



1 October 2018

Warren Allen
Chief Executive
External Reporting Board
PO Box 11-250
Manners Street Central
WELLINGTON 6142

Dear Warren

LIMITED SCOPE REVIEW DRAFT – THE AUDIT OF SERVICE PERFORMANCE INFORMATION

We have read the Limited Scope Review Draft of NZ AS 1 *The Audit of Service Performance Information* that was issued for comment in August 2018 (the proposed standard). The proposed standard was issued for the purpose of inviting feedback on whether it is:

1. Unworkable; or
2. May result in unintended consequences.

In reading the proposed standard, we assessed whether it had addressed the matters in our letter dated 21 December 2017 in response to NZAuASB ED 2017-2. We acknowledge that extensive changes have been made to the proposed standard in response to concerns raised by our office. However, we still have some significant concerns with the latest version of the proposed standard. As a result, it is our view that the proposed standard, in its current form, is unworkable and may result in unintended consequences. The reasons for our view are set out in Appendix 1 to this letter.

This is an important standard. It is essential that the time is taken to get the settings right so that auditors can readily engage with the standard and know what is required of them. Because service performance reporting is an emerging area it is also important that auditors are not seen as inhibiting innovative ways of reporting performance that is permitted under the New Zealand Accounting Standards Board standard, *PBE FRS 48: Service Performance Reporting*.

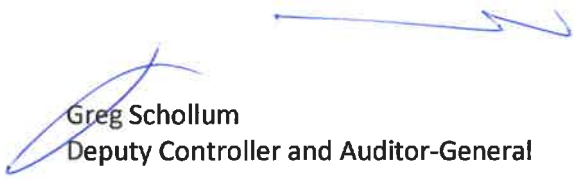
We also consider it is important that, as much as possible, evidence is provided to demonstrate that the proposed standard contributes positively to the public interest it is intended to serve. Consequently, we consider that the NZAuASB should endeavour to quantify the compliance and audit cost implications of the proposed standard together with the accompanying benefits.

We appreciate that the proposed standard is primarily intended to assist auditors in the not-for-profit sector who will be carrying out audits of service performance information for the first time. Although the Auditor-General cannot speak for this category of auditors, it is our sense that the proposed standard may not be helpful to them because it is overly complex and does not communicate its requirements in plain English in the context of audits of relatively simple statements of service performance.

I reiterate our comfort to support the continued development of the proposed standard by making Office staff available to elaborate on our concerns and possible solutions, if that would be helpful.

If you have any questions about our submission, please contact Todd Beardsworth at todd.beardsworth@oag.govt.nz.

Yours sincerely



Greg Schollum
Deputy Controller and Auditor-General

Appendix 1 – The Auditor-General’s Comments on Limited Scope Review Draft of NZ AS 1 *The Audit of Service Performance Information*

1. Consistent use of terminology in External Reporting Board standards and guidance

The proposed standard contains terms that are different to the accounting standards. In our view, this is a fundamental matter that must be addressed if the proposed standard is to be workable and avoid the possibility of unintended consequences.

Our concern is that auditors must use the same language as preparers. In this regard, we specifically refer to the “qualitative characteristics” and “pervasive constraints” that form the framework for service performance reporting in the New Zealand Accounting Standards Board standard PBE FRS 48: *Service Performance Reporting*. Otherwise there will be confusion and the real possibility that auditors will apply different standards to preparers. This situation is concerning, particularly when the accounting standards have been set within a permissive framework to allow innovative means of reporting service performance.

2. Selected service performance and the methods used to measure, describe, aggregate, present and disclose the entity’s service performance

In line with our concern in section 1 above, we note that the proposed standard introduces the concept of an entity’s “selected service performance and the methods used to measure, describe, aggregate, present and disclose the entity’s service performance”. We have three observations to make about the application of this concept in the proposed standard.

- (a) Selected service performance and the methods used to measure, describe, aggregate, present and disclose the entity’s service performance is a new concept. Unless there is a complete understanding of this concept by both preparers and auditors, and what this means for reporting and auditing service performance information, the inclusion of this concept in the proposed standard makes it unworkable.

We consider the term selected service performance and the methods used to measure, describe, aggregate, present and disclose the entity’s service performance in the proposed standard to be a problem because:

- This is not a consideration for preparers of service performance information;
- It is not a “standard” or “frame of reference” for all preparers and auditors of service performance information. Instead, it is an entity specific concept; and
- It is not clear what it means.

In our opinion, the proposed standard needs to refer directly to the qualitative characteristics and pervasive constraints in PBE FRS 48.

We note that paragraph 22 of the proposed standard attempts to describe a relationship between the qualitative characteristics and the selected service performance and the methods used to measure, describe, aggregate, present and disclose the entity’s service performance.

- (b) The proposed standard imposes a disclosure requirement on the auditor that is the preparer’s responsibility. Disclosure is the responsibility of the preparer under the applicable accounting standard. The proposed standard should not place a disclosure requirement on the auditor,

particularly when the proposed standard requires significantly more disclosure than is required under the accounting standard.

Specifically, the proposed standard includes a requirement for the auditor to evaluate whether the entity's methods used to measure, describe, aggregate, present and disclose the entity's service performance are available to the users. Whilst we disagree that the concept of methods should be included in the proposed standard in the first place, we are concerned that the proposed standard places a disclosure obligation on the auditor to evaluate if the methods are available to intended users. For example, paragraph 23 states:

*"The auditor **shall evaluate whether the entity's methods** used to measure, describe, aggregate, present and disclose the service performance **are available to intended users** so as to enable intended users to understand the methods and assumptions underlying the information, for example, disclosed in the judgements reported as part of the service performance information or by cross reference."*

There is no indication that users want this information. For a department or council with many measures, this would be a lot of information and an onerous requirement for preparers and auditors for no clear benefit. We consider it both unworkable and having an unintended consequence of significant extra effort for preparers to document and make this information available for users (who have not asked for it).

(c) Implications for the audit report.

The proposed audit report opinion on the service performance information is worded:

"In our opinion the accompanying general purpose financial report presents fairly, in all material respects:

- *the financial position of the [entity] as at December 31, 20X1, and its financial performance, and its cash flows for the year then ended; and*
- *the service performance for the year ended December 31, 20X1 **in accordance with [the entity's] methods to measure, describe, aggregate, present and disclose its service performance***

in accordance with [Public Benefit Entity Standards/Public Benefit Entity Simple Format Reporting] issued by the New Zealand Accounting Standards Board."

The bold text has been added since the original ED. We consider it unnecessary and confusing. We note that the standard should be seeking compliance with generally accepted accounting practice, rather than compliance with an entity's own methods. The methods are the means by which the entity achieves compliance with generally accepted accounting practice.

3. The proposed standard is difficult to understand

Whilst the proposed standard is an improvement on NZAuASB ED 2017-2, it is still difficult to read and understand. The proposed standard is primarily intended to assist auditors in the not-for-profit sector who will be carrying out audits of service performance information for the first time. This means the proposed standard must communicate its requirements to auditors for the audits of relatively simple statements of service performance in plain English.

In our view, the main body of the proposed standard should include only a small number of essential requirements. Application and Explanatory Information should provide helpful guidance to auditors

on the practical application of the requirements. This recognises that auditors are busy people. Unless the proposed standard is clear and readable there is a good chance that it will not be properly understood, which could lead to it being misapplied.

4. Scope of the proposed standard

We are concerned that the proposed standard may lead auditors to limit their audit to “service performance information” and, in doing so, cause preparers to also limit their reporting to service performance information. Unfortunately, this deficiency is also present in the accounting standard PBE FRS 48 because it is titled *Service Performance Reporting*.

Reporting performance information is a developing area. There are different, and sometimes better, ways of reporting performance beyond a *service performance* dimension. Both PBE FRS 48 and the proposed standard allow for broader information to be reported, as service performance information is explained as follows:

*“Service performance information is information about what the entity has done during the reporting period in working towards its broader aims and objectives, **together with supporting contextual information**” [emphasis added].*

It is the “supporting contextual information” that allows for broader information to be reported and audited.

The proposed standard now explains service performance information in paragraph A1 under the “Application and Other Explanatory Guidance” heading. However, we consider that the proposed standard should specifically state that, under the “Scope of this NZ AS” heading at the beginning of the proposed standard, the proposed standard applies equally to any supporting contextual information.

We make this point because meaningful performance reporting in the public sector is trending towards how individual entities collectively contribute towards a wider objective. Such reporting may also apply to entities in the not-for-profit sector.