AUSTRALIAN AUDITING STANDARDS

FACT SHEET FOR MANAGEMENT, DIRECTORS AND AUDIT COMMITTEE MEMBERS

ASA 580 Management Representations

OBJECTIVE

The objective of ASA 580 *Related Parties* is to prescribe mandatory requirements for auditors regarding the use of management representations as audit evidence, the procedures to be applied in evaluating and documenting management representations and the action to be taken if management refuses to provide appropriate representations.

APPLICATION

Financial reporting periods commencing on or after 1 July 2006.

ACKNOWLEDGMENT BY MANAGEMENT OF ITS RESPONSIBILITY FOR THE FINANCIAL REPORT

The auditor, under ASA 580, is required to obtain sufficient appropriate audit evidence that management acknowledges its responsibility for the fair presentation of the financial report in accordance with the applicable financial reporting framework, which generally in Australia will be the AASB Standards, and has approved the financial report. The guidance in ASA 580 explains that the auditor can obtain audit evidence of management's acknowledgement of such responsibility and approval from relevant minutes of meetings of those charged with governance, or by obtaining a written representation from management or a signed copy of the financial report.

The auditor's responsibility to obtain and document representations from management

Under ASA 580, the auditor is under an obligation to endeavour to obtain appropriate representations from management. In particular, written representations must be sought on matters material to the financial report, when other sufficient appropriate audit evidence cannot reasonably be expected to exist. Other representations the auditor is obliged to seek concern management's acknowledgement of its responsibility for the design and implementation of internal control to prevent and detect error; and it's beliefs that the effects of those uncorrected financial report misstatements aggregated by the auditor during the audit are immaterial, both individually and in the aggregate, to the financial report taken as a whole. A summary of such items is to be included in or attached to the written representations.

The guidance in ASA 580 explains that during the course of an audit, management makes many representations to the auditor, either unsolicited or in response to specific enquiries. When such representations relate to matters which are material to the financial report, the auditor ordinarily needs to:

- seek corroborative audit evidence from sources inside or outside the entity;
- evaluate whether the representations made by management appear reasonable and consistent with other audit evidence obtained, including other representations; and
- consider whether the individuals making the representations can be expected to be well informed on the particular matters.

The guidance goes on to explain that representations by management cannot be a substitute for other audit evidence that the auditor could reasonably expect to be available. If the auditor is unable to obtain sufficient appropriate audit evidence regarding a matter which has, or may have, a material effect on the financial report, and such audit evidence is expected to be available, under ASA 701 *Modifications to the Auditor's Report*, this will constitute a limitation on the scope of the audit, even if a representation from management has been received on the matter.

In certain instances, audit evidence other than that obtained by performing enquiry may not be reasonably expected to be available; therefore the auditor ordinarily obtains a written representation by management.

Under ASA 580, the auditor is under an obligation to, if a representation by management is contradicted by other audit evidence, investigate the circumstances and, when necessary, reconsider the reliability of other representations made by management.

ASA 580 Management Representations

THE AUDITOR'S ACTION IF MANAGEMENT REFUSES TO PROVIDE REPRESENTATIONS

Under ASA 580, the auditor is under an obligation to, if management refuses to provide a representation that the auditor considers necessary, treat this as constituting a scope limitation and express a qualified opinion or a disclaimer of opinion. In such circumstances the auditor would ordinarily:

- evaluate any reliance placed on other representations made by management during the course of the audit;
- draw to the attention of those charged with governance or management any relevant statutory and/or regulatory provision which gives the auditor access to records and information; and
- consider if the other implications of the refusal may have any additional effect on the auditor's report.

BASIC ELEMENTS OF A MANAGEMENT REPRESENTATION LETTER

The management representation letter should be addressed to the auditor, contain specified information, and be appropriately dated and signed. It would ordinarily be dated the same date as the auditor's report. However, in certain circumstances, a separate representation letter regarding specific transactions or other events may also be obtained. This letter is ordinarily be signed by the members of management who have primary responsibility for the entity and its financial aspects, (eg senior executive officer and senior financial officer), based on the best of their knowledge and belief. In certain circumstances, the auditor may wish to obtain representation letters from other members of management. For example, the auditor may wish to obtain a written representation about the completeness of all minutes of the meetings of shareholders, the board of directors and important committees from the individual responsible for keeping such minutes. Appendix 1 to ASA 580 provides an example management representation letter. Listed below is an extract of items from that Appendix illustrative of representations typically sought by an auditor.

"We confirm, to the best of our knowledge and belief, the following representations made to you during your audit.

1. We have made available to you:
   (a) all financial records and related data, other information, explanations and assistance necessary for the conduct of the audit; and
   (b) minutes of all meetings of [shareholders, directors, committees of directors].
2. There:
   (a) has been no fraud, error or non-compliance with laws and regulations involving management or employees who have a significant role in internal control;
   (b) has been no fraud, error or non-compliance with laws and regulations that could have a material effect on the financial report; and
   (c) have been no communications from regulatory agencies concerning non-compliance with, or deficiencies in, financial reporting practices that could have a material effect on the financial report.
3. We acknowledge our responsibility for the design and implementation of internal control to prevent and detect error. We have established and maintained adequate internal control to facilitate the preparation of a reliable financial report, and adequate financial records have been maintained. There are no material transactions that have not been properly recorded in the accounting records underlying the financial report.
4. We believe the effects of those uncorrected financial report misstatements aggregated by the auditor during the audit are immaterial, both individually and in the aggregate, to the financial report taken as a whole. A summary of such items is attached.
5. We have no plans or intentions that may materially affect the carrying values, or classification, of assets and liabilities.
6. We have considered the requirements of [AASB 136, "Impairment of Assets",] when assessing the impairment of assets and in ensuring that no assets are stated in excess of their recoverable amount.
7. The following have been properly recorded and/or disclosed in the financial report:
   (a) related party transactions and related amounts receivable or payable, including sales, purchases, loans, transfers, leasing arrangements and guarantees (written or oral);
   (b) share options, warrants, conversions or other requirements;
   (c) arrangements involving restrictions on cash balances, compensating balances and line-of-credit or similar arrangements;
   (d) agreements to repurchase assets previously sold;
   (e) material liabilities or contingent liabilities or assets including those arising under derivative financial instruments;
   (f) unasserted claims or assessments that our lawyer has advised us are probable of assertion; and
   (g) losses arising from the fulfilment of, or an inability to fulfil, any sale commitments or as a result of purchase commitments for inventory quantities in excess of normal requirements or at prices in excess of prevailing market prices.
8. There are no violations or possible violations of laws or regulations whose effects should be considered for disclosure in the financial report or as a basis for recording an expense.
9. The entity has satisfactory title to all assets, and there are no liens or encumbrances on such assets nor has any asset been pledged as collateral. Allowances for depreciation have been adjusted for all important items of property, plant and equipment that have been abandoned or are otherwise unusable.

10. The entity has complied with all aspects of contractual agreements that would have a material effect on the financial report in the event of non-compliance.

11. There were no material commitments for construction or acquisition of property, plant and equipment or to acquire other non-current assets, such as investments or intangibles, other than those disclosed in the financial report.

12. We have no plans to abandon lines of product or other plans or intentions that will result in any excess or obsolete inventory, and no inventory is stated at an amount in excess of net realisable value.

13. No events have occurred subsequent to the balance sheet date that would require adjustment to, or disclosure in, the financial report.

We understand that your examination was made in accordance with Australian Auditing Standards and was, therefore, designed primarily for the purpose of expressing an opinion on the financial report of the entity taken as a whole, and that your tests of the financial records and other auditing procedures were limited to those which you considered necessary for that purpose.

Yours faithfully

[Name of signing officer and title]"

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