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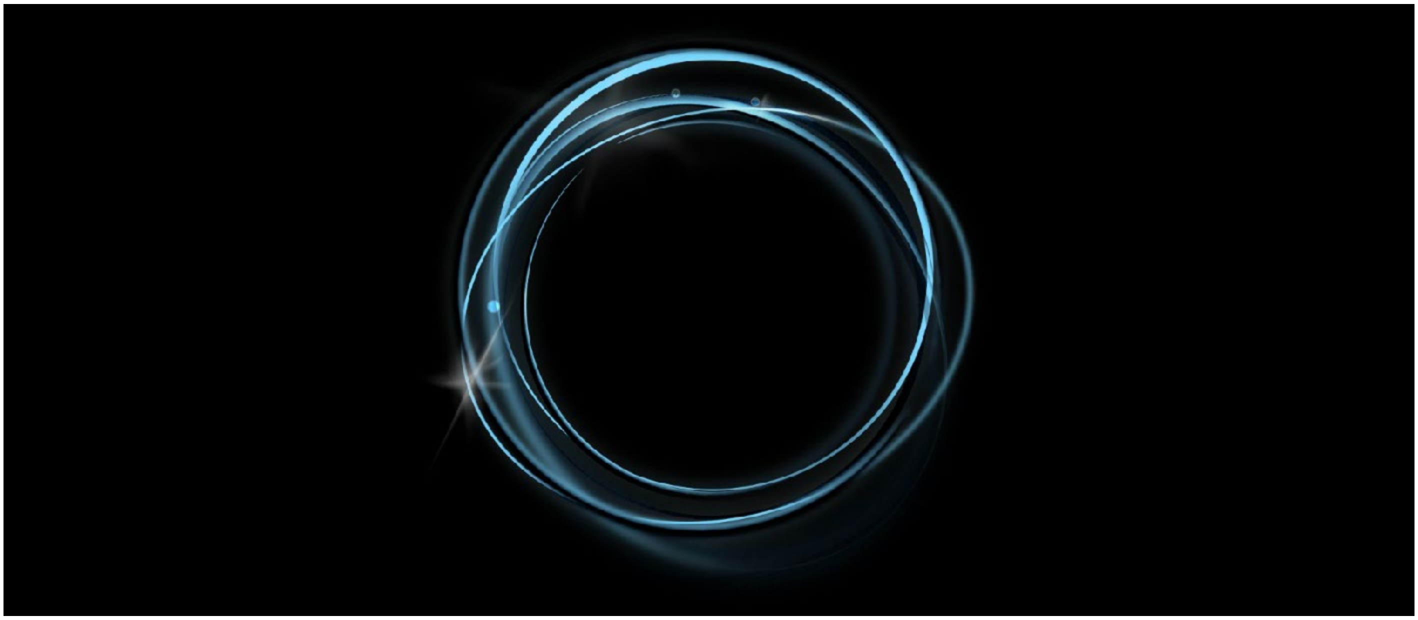

Corporate reporting and audit—a collective responsibility

The capital markets need to work in the public interest now more than ever

At a time when society is facing unprecedented disruption and upheaval, and public monies are being used to support business solvency and liquidity, the conduct and obligations of management are subject to increased scrutiny. Through the corporate reporting process, stakeholders need to be able to identify well-governed companies who act in the public interest. Meaningful reporting and robust governance mechanisms are key tenets of public interest and drive trust.

There needs to be transparency around the corporate business model and risks, the governance and controls that are in place and the balanced narrative around sustainable performance. According to Sir Donald Brydon, ultimately, stakeholders want to know, “Is the company being honestly run and is it likely to have a future?”[1]

To achieve this, all elements of the market “ecosystem” need to be working in the public interest—the company, the regulatory bodies and the independent auditor.

From a company perspective, this includes management, executive teams and compliance functions; independent governance vehicles, including board oversight and internal audit functions; as well as active engagement from the owners and other stakeholders of the business.

Strong regulation—of the company, the capital markets, the independent auditors and the relevant standard setters—is another critical component of a robust corporate reporting environment. Coordinated, proportionate regulation delivered by strong national and international capital markets and audit regulators, taking best practice from multiple geographies, is essential in today’s global capital markets. At the current time, there is fragmentation across the global regulatory landscape and this entire regulatory system needs to strive towards greater consistency if we are to achieve this goal.

In addition, standard setting needs to work alongside local legal requirements to drive clarity and transparency, so that the resulting corporate reporting is meaningful to all stakeholders.

[1] Sir Donald Brydon presentation to the Institute of Chartered Accountants of England and Wales, Audit and Assurance Faculty, February 2020

Across the world, there are several active reviews into the financial reporting ecosystem, including the role and purpose of audit. The challenges that have arisen as a result of these reviews have been amplified by the COVID-19 landscape. The public interest role of the auditor is under increased scrutiny.

The independent auditor is an important part of this ecosystem. Yet there are examples, in certain parts of the world, where audit seems to be perceived as falling short of public expectations—bringing into question the role and value of audit.

We believe it is important to continue to challenge all parts of the ecosystem to ensure that they are working optimally for society.

Supply side considerations

Audit is valuable and is not broken.

In most cases, the rigor of the independent audit drives strong corporate discipline in well run companies and often makes recommendations leading to companies making adjustments to corporate reporting. These adjustments ensure compliance with financial reporting standards and are often unseen to the outside world, but are adopted by the board.

These valuable elements of the audit process could be more transparent to stakeholders.

As auditors, we have a responsibility to bring transparency to the work we perform and the way we perform it. We need to better demonstrate that we have adopted a robust and independent mind- set that does not hesitate to question or challenge senior management. We need to ensure that our commitment to quality is consistently upheld, and that we swiftly learn from human error.

Audit has at times, though, fallen short—both in the quality of delivery and in terms of not meeting the public's expectations.

We welcome further debate on the quality and relevance of audit, in particular in areas such as sustainability, fraud, and viability, adopting a more forward looking rather than historic backwards looking lens. We recognize the perceptions of conflicts of interest or areas where inadequate attention appears to have been focused on areas of key business risk. In certain markets, for example the Netherlands, Australia, and the UK, current debates are seeking to address a number of these concerns.

However, supply side reform by auditors is not the whole solution.

Market side considerations

Market side developments, including strong regulation over director responsibilities for the internal control environment and the regulatory oversight of corporate reporting, must sit alongside any changes to the audit process and product.

It is critical that companies and their boards are both transparent and accountable for their business and an appropriate strong regulatory environment exists to drive responsible behaviors in the public interest. In the UK, the recommendations of the Kingman and Brydon reviews are detailed and thoughtful in this regard. And in the US, the adoption of the Sarbanes Oxley Act has proved to be beneficial in driving company management and director responsibilities, reporting on internal controls over financial reporting, and many other elements of the financial reporting ecosystem.

Investors and other stakeholders also have a critical role to play to bring challenge and change.

In conclusion

The accounting profession, the corporate world, regulators, and investors need to work together to drive change across the corporate reporting ecosystem to respond to the changing relationship between companies and the society they work within.

Any reform cannot—and should not—eliminate corporate failure. It must, however, address the increasingly visible weaknesses and concerns that exist currently across financial ecosystems and should act as a catalyst for responsible business behavior and more meaningful corporate reporting.

Corporate reporting should evolve to meet complex societal needs, reflecting non-financial as well as financial matters and providing greater clarity on the corporate business model and the risks and returns that the business is taking to execute that model.

We need to be prepared to challenge the corporate reporting system as a whole—including the role of audit—to restore trust and ensure that the capital markets demonstrably act in the public interest.

Deloitte is committed to this evolution of corporate reporting in the public interest and will explore elements of this further in a series of points of view to stimulate and inform the debate.

Connect with us

For more information, feel free to reach out to Jean-Marc Mickeler, Deloitte Global Audit & Assurance Business Leader.