



ACCOUNTANCY FUTURES

The value of audit: views from retail (private) investors

A RESEARCH PROJECT CONDUCTED IN COLLABORATION WITH THE SECURITIES INVESTORS ASSOCIATION
(SINGAPORE) (SIAS)

ACKNOWLEDGEMENTS

ACCA is extremely grateful for the support provided by SIAS, particularly in inviting their members to participate, without which this survey would not have been possible.

ACCA and SIAS thank the respondents of this online survey for providing their responses and the following participants of the Focus Group Discussion for their valuable feedback:

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CONFIDENTIALITY

This survey was conducted on a confidential basis. Accordingly, we do not provide information on individual survey responses.

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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 in all stages of development. We aim to develop capacity in the profession and encourage the adoption of consistent 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 work to open up the profession to people of all backgrounds and remove artificial barriers to entry, ensuring that our qualifications and their delivery meet the diverse needs of trainee professionals and their employers.

We support our 147,000 members and 424,000 students in 170 countries, helping them to develop successful careers in accounting and business, and equipping them with the skills required by employers. We work through a network of 83 offices and centres and more than 8,500 Approved Employers worldwide, who provide high standards of employee learning and development. Through our public interest remit, we promote the appropriate regulation of accounting. We also conduct relevant research to ensure that the reputation and influence of the accountancy profession continues to grow, proving its public value in society.

ABOUT SIAS

Founded in 1999, the non-profit Securities Investors Association (Singapore), SIAS, is the largest organised investor lobby group in Asia – with close to 70,000 retail (private) investors as members. It is run by a Management Committee comprising professionals who volunteer their time to actively promote Investor Education, Corporate Transparency, Corporate Governance and Shareholder Activism. Today, SIAS is the watchdog for investor rights in Singapore.

Committed to investor education at all levels, SIAS now provides physical and online investor education and information to a much wider audience in and out of Singapore. SIAS has successfully organised over 500 investor education programmes ranging from basic investment seminars for novices to certificate courses for the investment savvy. Thus far, more than 60,000 retail (private) investors have benefited from these programmes.

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PURPOSE OF SURVEY

The value of external audit has been questioned in various quarters during the global financial crisis. ACCA, however, firmly believes in the value that external audit brings to shareholders and the wider economy by instilling trust and confidence in companies' financial statements. We also believe that it engenders wider 'intangible' benefits in terms of imposing discipline on companies, deterring fraud and giving comfort to other stakeholders that businesses are going concerns.

We believe that the profession needs to do more to promote that value – particularly at a time of economic uncertainty. There has historically been a very limited body of published research on the value of financial statements' audits to investors and other stakeholders, despite some notable recent studies in this area. ACCA is keen to play its part in providing evidence-based assessments which will contribute to the debate on the value of audit.

For this purpose, ACCA held a series of ten international round-table discussions over a 12-month period from September 2009 to September 2010 and has published the consolidated findings in *Reshaping the Audit for the New Global Economy*.¹

SIAS, the largest organised investor lobby group in Asia, is keen to understand how the value of audit can be enhanced for its members.

ACRA, as the national regulator of business entities and public accountants, has an interest in the value of external audits and in raising its quality. In 2010, ACRA commissioned ACCA to carry out a survey on the *Value of Audit: Views of Audit Committee Chairmen*² which reaffirmed the value of audit to this stakeholder group.

The objective of this report, a follow-up to the 2010 survey and report, is to inform the current debate by providing contemporary evidence on the value of audit as perceived by an important stakeholder group to which the audit report is addressed and which ultimately pays for the audit, namely, the investors. This survey is concerned with audits in the listed company market and deals mainly with the perspectives of retail (private) investors in that sector.

KEY FINDINGS

1. **Overall, 90% of respondents felt that the external audit, in its current form and scope, brings value to them.** More than 40% were of the opinion that the external audit brought 'a lot of value' to them. However, about 8% concluded that it had very little or no value to them and blamed it mainly on the historical nature of the financial statements on which the audit opinion was given.
2. **80% of respondents felt that audited financial statements were important to them in making investment decisions,** with more than a quarter (30%) who felt that they were 'very important'. However, a small percentage (4%) felt that audited financial statements were not important because the auditor's opinion focussed mainly on historical financial statements.
3. **More than 75% of respondents agreed that the scope of the audit should be extended to enhance the value of audit.** Almost a third strongly agreed that this should be done. The two main extensions that investors asked for were specific assurance on a company's internal controls (83%) and a report on the adequacy and effectiveness of a company's risk management programme (80%). Almost all (94%) of respondents desired that the additional information be made available to the public at large and not be restricted to only the audit committee.
4. **More than 85% of respondents felt that the provision of non-financial information (such as corporate governance practices and corporate social responsibility issues) would serve their (investment) decision making purposes.** More than 90% felt that it would be of value to them if this information was audited.

¹Reshaping the Audit for the New Global Economy', ACCA, 2010.

²A Survey on the Value of Audit – Views from Audit Committee Chairmen', ACCA, 2010.

Terms of Reference

This report presents the results of a research project on the value of audit conducted by ACCA, in collaboration with SIAS. It is based on responses provided by mainly retail (private) investors of listed corporations in Singapore on two major themes:

- *Value of current audit* – frank assessments by investors of the value of the audit of financial statements in today’s complex environment
- *Future enhancements to the value of audit* – views from investors on how the value of audit can be further enhanced.

TERMINOLOGY

Audit: ‘Audit’ refers to the external audit of a company’s financial statements required by statute and ‘auditor’ refers to the external auditor. The relevant statute for this survey was the Singapore’s Companies Act (Chapter 50).

Retail (private) investor: A retail or private investor is an individual who purchases securities for his or her own personal account rather than for an organization.

METHODOLOGY

This research survey was conducted in April 2011 using an online questionnaire which was sent out to more than 30,000 SIAS members and 3,000 ACCA members.

As the respondents to the survey are allowed to pass over particular questions, the number of responses varies from question to question. The maximum number of responses received for a single question in this survey was 390. The responses were consolidated to highlight the main themes in this report. As such, the referenced question numbers in this report do not necessarily run in sequence and not all questions are captioned.

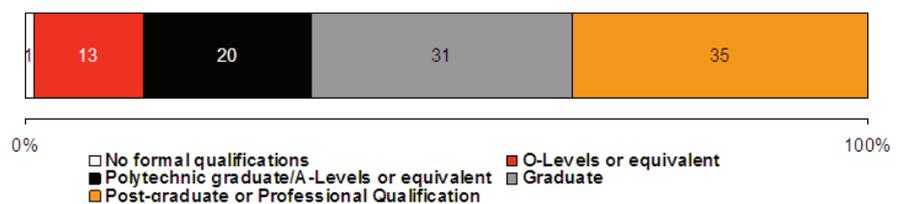
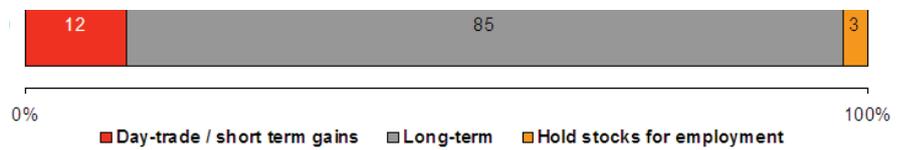
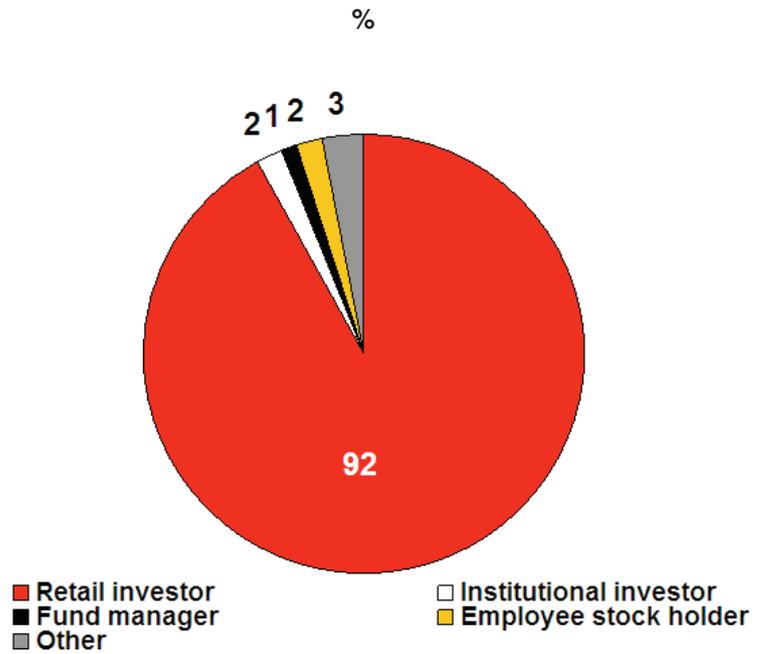
A Focus Group Discussion (‘focus group’), comprising senior staff members of SIAS (including a former banker and an academic), a former journalist and broadcaster, an external auditor and a management consultant, was organised in May 2011 to discuss the findings from this survey. Their feedback is incorporated within the report.

The report uses unattributed direct and paraphrased quotations from respondents selectively, to illustrate various themes and opinions.

PROFILE OF RESPONDENTS

More than 90% of respondents were retail (private) investors who invested in the long-term and described themselves as moderate risk takers. The overwhelming majority (86%) had qualifications of 'A' Levels or higher. Two-thirds (66%) were university graduates or post-graduates.

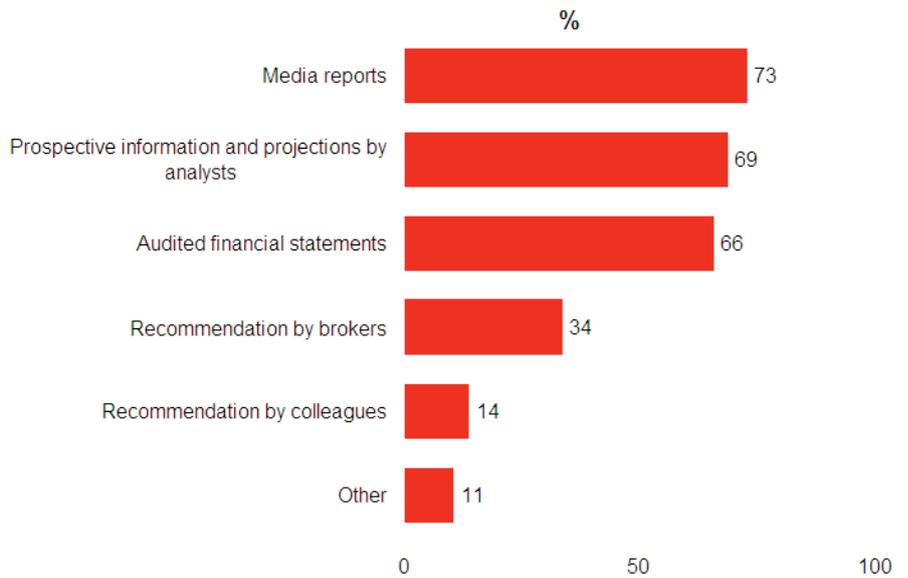
PROFILE OF RESPONDENTS



IMPORTANCE OF AUDITED FINANCIAL STATEMENTS TO INVESTMENT DECISIONS

Investors used multiple sources of information to guide their investment decisions. The 3 most important sources of information were media reports (73%), prospective information and projections by analysts (69%) and audited financial statements (66%).

Some participants of the focus group proposed that media reports probably catch the attention of most investors as they tend to focus on negative news. They also suggested that the apparent dependence on media reports and information from analysts may be more to do with their widespread availability rather than their inherent content value. Furthermore, they speculated that audited financial statements were less popular because it was reporting on historical information rather than the more current or prospective information in media reports and analysts' projections. As media reports are the main source of information, participants of the focus group called for business journalists to be more informed so that they can provide better and more accurate interpretations of the audit report and the financial statements.



Q6. What source of information do you typically use to help you make investment decisions?
Responses: 387

Audited financial statements are important to most investors when making investment decisions. 80% of respondents felt that audited financial statements were important to them in making investment decisions, with more than a quarter (30%) who felt that they were ‘very important’.

However, a small percentage (4%) felt that audited financial statements were not important, with some attributing this to:

- the fact that the opinion in the audit report relates to historic information
- reservations about the credibility of the audit report.

Some participants of the focus group proposed that the impact of this response should not be overstated as it is not clear from the question whether respondents were providing feedback on the importance of ‘audited financial statements’ or simply ‘financial statements’.

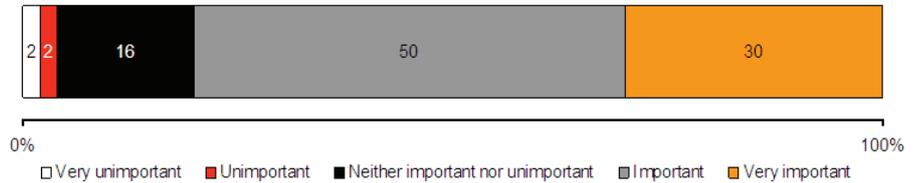
WHAT CAN BE DONE TO ENHANCE THE VALUE OF AUDIT?

Extend the Scope of the Audit

Current audited financial statements are important in supporting investment decisions. However, most investors still welcomed extending the scope of audit. More than three-quarters (77%) of respondents agreed that the scope of audit should be extended to enhance the value of audit. Almost a third (33%) strongly felt that this should be done.

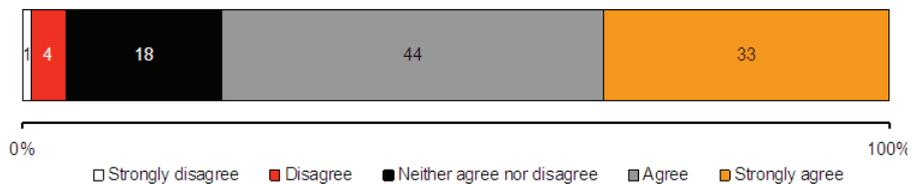
Only 5% of respondents disagreed with extending the scope of the audit and felt that the current scope was adequate. The cost implications of these extensions were cited as one reason why it should not be extended.

IMPORTANCE OF AUDITED FINANCIAL STATEMENTS



Q7. Overall, how important are audited financial statements to your investment decisions?
Responses: 390

EXTENSIONS TO SCOPE OF AUDIT



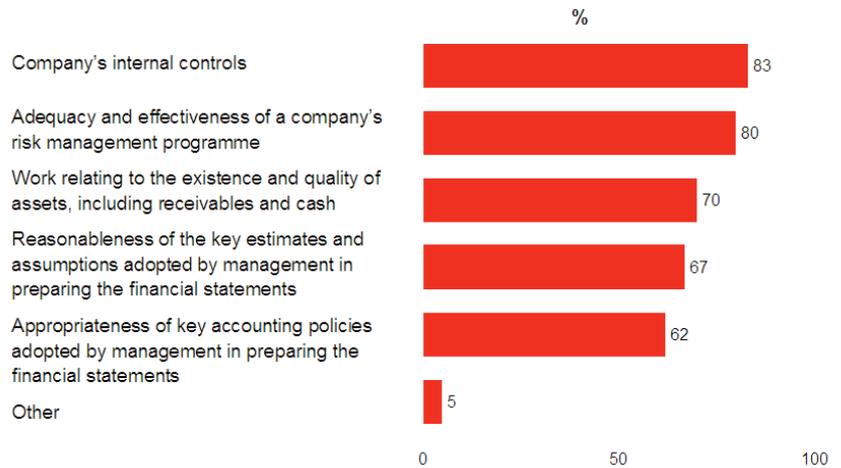
Q9. Do you agree or disagree with extending the scope of the audit?
Responses: 390

What specific scope extensions are investors requesting for?

The two main extensions that investors asked for was specific assurance on a company’s internal controls (83%) and a report on the adequacy and effectiveness of a company’s risk management programme (80%).

A commentary on the work relating to the existence and quality of assets, including receivables and cash was also desired (70%). A commentary on the reasonableness of the key estimates and assumptions adopted by management in preparing the financial statements (67%) and a commentary on the appropriateness of key accounting policies adopted by management in preparing the financial statements (62%) were also requested.

REQUESTED AREAS OF EXTENSIONS TO SCOPE OF AUDIT



Q11. In extending the scope of the audit, which of the following do you think would be of value to investors?

Responses: 299

5% of respondents requested for other extensions, including:

- information about people costs e.g. salaries and expense accounts of senior managers
- insight into relationships between senior managers, whether they hold multiple positions at other companies and their plans for succession
- information about the company's shareholders and customers.

Several participants of the focus group felt that these extensions to the scope of external audit would be better provided by internal rather than external audit. They felt that internal auditors would be in a better position to deliver more comprehensive reports and opinions on internal controls and risk management programmes, compared to external auditors. Furthermore, some expressed concerns that the provision of these types of reports by the external auditor may blur the distinction between internal and external audits.

One participant observed: 'it is not the role of external audit; it is the role of internal audit to provide this additional information'. One participant of the focus group was sceptical about whether respondents fully understood the cost implications of these extensions on the company and the external auditor.

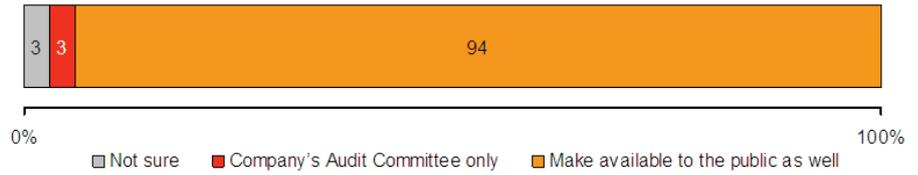
Notwithstanding who should provide this additional information and the cost implications, at least one participant felt that 'investors may feel short-changed if information of possible failures is not given to them'. Another participant noted that the significant proportion who wanted extensions evidences the wide expectation gap between what external audits currently deliver and what investors require.

SPECIFIC REQUESTS FOR SCOPE EXTENSIONS



Sharing additional information with a wider audience

Almost all (94%) of respondents desired that the additional information be made available to the public at large and not be restricted to only the audit committee.



Q12. Do you think this additional information should be made available to the public, or is it only necessary to provide this to the company's Audit Committee?
Responses: 298

Is Non-Financial Information Important?

More than 85% of respondents felt that the provision of non-financial information (such as corporate governance practices and corporate social responsibility issues) would serve their (investment) decision making purposes.

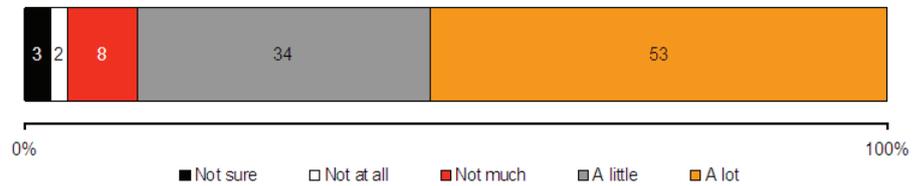
A participant of the focus group noted that the survey question does not distinguish between corporate governance practices and corporate social responsibilities. He felt that respondents are probably asking for more information about corporate governance practices rather than corporate social responsibilities. Another participant of the focus group proposed that the high percentage who wanted non-financial information may be influenced by the media, which raised their expectations.

Some participants were concerned that there are no existing established frameworks to guide the auditor in auditing this additional information and speculated if auditors could realistically deliver on these extensions.

Other participants of the focus group expressed doubt as to whether investors can go through so much information and noted that the more information requested, the higher the costs of preparing reports.

One participant was of the view that information should be made available when needed. Investors might not want to go through a thick file of information, but they should have access to it when required.

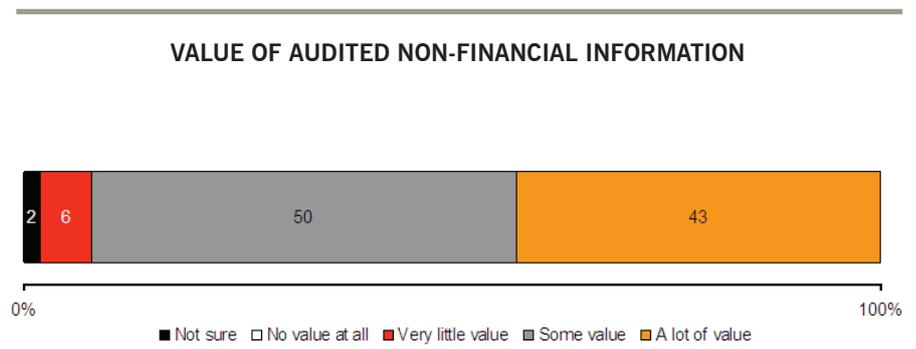
UTILITY OF NON-FINANCIAL INFORMATION



Q14. To what extent does the disclosure of non-financial matters in companies' annual reports serve your decision-making?
Responses: 390

Issues

More than 90% felt that it would be of value to them if this information was audited; with more than 40% saying it will bring 'a lot of value'. No respondent indicated that there was 'no value' in audited non-financial information.



Q15. If the information about non-financial matters was audited by an external auditor, what value would this add to you as an investor?
Responses: 338

Conclusion

Overall, more than 90% of respondents felt that the external audit, in its current form and scope, brings value to them. More than 40% were of the opinion that the external audit brought 'a lot of value' to them. The responses from this survey therefore clearly confirm that the traditional audit model is not broken and continues to fulfil a critical role in the financial reporting value chain and the corporate governance framework. Nevertheless, 8% felt that it had less value for them. How could audit be modified to enhance its value to this group?

The majority of respondents requested extending the scope of the audit to enhance the value. High on their agenda is an assurance report on the internal controls of a company. This is not surprising and may be influenced by the greater focus in this area brought about by the *Sarbanes-Oxley Act*. Investors are clearly aware of the importance of good internal controls to ensure that financial statements are reliable and assets are secure.

Respondents have also asked for a commentary on the adequacy and effectiveness of a company's risk management programme. Information on risk management has perhaps become more critical in the light of several risk management failures in the past decade.

Both of these extensions are consistent with previous feedback received by ACCA, as published in *Reshaping the Audit for the New Global Economy* (cited above). If the scope of audit is extended, investors expect additional information arising from these extensions to be made available to the public. Those who were not in favour of extending the scope of audit feel that the current format is sufficient and raised concerns that extending the scope of audit will have significant cost implications. No doubt, there will be cost implications for each extension. There will, however, also be benefits. It is perhaps because of this that the majority of respondents appeared to be in favour of these extensions.

Several participants of the focus group felt that the suggested extensions to the scope of external audit would be better provided by internal rather than external audit. The review of internal controls and risk management frameworks are core activities of internal audit in many organisations. In extending the scope of external audit, therefore, special attention must

also be placed on the work of internal audit and how it interfaces with external audit.

Some respondents blamed the historical nature of financial statements for the lower (overall) value of audit – indicating the close connection between the value of audit and the relevance of the financial information being audited. Further enhancements could be made in the light of this feedback which was also received from the small number of respondents (specifically 15 respondents) who felt that audited financial statements were not important to them. This may be a call from investors for more prospective information in the annual reports. To some extent this issue is being addressed by the *FRS Practice Statement on the Management Commentary* issued by the Accounting Standards Council in 2011. This is a non-mandatory framework to guide the presentation of management commentary, which would have the effect of including more forward-looking information and analysis. However, this information (required in the management commentary) is not within the scope of the current audit.

A high percentage of respondents called for more non-financial information (such as corporate governance practices and corporate social responsibility issues) which received some form of assurance. According to these responses, it appears that investors are paying increased attention to non-financial information and that there is a growing awareness of its importance in making investment decisions. This may indicate that there is some desire to use non-financial information more in the future. Furthermore, it appears that they would like the information prepared by management to be reviewed and assessed by other parties for their veracity. The findings therefore imply that investors desire not only extensions to the scope of the audit but also the financial reporting framework – the two frameworks being inextricably intertwined.

It is clear from this survey that the current audit brings much value to most retail (private) investors. It suggests that this value can be further enhanced if audit reports also provided views on the company's internal controls and risk management programmes. Investors are also requesting for more audited non-financial information (relating to corporate governance practices and corporate social responsibilities).

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