, Healthcare & Government 6

KAMs by topic



The above dark blue bars show the number of KAMs reported in audit reports released since April 2017. The light blue bars show the cumulative KAMs reported in the audit reports that have been released to the NZX since December 2016.

KAM trends

- As with March 2017, Goodwill and Intangibles, Property, Plant and Equipment (PPE), Revenue Recognition and Acquisitions remain to be the most reported KAMs. For the June 2017 period, these made up 68% of all KAMs.
- While the top 4 KAMs remain unchanged, the June period saw a number of new KAM topics being reported. KAMs relating to Impairment, Financial Instruments, Provisions, Taxation, Related Party Transactions, Employee Entitlements and Debt Instruments were included for the first time within the audit reports. While half of these new KAM topics only had one KAM each (as seen in the graph above) the other half had a significant amount of KAMs.
- The June period also saw an increase in entities reporting in the Energy and Natural Resources (ENR) industry and in the Agribusiness industry. When compared to the December 2016 and March 2017 periods, the number of entities reporting under these two industries has nearly doubled. The number of KAM reports for all other industries remained relatively consistent. See the *Industry deep dive* section for further analysis of the ENR industry.

Other key statistics

Included Materiality | Included Scoping | Included Findings | Average pages per report | Average KAMs per report

Key statistics by audit firm

Under ISA (NZ) 701, the inclusion of Findings within the audit report is optional and is at the auditor's discretion. Including Materiality and Scoping in the audit report is not contemplated by ISA (NZ) 701, but is a feature of the equivalent UK standard. These three topics are being adopted differently between audit firms. The following table highlights statistics by firm for April to June 2017 year-ends. As seen below, PwC include Materiality, Scoping and Findings in every instance, while EY do not include these in any reports. KPMG, Deloitte and the 'Other' firms report on these in some instances, tailoring these disclosures to be most relevant for each audit.

Firm	Number of reports issued	Percent reporting Materiality	Percent reporting Scoping	Percent Reporting Findings
PwC	14	100%	100%	100%
KPMG	12	83%	17%	58%
Deloitte	9	89%	0%	22%
EY	9	0%	0%	0%
Others*	5	20%	40%	0%

* Others include Australian audit firms where the entity is dual listed on the NZX and ASX, and the audit reports have been prepared under the Australian Auditing Standards.

Note: this is KPMG's assessment of of the 49 reports issued in the June period and what they included.

Industry deep dive – Energy and Natural Resources

- As mentioned above, this June period saw more ENR entities reporting KAMs than any other period. There were a total of 17 KAMs reported across the seven ENR entities.
- The most commonly reported KAM within ENR related to PPE, highlighting the importance of PPE assets within the industry and the significant amount of effort auditors spend on these items.
- ENR is responsible for almost 50% of the newly reported Impairment and Financial Instruments KAMs (40% and 50% respectively). KAMs relating to Impairment are focused on assessing the carrying value of assets other than Goodwill and Intangibles, which are often large balance sheet items with central importance to the entity. Those KAMs relating to Financial Instruments focused on items such as forward foreign currency swaps, interest rates swaps and electricity derivatives. Electricity derivatives are unique to the ENR industry and often require significant auditor attention due to the complex nature of these instruments.
- Also included within ENR were three KAMs relating to Acquisitions. This reflects the dynamic nature of the industry, which often has to innovate and make key strategic decisions to stay competitive in the market. These acquisitions often reflect large transactions which are multifaceted and complex.
- Interestingly, there were no KAMs relating to Goodwill and Intangibles and only one KAM relating to Revenue Recognition. This is unique for ENR as these KAMs are within the top 4 KAMs across all other industries.
- Of the seven ENR sector reports, six included Materiality yet only three included Findings.
- Three of the seven entities are audited by firms on behalf of the OAG, however the reports appear to follow each firm's standard approach (as opposed to an OAG approach to KAMs).
- One ENR report took a different approach by using the strategic direction of the entity as the basis for their KAMs. This allowed the auditor to show their clear understanding of the entity, and how the direction impacts the audit (see more under *Other Observations* below).

Other observations on the auditor's report

- For the first time, we saw two audit reports where the KAMs were linked to either the entity's strategic goals (as discussed under the ENR Industry Deep Dive), or wider macro-economic factors impacting the entity. These KAMs provide a broader picture of the challenges faced by these entities and the impact these have on the audit. This illustrates the dynamic nature of an audit, and shows that auditors look beyond just what is in the financial statements.
- The way in which Findings are included in audit reports, and the detail provided, seems to be changing over time. Some reports have provided detailed findings by audit procedure, whilst others include a single statement about the overall findings by KAM. ISA (NZ) 701 precludes auditors from implying discrete opinions on separate elements of the financial statements. Given most audit reports provide a 'clean' or unmodified opinion (that the financial statement as a whole are free from material misstatement), including findings gives the opportunity for auditors to provide greater transparency about their audit work.
- Whilst the average number of KAMs per report increased from 2 at March to 2.1 at June, there are still varying number of KAMs being presented. 14 reports included only one KAM, while we saw one report with six KAMs. The average number of pages has also reduced from 4.4 to 4.0 which could indicate auditors are improving their ability to be more succinct when describing KAMs.
- Similar to March, there was only one report which included a Material Uncertainty Relating to Going Concern (MURGC). There was also one report which had Going Concern as a KAM, but not a MURGC. These two reports illustrate the variation in approach and complexity of addressing issues that the inclusion of KAMs has provided.
- In accordance with ISA (NZ) 720, auditors are now required to report on "Other Information". Other Information is defined as financial or non-financial information (other than the financial statements and auditor's report thereon) which has been included in the entities annual report. Of the 49 audit reports reviewed, 32 reported that the auditors had obtained all of the Other Information. Of the 32, none had any issues to report.
- June saw a banking audit report produced which was seven pages long. This is due to the RBNZ rules which require the audit report to also include assurance on certain supplementary information and a review on capital adequacy.

The implementation of KAMs is the biggest change to auditing standards and the audit report since the introduction of the clarity standards in 2004.

The platform for change was to provide insights to shareholders on the conduct of the audit, previously only viewed by those in the board room.

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