Key Audit Matters –How key is key? And do they really Matter?

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Key Audit Matters – Structured Abstract

Purpose of this paper:

The New International Standard of Auditing (ISA) statement number 701 titled *Key Audit Matters* (KAM) has been reported as one of the most significant changes to the audit profession and the manner in which audit reports are to be delivered. Effective 15 December 2016, auditors for Johannesburg Stock Exchange (JSE) listed companies will need to disclose key and significant transactions that occurred on the audit, even in the event of an unmodified audit opinion.

This paper uses a detailed content analysis of prior academic and professional audit literature to explore possible unintended consequences, uncertainties and risks of the new statement and examines its potential effect on both auditors, and audit clients alike.

Design/methodology/approach

The paper uses a detailed review of prior literature and utilises the theoretical framework of Unintended Consequences, particularly of regulatory developments, to further explore this incumbent legislation.

Findings:

This paper suggests that numerous unintended consequences, uncertainties and risks may exist within the new legislation. These include disclosure of potential confidential information, a potential increase to the auditor's liability as well as the potential to further fragment the auditor's relationship with its clients.

Value:

These findings give the paper scope to make a meaningful contribution by critically assessing the proposed introduction of the KAM with an aim to informing auditing legislative development and future quantitative studies on the introduction of the KAM in South Africa.

Keywords:

Key audit matters, Transparency, Auditor liability, Unintended consequences, Relevance, Disclosure

1: INTRODUCTION

South Africa has long been lauded as having the highest rating when it comes to accounting practice, accounting standards and audit reporting (Business, 2014), (Maroun and Gowar, 2013). South Africa ranks first in the world in respect of the strength of auditing and reporting standards (Bowes et al., 2004). Closely linked to this is a significant emphasis on the audits that are performed. The majority of prospective Chartered Accountants who serve their articles/traineeship at a South African Institute of Accountancy (SAICA) accredited training institution serve at least three years in the audit environment (Kretzschmar et al., 2013) . During this period, candidates are exposed to a wide range of transactions in many sectors, and the candidate gains an understanding of whether these transactions comply with the appropriate accounting and auditing standards or not. Furthermore, if not, the Chartered Accountant (SA) is trained as to what effect, if any, this non -compliance would potentially have on the audit report (Puttick et al., 2008).

The audit culminates in the audit opinion. The opinion provides reasonable assurance as to whether the Annual Financial Statements (AFS) fairly presents the results of operations and the financial position of the entity at the financial year end (International Audit and Assurance Standards Board (IAASB), 2014b). In a sense, at the discretion of the audit partner and firm a type of yes / no or pass / fail opinion is given on the organisation (Francis, 2004); (Carcello, 2012). Although not to certify one hundred percent factual correctness, a clean audit report concludes fair presentation with no material misstatement (Hayes et al., 2014). However, as in the infamous case of Enron, Arthur Anderson had reported an unmodified audit opinion on the Annual Financial Statements (AFS) despite the fact that the corporation had large off balance sheet financed debt and numerous dubious 'creative accounting' transactions 'hidden' in their AFS (Cordos and Fulop, 2015); (Porter and Gowthorpe, 2004).

In the case where a modified audit opinion is given, additional information with regards to the opinion is provided to the users (IAASB, 2014c , GROSU et al., 2015). An important aspect of the current standard is that where a clean or unmodified opinion is given, no further corroboration from the auditor is required in terms of the opinion disclosed consider (Gold et al., 2012). It is expected then that the user would rely on his/her own professional scepticism (ISA 200), due care and quality control process of the professional firm in reaching the unmodified audit opinion International Standard on Quality Control (ISQC 1).

Reliance is then placed on the audit report by the relevant users of the AFS. Users are not limited to the shareholders but also include a wide range of stakeholders such as suppliers, customers, employees, regulators such as the South African Revenue Service (SARS) and in the case of a public entity the citizens of the country (Kretzschmar et al., 2013)

Why then, the need for additional disclosure with regards to the audit opinion? Is there perhaps some doubt over the opinions expressed or the ability of the auditor to express this opinion? What are the additional types of information required by users that are currently not being fulfilled? (Cordos and Fulop, 2015). This research continues with this line of thought by exploring possible unintended consequences of the proposed introduction of the KAM. A detailed content analysis of the existing body of literature on the introduction of the KAM is carried out to identify key arguments and counter-arguments in favour of the KAM introduction. The absence of direct prior research on the KAM in South Africa means that this research is interpretive. It does not provide a quantitative assessment of the costs and benefits of the KAM introduction in South Africa but rather seeks to add to the existing debate on the implementation. While this may be construed as threat to validity and reliability in a positivist sense (Creswell, 2009) the normative and qualitative style sheds light on what is and should be happening when it comes to South Africa's audit reporting structure making an important contribution to audit reporting transparency and accountability (see Humphrey, 2011; (Ahrens et al., 2008). At the same time, the exploratory style provides a basis for subsequent research, relying on quantitative methods.

The remainder of this article is organised as follows: Section 2 provides a brief frame of research for the reference. Section 3 outlines the audit opinion, describing the audit framework in the context of the audit opinion and the link this has to the KAM, it also includes a discussion on the going concern opinion and the connection to the KAM as well as a discussion on the proposed implementation initially on listed entities. Section 4 discusses certain possible consequences of the introduction of the KAM. Section 5 concludes and identifies areas for future research.

2: THEORETICAL FRAMEWORK: UNINTENDED CONSEQUENCES OF REGULATORY DEVELOPMENTS

The prior corporate governance literature provides numerous accounts of regulatory developments having unintended consequences. For example (Vakkur et al., 2010) examine the impact of the Sarbanes Oxley Act (2002) (SOX), which was intended to improve the control environment at organisations and promote greater certainty in capital markets (Maroun, 2012). SOX which have resulted in an inflexible environment focusing on rules based rather than conceptual compliance based and have inadvertently resulted in a decrease in the value of firms (Maroun, 2012). In examining a financial reporting environment the introduction of monitoring bodies that are aimed at ensuring certain quality reporting levels do not always result in an improved quality of reporting (Maroun, 2015a). In a taxation context laws and regulations implemented by authorities to eliminate anti-avoidance transfer pricing schemes have often been unsuccessful and have instead added increased complexity and costs to the tax system both locally and internationally (Stiglingh, 2011). The unintended result of these increased taxation compliance implementations is an increased administrative responsibility on the taxpayer, which is often a smaller business without the sufficient resources and capability to manage the significant increased financial expenditure (Maroun, 2015a).

Reflecting on auditing specific areas, a further example is that the quality reviews by the Public Company Accounting Oversight Board (PCAOB) which is designed to improve the reliability and standards of external audits has resulted in unintended consequences for the quality of audit reporting (Segal and Maroun, 2014) .This has occurred through the increased time taken to complete the audit of financial statements and as a result preliminary results have been released by companies prior to the actual audit work being completed and has thus resulted in a decrease in the dependability of these preliminary results (Segal & Maroun, 2014). Humphrey et.al (2011) has also noted that even though there are increased regulations continually being implemented in the audit profession there is minimal visible effect on the quality of the audit being performed (Parker et al., 2008), (Power, 1994). What has resulted is that the increased attempts at regulating the non-audit services performed, partner rotation and audit reporting requirements have not always resulted in the desired effects that was expected (Maroun, 2015a).

The situations highlighted above reflects how legislation and changes which have not been well grounded in professional practice 'run the risk of producing unintended and potentially dysfunctional consequences (Humphrey et al., 2011). The aim of this literature review is not to provide a complete analysis of the problematic aspects of the introduction of new auditing legislation. What is important to appreciate is that rarely are proposed regulatory developments free from unintended consequences (Segal and Maroun, 2014).

3: AUDIT OPINION AND KEY AUDIT MATTERS (KAM)

The objective of an audit of financial statements is to enable the auditor to express an opinion whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework (IAASB, 2009) Thus the audit of financial statements is an assurance engagement, as defined in the International Framework for Assurance Engagements.

The audit firm carries out the engagement according to the standards to which the International Standards of Auditing (ISA's) apply and also in accordance with the audit firms own internal policies (Maroun & Atkins, 2014). Predominantly, audit firms use a risk based approach to auditing. By doing this, during the planning phase of the audit, the auditor identifies the main areas of risk (a) that the entity faces and (b) how these risks may affect the annual financial statements and thus the audit (IAASB, 2014d). IAASB (2009), ISA 200 divides the risks into three main risk categories viz 'Inherent Risk', 'Control Risk' and 'Detection Risk'.

<u>Inherent Risk:</u>-

ISA 200 p13 defines 'inherent risk' as the susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls. Thus this represents the 'inherent' or environmental risks that the client faces. These risks included environmental risks such as geographic factors, environmental risks such as pollution, weather, currency fluctuations as a result of being exposed to foreign currency, and other such risks (Maletta, 1993). While the auditor is required to be aware of these risks, there is no procedure that the auditor can put in place to mitigate the risk. That in part is done by the entity's own internal control mechanisms and hence their management of 'Control Risk' (Hogan and Wilkins, 2008).

Control Risk:-

'Control risk' represents the auditor's assessment of the likelihood that a material misstatement in relation to a financial statement assertion will not be detected or corrected on a timely basis by the clients internal control system (Wiley, 2014).

All audits require testing of the clients internal control mechanism. The results of these tests will determine to what extent, if any, the audit firm will rely on the internal control mechanisms of the client (Wiley, 2014). In addition, no matter the extent and magnitude of a client's internal control systems, ISA 315 (Identifying and Assessing the Risk of Material Misstatement through Understanding the Entity and Its Environment) requires the auditor to tests and document the internal control system (IAASB, 2014d). It is submitted then, that the auditor by carrying out the audit is required to gain a thorough understanding of the client's internal controls, management integrity and overall governance of the entity by management. It is this testing that, to a large extent has played a significant role in determining the overall opinion expressed by the auditor (Wiley, 2014).

Detection Risk:-

'Detection Risk' is defined by ISA 315 as the risk that the auditors substantive testing will not detect a material misstatement (IAASB, 2014d). This risk is borne by the auditor. As with 'control risk', the auditor would need to balance this risk with how much reliance it can place on the client's controls. This would then lead to the audit opinion.

In order to effectively lower the 'detection risk' the auditor implements a variety of different quality safeguards as required by ISQC 1. According to ISQC 1 engagement teams require the necessary and appropriate skills and resources in order conduct the engagement quality control mechanisms include the allocation of an engagement partner who has sufficient time and skills necessary to lead the engagement (Maroun and Atkins, 2014). Each client has their own unique risk and quality control mechanisms that must address the risk-specific nature of the client, specifically the skill-set and appropriate supervision, monitoring and review of the less experienced engagement team by the more experienced team (Maroun & Atkins, 2014). An audit by its nature requires significant professional judgement and as such quality control mechanisms in place aim to cater for this judgement by requiring a mentoring and monitoring process by more experienced staff assigned to the audit (Maroun & Atkins, 2014). ISQC 1 requires consultation on difficult and contentious issues which should be appropriately documented and which will result in a lowering of 'detection risk' (Maroun and Atkins, 2014). Quality control is not static and audit firms should be continually reassessing their design operation and effectiveness of their quality control systems (ISQC 1). Specifically this should be carried out by senior and experienced partners and should be aimed at continual improvement and corrective action if required (Maroun & Atkins, 2014).

The KAM report aims to require disclosure of these quality control safeguards and implementations (Council). The inference would surely be that there is a lack of investor confidence in the audit opinions provided (Cordos and Fulop, 2015) or perhaps it is a case where the users of the financial statements and in turn those reliant on the audit opinion seeking additional comfort in that as expressed by the auditors.

Audit quality is of vital importance to the economy. As stated by (Cordos and Fulop, 2015), audit quality is a fundamental pillar of the audit market and that auditing and the audit itself has no value if the public has no confidence in the assurances given (Maijoor and Vanstraelen, 2012).

3.1 Key Audit matters linked to the audit opinion:

The word 'key' is defined by the Oxford English Dictionary (Simpson and Weiner, 1989) as 'of crucial importance', applying this to a key audit matter; one could translate this to an audit matter of crucial importance (Simpson and Weiner, 1989).

ISA 701:7 (Communicating Key Audit Matters in the Independent Auditors Report) defines a key audit matter as 'Those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period' (IAASB, 2015). It also states that key audit matters are selected from matters communicated with those charged with governance.

ISA 701:8 gives examples of such matters as matters ‘requiring significant auditor attention during the audit’ (IAASB, 2015). These include areas of significant risk as well as areas where professional judgement had to be used.

The main changes in audit reporting are aimed at reducing the information gap. The International Auditing and Assurance Standards Board (IAASB) has defined this gap as the difference between the information users desire and what is available to them through the entity‘s disclosures and the auditor’s report. It appears then that users and/ or investors in general may not have the appropriate skills set to analyse the annual financial statements and are thus looking for a summarised view from the auditor to give users more confidence.

For example, in the invitation to comment (Humphrey et al., 2013)

Schilder, the IAASB Chairman, (Schilder, 2011) states in his IAASB chairman's statement

> ‘What does today’s auditor’s report on financial statements deliver? It is generally a short, standardized report that describes the financial statements subject to audit, the audit itself and the respective responsibilities of management and the auditor. (-) The global financial crisis also has spurred users, in particular institutional investors and financial analysts, to want to know more about individual audits and to gain further insights into the audited entity and its financial statements. And while the auditor’s opinion is valued, many perceive that the auditor’s report could be more informative. Change, therefore, is essential.’

In providing the audit opinion the auditor provides assurance relating to the going concern of the entity. Going concern is one of the fundamental pillars of corporate reporting. IAS 1 requires the presentation of an entity’s financial statements using the assumption that the entity will be a going concern, i.e. able to settle its liabilities and realise its assets through the ordinary course of business activities (DeFond et al., 2002 , IASB, 2014)

One of the more serious cases of a corporate entering bankruptcy despite going concern assurances was that of Parmalat in 2003 when they were involved in a scandal amounting to around 8 million Euros (Demaki, 2011 , Cordos and Fulop, 2015). To this extent questions were posed as to the role of the auditor and that the audit opinion did not suggest there was a material concern with regards to the going concern of the entity in question (Melis and Melis, 2004).

In order for the auditor to express an opinion on going concern, the auditor must comply with ISA 570. (IAASB, 2014a)This standard sets out numerous substantive tests (Blay et al., 2007) required by the auditor such as discussions with those charged with governance, a review of managements future cash flow forecasts and budgets. The auditor is also required to take cognisance of market conditions, business conditions and the related environments and other relevant risks in order to reach an opinion of an entities going concern (IAASB, 2014a). It can be concluded, that the going concern opinion expressed by auditors is one of the most fundamental opinion made in the auditor's report (Asare, 1992) and has a high impact on investor responses judged by the market reactions from a change in going concern review (Chen and Church, 1996).

In addition, ISA 700 requires the auditor to be confident about an entities going concern in order to reach an unmodified or unqualified opinion (IAASB, 2014b). In the event that an entity has prepared its financial statements on the wind up basis, the auditor must highlight this to the users by way of an emphasis of matter paragraph (IAASB, 2014a). The international literature supports the significance of a going concern review, and suggests that the issuance of a going concern review by the auditor would potentially have an adverse effect on both the audit firm as well as the audit client (Carcello and Neal, 2000), (Antle and Nalebuff, 1991). The adverse effect from the client's perspective would be potential adverse market reactions to the going concern review. For the auditors, the potential negatives are fee pressure, a break down in the relationship between the client and the auditor and a higher chance of the client switching audit firms (Carcello and Neal, 2000).

It was noted during a presentation hosted by the South African Institute of Chartered Accountants on 19 May 2015 in Sandton that a likely area which would be included in the KAM report would be justification about the entities going concern review. In this presentation, it was suggested by Dan Montgomery, a previous IAASB Chairperson that 'the auditor is required to challenge the adequacy of going concern calculations and disclosure by management'. The suggestion was thus more of an interrogation of the calculations and assumptions made by management.

It is somewhat implied then that the going concern opinion in the audit report would always be a key audit matter. Hence, using the guidelines in the standard, the auditor would have to expand on the work conducted during the audit that allowed the auditor to reach this conclusion.

In a South African context, the roll out of auditors having to comply with the new audit reporting will be for all entities listed on the Johannesburg Stock Exchange (JSE) whose year-end reporting period is on or after 15 December 2016 (Nkonki, 2015). The decision to initially roll this out to listed companies is an interesting one.

On the one hand, it can be argued that the most prominent users of audited financial are investors of listed entities. All such shareholders are entitled to receive a set of the audited financial statements and use these for speculative investment purposes (Cooke, 1992). Since the audited results of these entities are in the public domain, one the one hand, it makes sense to roll out the changes in this context as this would appear likely to have the most material impact on the users of these annual financial statements, if at all (Nkonki, 2015).

This in turn could, and in all probability would, expose the audit opinion and the justification of the opinion made by the auditors into the public domain. Thus, this would expose the new standards into a live environment and provide very real and accurate feedback as to what reaction the market will have to these enhanced disclosure, if any (Nkonki, 2015).

This in turn may then influence the decision of the IAASB as to whether this enhanced disclosure should be made mandatory to all those entities requiring or producing and audited set of accounts. In summary then, a logical methodology being requiring the approximately 400 listed companies who produce audited accounts to have their audit opinion's disclosure (Bédard et al., 2014).

However, empirical research carried out in Europe (Section 4) points to the fact that the market did not react materially or significantly at all to the additional reporting (Bedard et al., 2014). Should a similar pattern present itself in South Africa, is this perhaps a case then of diminishing the relevance of the new ISA 701 (IAASB, 2015)? The lack of relevance may increase the risk of the exercise being reduced to a compliance based, tick box, boiler plate type approach as evidenced in France from 2003 – 2007 (Bédard et al., 2014).

4. UNINTENDED CONSEQUENCES OF THE PROPOSED INTRODUCTION OF THE KEY AUDIT MATTERS (KAM) STANDARDS

Unintended consequences is the consideration of the failure to match the reality of economics to the regulatory approaches adopted and thus leading to results which are contrary to the objective of improving audit quality (Knechel and Shefchik, 2014). In considering section 3 appears as if the introduction of the KAM is aimed at reducing the 'information gap' (Robert Knechel et al., 2015) but what is of concern is that the idea that it is up to the discretion of the auditor to decide which professional judgements should be included as part of the key audit matters based on professional judgment and in view of the steps taken throughout its audit (Lessard, 2006), (Bédard et al., 2014). It can then be purported that the opinion of the auditor would not change as a result of being compelled to disclose key matters as ultimately the standard still seeks the auditor to express his / her opinion using the appropriate levels of professional scepticism and judgement (Lessard, 2006), (Bédard et al., 2014). It is also then deduced that the auditor's opinion would not be able to differ, potentially leaning more on the side of unqualified simply by disclosing in more detail the issue, or potential issue that is causing the auditor some concern(Lessard, 2006), (Bédard et al., 2014). The KAM would serve then purely as a mechanism to allow users greater insight into the issue and not how the auditor firm reached its conclusion (Lessard, 2006), (Bédard et al., 2014). The implementation of the Reportable Irregularity (RI) is a further example of an instance where South Africa adopted a new standard based on international similarity and ended up having a very minor, if any, impact on the local audit reporting (Maroun, 2015b).

Over time, they may become boilerplate (Footprint Consultants, 2011) and auditor liability concerns may result in auditors reporting on as few matters as possible or providing a lengthy list of redundant disclosures (IAASB 2012a), the disclosures may not be easily understandable because of the use of technical language (Footprint Consultants, 2011), they may result in excessive other reporting that might cause the auditor's report to be ambiguous and an additional significant cost with questionable benefit.

The idea that auditors should disclose more detailed reports spreads widely since the 2008 financial crisis. The IAASB, the PCAOB and the European Commission are particularly favourable to the disclosure of Key Audit Matters (or Critical Audit Matters) by auditors. A few years ago, such a debate existed in France, where auditors are required to justify their assessments since 2003.

In further exploring this unintended consequence raised above a research study was performed in France, which has introduced this legislation under the provision of commentaries called "Justification of Assessments" (JOA) in their audit report (Bedard et al., 2014). A study was performed on this JOA by sampling 953 audit reports and studying the reaction of the French financial market at the announcement of the JOA's. Their findings revealed that the reaction of the market after the release of the JOA's were not different at all, suggesting a minimal if any impact on investors.

Their study produced three significant findings in France:

1. The quality of the audit using earnings management as a proxy was not affected by the JOA.
2. The cost of the audit after including JOA's was not significantly modified (The JOA's were generally approximately 2 page reports). Resultantly, the quality to cost ratio was not modified at all.
3. However, the efficiency lag (measured as the time between conclusion of the audit and issuance of the audit report) had improved slightly. This is in contrast to concern expressed. (Bédard et al., 2014)

Their research suggests that although the market in France appeared non-reactive to Key audit matters, it was suggested that in other economies, potentially in those countries where smaller minorities have the power to sue auditors there may be more significant reaction (Bedard et al., 2014).

In considering Section 4 further unintended consequences may also result.

Such key consequences, raised as questions, could be:

1. What if the content is confidential in terms of potentially confidential client information and its strategy, i.e. if key to the client's going concern is a strategic policy or decision or product that the client would not want disclosed in a public forum.
2. Does the auditor's disclosure or expansion of its audit procedures carried out leave the audit firm vulnerable to external scrutiny and / or potential litigation?

This paper suggests that requiring auditors to expand and justify their going concern work performed to justify their opinion can and will prove problematic. In particular, and as suggested by the IAASB that these key audit matters should be unique to each client and not boiler plate or templates.

The literature suggests that the audit opinion is to an extent not only a statement from the auditor, but rather a form of joint statement from both client and auditor (Antle and Nalebuff, 1991). This literature suggests that the final opinion is the result of many discussions and negotiations between client and auditor which may result in adjustments passed and opinions modified to an acceptable level to both client and the auditor. The authors describe the final audit report and audited financial statements as the 'final negotiated outcome'.

It is in this vein where the author sees a potential pitfall and an unintended consequence with going concern being expanded on in the key audit matter.

In a South African context, there is little evidence, if any to suggest that going concern audit work is inadequate. In addition, ISA 570 has been updated over the last few years to address areas of concern, primarily in terms of what is a material uncertainty and gives the auditor guidance in this regard (IAASB, 2014a).

With this in mind, is the Key Audit Matter disclosure, in particular with regards to going concern in fact relevant in the South African context? This research suggests that initially not and that further in depth research into this area should be undertaken before the systemic roll out of such reporting requirements in South Africa. This is further corroborated by (Bédard et al., 2014) whose empirical evidence suggested that in France, there was very little, if any, reaction by the market to entities whose first time audit reports included a Justification of Assessment, also known as a Key Audit Matter in a South African context.

With this in mind, and as confirmed by Mr Montgomery that going concern is most likely to be a key audit matter, there is a risk of firms using boiler plate (Auditing and Board, 2011), (Bédard et al., 2014) or template type methodology to disclose these key audit matters. Carcello et al. (2002) (Carcello et al., 2002) suggest that it is these very type of boiler plate type reporting in the United States of America (U.S.A) that detracted from the audit committees taking responsibility for the audits and their actions by producing long lists of to whom they discharged their obligations rather than how these obligations were discharged.

Bédard et al. (2014), states however, that prior research conducted in Europe suggests otherwise. In their evaluation, and corroborated by (Church et al., 2008), that the audit report is merely a symbolic gesture. This is as they state because investors permanently revise their expectations and do not wait for the auditor report. The same may thus hold for going concern review. The same may apply for the auditor expressing their opinion on the entity's going concern. This research thus suggests that the users, in more particular the financial markets (Bedard et al., 2014) reaction does not depend on the content of the audit report, even if it is more elaborate and more detailed. This may be aggravated or exacerbated by the fact that the audit report including the key audit matters will be longer and runs a risk of being to standardise i.e. boiler plate and template type reporting, too detailed and in fact too complex to be deemed useful.

An additional concern is that the manner in which this new regulation is imposed and managed may have far-reaching consequences for the audit profession (Knechel and Shefchik, 2014)
This legislation may result in causing auditors to continually defend their judgments, to answer for alleged failures in audit documentation that do not translate into broader audit failure, and to be belittled in front of the public and clients is thus unlikely to improve their professional standing, attitude or satisfaction in providing professional services(Knechel and Shefchik, 2014). What may in turn result is an extremely negative environment that damages the already fragile 'trust-relationship' between auditor and client. Despite the actual increase in legislation the result could be an increase in the drain of professional talent and certainly a long-term deterioration of the profession and a further reduction of the economic benefits and rewards of the profession (Knechel and Shefchik, 2014). Failure to match regulatory actions to the true economics of the audit profession increases the risk that these negative, but unintended, consequences may eventually arise (Knechel and Shefchik, 2014)A greater concern is that this increased legislation could result in an exacerbation of the regulatory audit problems currently facing the profession (Knechel and Shefchik, 2014).

5. CONCLUSION

This article has provided an exploratory account of the introduction of the key audit matters standard (KAM) in a South African context. KAM and the reporting thereof is a fundamental shift in the nature of the audit report. As demonstrated by the literature, the effect on audit risk will need to be considered. It is suggested that in order for auditors to seek protection from not disclosing a key audit matter, audit reports may contain longer key audit matter reports in order to mitigate any potential risk which the literature suggests may cause boiler plate type reporting.

Auditors will need to further substantiate their findings, particularly with regards to their clients going concern. By highlighting procedures performed and potential assumptions made, indirectly then, the auditors may be disclosing what procedures were not done or not performed which could raise questions by potential investors and users that ordinarily would not have been posed. A critical concern has been raised which is that a case of increased transparency and legislation may in fact lead to an increase in 'questioning' and a potential decrease in the level of trust and confidence associated with the audit report thus exacerbating an already fragile auditor-client relationship and adding an additional significant burden onto the already arduous profession.

JSE listed entities and their auditors will be the first to embark on this journey. This can be seen as a bold move by the regulator, a demonstration of their sound belief in the principles associated with increased transparency with a view to greater investor confidence. On the other hand, any pitfalls and unintended consequences may be materially felt, and if this is the case, then could the regulator rather have considered a more conservative roll out such as requiring a sample of non-listed entities to embark on this voyage first? Time will tell (Schiefer, 2014) and that time will commence 15 December 2016.

In reaching this conclusion, it must be noted that this study is not without limitations. It concentrates in an exploratory fashion only on the KAM introduction in South Africa to inform the on-going debate. Future research needs to expand on this by examining the advantages and disadvantages of equivalent legislative introductions in other jurisdictions. In addition, this article has not carried out a detailed empirical analysis. Given the lack of formal literature on the KAM in South Africa, a qualitative study was best suited to offering initial insights. Subsequent work may expand on this in a positivist setting – for example, by creating a model to predict future costs, consequences and the negative impact on the auditing profession after the introduction of the KAM.

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