

- 3.1 Last year, we resumed reporting on the non-standard audit reports issued on the annual financial reports of local authorities.<sup>1</sup>
- 3.2 This article resumes our reporting of the non-standard audit reports – issued during the period 1 July 2001 to 31 December 2002 – on the financial reports of:
- entities that are part of the Crown reporting entity<sup>2</sup>; and
  - other public entities not within the local government portfolio.

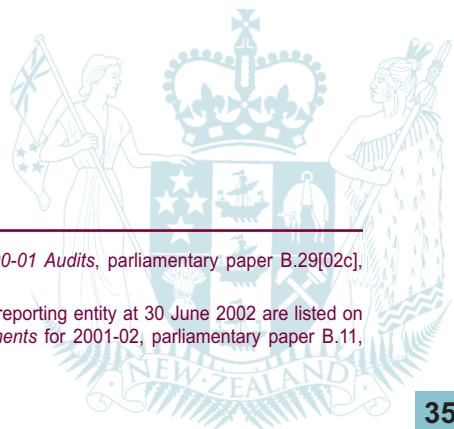
### Why Are We Reporting This Information?

- 3.3 An audit report is addressed to the readers of an entity's financial report. However, all public entities are in one sense or another creatures of statute and, therefore, also accountable to Parliament. We consider it important to draw Parliament's attention to the range of matters which give rise to non-standard audit reports.
- 3.4 In each case, the issues underlying a non-standard audit report are drawn to the attention of the entity and discussed with its governing body.

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1 *Local Government: Results of the 2000-01 Audits*, parliamentary paper B.29[02c], 2002, pages 30-37.

2 The entities that comprised the Crown reporting entity at 30 June 2002 are listed on pages 100-101 of the *Financial Statements for 2001-02*, parliamentary paper B.11, 2002.



## What Is a Non-standard Audit Report?

- 3.5 A non-standard audit report is one in which the auditor has:
- qualified the audit opinion due to a disagreement or a limitation on scope;
  - drawn attention to a breach of law; or
  - drawn attention to a fundamental uncertainty.<sup>3</sup>
- 3.6 There are three types of qualified audit opinion, as explained in paragraphs 3.7-3.10. Attention is drawn to a breach of law or a fundamental uncertainty in an explanatory paragraph that is included in the audit report in such a way that it cannot be mistaken for a qualification of the opinion.

### “Adverse” Opinion

- 3.7 An “adverse” opinion is expressed when there is disagreement between the auditor and the entity about the treatment or disclosure of a matter in the financial report and, in the auditor’s judgement, the treatment or disclosure is so material or pervasive that the report is seriously misleading.
- 3.8 Expression of an “adverse” opinion creates the most serious type of non-standard audit report and happens only rarely.

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<sup>3</sup> The Institute of Chartered Accountants of New Zealand Auditing Standard No. 702 *The Audit Report on an Attest Audit* (AS-702) outlines in what circumstances an auditor can:

- Issue a qualified opinion because –
  - there is a limitation on the scope of the auditor’s examination; or
  - the auditor disagrees with the treatment or disclosure of a matter in the financial report; and
  - in the auditor’s judgement, the effect of the matter is or may be material.
- In an explanatory paragraph separate from the opinion, draw attention to a failure to comply with a particular law.
- In an explanatory paragraph separate from the opinion, draw attention to a fundamental uncertainty about the outcome of a future event.

### “Disclaimer of Opinion”

- 3.9 A “disclaimer of opinion” is expressed when the possible effect of a limitation on the scope of the auditor’s examination is so material or pervasive that the auditor has not been able to obtain sufficient evidence to support, and accordingly is unable to express, an opinion on the financial report.

### “Except-for” Opinion

- 3.10 An “except-for” opinion is expressed when the auditor concludes that either:
- the possible effect of a limitation on the scope of the auditor’s examination is or may be material but is not so significant as to require a “disclaimer of opinion” – in which case the opinion is qualified by using the words “except for the effects of any adjustments that might have been found necessary” had the limitation not affected the evidence available to the auditor; or
  - the effect of the treatment or disclosure of a matter with which the auditor disagrees is or may be material but is not, in the auditor’s judgement, so significant as to require an “adverse” opinion – in which case the opinion is qualified by using the words “except for the effects of” the matter giving rise to the disagreement.

### Explanatory Paragraph

- 3.11 In certain circumstances, it may be appropriate for the auditor to include in the audit report additional comment, by way of an explanatory paragraph, to draw attention to a matter that is regarded as relevant to a proper understanding of the basis of opinion on the financial report.
- 3.12 For example, it could be relevant to draw attention to the entity having breached its statutory obligations, or to a fundamental uncertainty which might make the going concern assumption inappropriate. Inclusion of an explanatory paragraph tends to be the most common type of non-standard audit report.

## Summary of the Non-standard Audit Reports Issued

3.13 The following summary covers non-standard audit reports issued during the 18-month period 1 July 2001 to 31 December 2002 and outlines the nature of those reports.

### *“Adverse” Opinions*

Class of Entity	No. of Entities	Reason for Opinion
State-owned Enterprise	1 <sup>4</sup>	The auditor disagreed with the accounting treatment of recording provisions for claims and litigation relating to the previous operations of the business. The provisions did not have the essential characteristics of a liability as outlined in the <i>Statement of Concepts</i> <sup>5</sup> .
Crown Entity (Education)	1	The use of the going concern basis to prepare the financial report was inappropriate because the entity was ceasing to exist.
Maori Trust Board	1	There was uncertainty about the carrying value of a number of investments and uncertainty about the collectability of a number of debts, loans, and advances. Provisions had not been made to reflect impairment in the carrying value of these items.  There was a lack of disclosure about contingent liabilities arising from an Inland Revenue Department tax audit of a subsidiary company.

*... continued on opposite page.*

<sup>4</sup> For financial reports for two years.

<sup>5</sup> Institute of Chartered Accountants of New Zealand: *Statement of Concepts for General Purpose Financial Reporting*.

Class of Entity	No. of Entities	Reason for Opinion
Maori Trust Board <i>... continued.</i>		The auditor had issued an adverse audit opinion on the and was therefore unable to provide any assurance on comparative figures.
Crown Entity subsidiary	2	The auditor disagreed with the use of the going concern basis to prepare the financial statements.

## “Disclaimers of Opinion”

There were no “disclaimers of opinion” issued during the period.

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## *“Except-for” Opinions*

Class of Entity	No. of Entities	Reason for Opinion
Crown Entity	1	The auditor disagreed with the entity recognising a grant as a liability, because the terms of the grant did not have the essential characteristics to make it a liability as outlined in the <i>Statement of Concepts</i> .
District Health Board subsidiary	2	The auditor was unable to verify some material revenues, due to limited control over those revenues.
Maori Trust Board	1	The auditor was unable to verify the valuation of the Board’s investment in another entity.
Maori Trust Board subsidiary	2 <sup>6</sup>	The auditor disagreed with the Board recording a provision for certain services. The provision did not have the essential characteristics of a liability as outlined in the <i>Statement of Concepts</i> .
Maori Trust Board	1 <sup>7</sup>	The Board did not consolidate its subsidiaries into group accounts as required by SSAP-8. The audit report for the third year included an explanatory paragraph drawing attention to the fact that Board funds had been misappropriated during the year, some of which had been recovered and recognised as revenue. <i>... continued on opposite page.</i>

<sup>6</sup> In both cases, for financial reports for two years.

<sup>7</sup> For financial reports for three years.

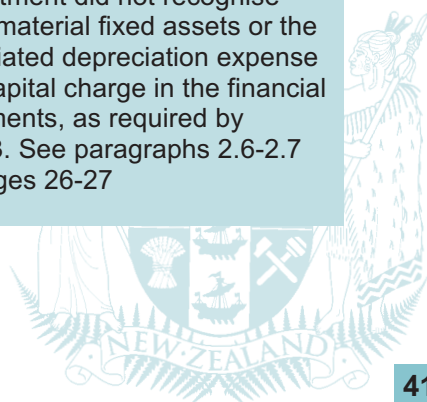


## NON-STANDARD AUDIT REPORTS ISSUED

B.29[03a]

Class of Entity	No. of Entities	Reason for Opinion
District Health Board	1	The Board did not revalue its buildings at component level, as required by FRS-3.
Education (R.E.A.P.*)	1	The auditor was unable to obtain independent confirmation or sufficient audit evidence to determine the accuracy of the figures presented in the statement of service performance.
Education (R.E.A.P.)	1	The auditor was unable to locate some of the accounting records, and some funds were misappropriated during the year. As a result, the auditor was unable to establish with certainty the amount of the misappropriated funds, and was unable to obtain sufficient evidence to substantiate certain revenue items.
Education (R.E.A.P.)	1	No budgeted figures were provided in the statement of financial position, which is a breach of statutory reporting requirements.
Government Department	1	The auditor disagreed with the Department's valuation of certain fixed assets. In addition, the Department did not recognise other material fixed assets or the associated depreciation expense and capital charge in the financial statements, as required by FRS-3. See paragraphs 2.6-2.7 on pages 26-27

\* Rural Education Activity Programme.



## NON-STANDARD AUDIT REPORTS ISSUED

### *Explanatory Paragraphs*

Class of Entity	No. of Entities	Reason for Opinion
Crown Entity (Education)	1	The auditor drew attention to the uncertainty surrounding the entity's proposed disestablishment, and use of the going concern basis in preparing the financial report.
Statutory Body	2 <sup>8</sup>	The going concern basis was not used in preparing the financial report.*
Statutory Body	1	The auditor drew attention to the uncertainty over the future status of the entity.
Polytechnic	1	The going concern basis was not used in preparing the financial report.*
Polytechnic subsidiary	2 <sup>9</sup>	The going concern was basis not used in preparing the financial report.*
District Health Board subsidiary	2	The going concern basis was not used in preparing the financial report.*
Health and Hospital Company	1	The going concern basis was not used in preparing the financial report.*
Health and Hospital Company	5	The company was dissolved, and the assets and liabilities vested in a successor District Health Board.
State-owned Enterprise	2	The going concern basis was not used in preparing the financial report.*

*... continued on opposite page.*

<sup>8</sup> In one case, for financial reports for four years.

<sup>9</sup> In one case, for financial reports for three years.



## NON-STANDARD AUDIT REPORTS ISSUED

B.29[03a]

Class of Entity	No. of Entities	Reason for Opinion
Crown Entity	4	The going concern basis was not used in preparing the financial report. * In addition, for one entity the auditor drew attention to the uncertainty concerning the final payment required to relinquish an ongoing lease obligation.
Government Department	1	The going concern basis was not used in preparing the financial report.*
Crown Entity (Education)	2	The going concern basis was not used in preparing the financial report.*
Education (Misc.)	1	The going concern basis was not used in preparing the financial report.*
Producer Board	1	The going concern basis was not used in preparing the financial report.*

\* Justified, because in each case the entity was ceasing to exist.

