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The Opinion Paragraph in the Auditor's Report: The Bane of Auditing

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ABSTRACT

The major threat in the accounting profession around the globe is the problem of corporate business failure. No doubt, strict efforts have been put in place to combat the problem of corporate business failure as well as limit the expectation gap, but all to no avail. At different stages and years, the opinion paragraph was changed severally; there were also conflicts to change the phrase from the term 'fairly present' to 'presents fairly' because fairness is a term that is imprecise. It was in a bid to proffer solution to the existing problems and hence narrow the expectation gap that suggestion (recommendation) was made to revert back to the previously used wordings of the opinion paragraph which were: "We certify that the above balance sheet (financial statement) in our opinion is a correct statement of the financial position of the company as of 31st Dec xxx and the accompanying profit and loss statement is correct"

Keywords: Opinion Paragraph, Fairly Present, Auditor's Report and Financial Statement.

INTRODUCTION

Corporate Business failure has drawn considerable attention all over the world (Apotu & Isreal, 2014). It has shown that those who are the master mind of the financial statement cannot be singled out from the problem of business failure because it has become a threat to growth in accounting profession around the globe. Enyi, Ifurueze & Enyi, (2013) posits that any subsequent failure of business resulting from management misconduct, fraudulent practices, and economic instability are viewed as failures of auditors. The fact remains that no matter how this is argued, the value/duty of the auditor should not begin from where the work of the management ended but should be a total scrutiny of all aspects of work carried out (from scratch to finish). If it should be viewed as what the management/directors have done, then whose opinion is reported in the opinion paragraph? Because as it is, the opinion paragraph stands as the heart of the audit report, the summary of the report and as such the center point of attraction.

In the opinion paragraph, the auditor should report his observations on the financial position of the company; he should address those illegal/unethical behaviors identified within the company. Enyi, et al (2013) suggested that the auditor should not be seen as translating the illegal behaviors as legal behaviors which obviously are done to satisfy his demands. The auditor must be mindful of the fact that any unethical behavior could result to the entire profession being under fire or may lead to the destruction of the fundamental nature of auditing while the management is being exonerated.

Enyi, Ifurueze & Enyi, (2013) further emphasized that the role of the 21st century auditor is to redefine, refocus on public interest and the duty of separating non-audit functions (the roles expected of the Auditor today). These arguments are immaterial and will further widen the expectation gap. This is because Fraud/corruption still remains the major problem in the modern day business and has not changed. And it is almost emphasizing that the Auditor has lost touch of the aim of his employment.

In agreement with Boydet (2001) in Enyi, et al, (2013) they emphasized that bridging the expectation gap will take forever if the problems of corporate business failure are not addressed now or the auditor accepting the responsibility of detecting fraud are not corrected. They further stated that the auditor should retract his steps, go back to the drawing board, drop the attitude of self defence and self preservation to meeting society's expectation. They should extend their services as to where more work should be done to detect fraud and more internal control audits should be carried out. However, since efforts have been put in place all over the globe to combat the corporate business failure but have not yielded good results, it is worthwhile for the profession to look elsewhere for solution to this problem. May be it is time for the profession to look at the opinion paragraph of the auditor's report which may be the major culprit.

In Boockholdt (2014) it was stated that there has been a long standing debate on the form and content the auditor's report would take; he emphasized that an early Audit Practitioner was evident in the 1840s in the United States and in Great Britain. That in the 19th century by 1846 to be precise, auditing became prominent to the extent that auditing was done twice a year; the audit committee stood as the accountant of the company as well as the auditor of the company with an audit committee of two to three persons and a hand written audit report (this was the first audit opinion recorded). And their duty at that time was to audit all vouchers before they were paid by the treasurer.

McKee, (1870) espoused that by the 19th century, there was evidence of independent accountants and bookkeepers who used to assist the audit committee. Also the accountant was used as an auditor and employee of the company because of their ability to detect fraud. This was the first time an auditor is used for fraud prevention. That is, the accountant played the role of an auditor and an accountant at the same time.

To explicitly explain this, it was stated in the newly created Statement on Auditing Standards (SAS) No. 99 (consideration of fraud in a financial statement audit) which is similar to SAS 53 and 82, International Standard of Auditing Regulations Nos. 240 and 700 of the UK (which guides the Nigerian accounting body), which all emphasized that in assessing fraud risk, auditors should gather much more information or substantial information to uncover fraud (DeZoort & Lee, 1998). This is because it is the duty of the audit team to inform the client that fraud can cause harm to the client's company (Brickner & Peason, 2003). And in Chandler, Edwards & Anderson, (1993), it was equally stated in the accounting policies that in the past, the duties of the accountant was to detect fraud and irregularities; later, however, the main objective changed from fraud detection to 'verification of financial statements' which came as a result of changes in the opinion paragraph.

In the light of this, it shows that prior to this period, the accounting profession was actually into fraud detection but suddenly towards the 19th century a decision was made for auditors not to detect fraud and irregularities but rather verify data and information among others. This indeed, has to a large extent widened the expectations of the investors. Others like Sweeney, (1997) argued strongly that the only way of bridging the expectation gap, is by combining the nature of the audit function with user expectations.

Evolution of the Opinion Paragraph of the Auditor's Report

In the past, Accounting and Auditing professions had no standards backing the presentation and preparation of audit reports. At that time, what was available was a free form audit report (PCAOB, 2010). That is, by 1840s in the United States and in Great Britain auditing was performed only by the audit committees; the auditor's opinion and the entire auditor's report were hand written at that time. Brewster, (2005) espoused that financial statement prepared at that time was not well understood by the general public because all the accounting principles were suggested by accountants. The Steel Company called the United States Steel was the first to publish a financial statement and an auditor's opinion (Hermann, 2014). Doron, (2015) and Wiesen, (1978) confirmed that at that same time, people had little knowledge of auditing.

It was also emphasized that by 1903, audit opinion was still at its inception and there were series of changes in the auditor's report. The first change observed in the form of reporting the opinion paragraph which stood as the heart of the report was showcased firstly in 1903 where the wordings were stated as "we have verified cash and securities by actual inspection, and full provision has been made for bad and doubtful accounts receivable and for all ascertainable liabilities". This shows that proper scrutiny was made at that time, there was physical cash count and asset verification was significantly done.

The second change observed in the form of reporting the opinion paragraph was showcased in a bid to reduce the audit report to a single paragraph (PCAOB, 2010) and to promote uniform accounting. Another change took effect in 1920 with the wordings "we certify that the above balance sheet in our opinion is a correct statement of the financial position of the company as of 31st Dec 19xx and the accompanying profit and loss statement is correct."

Flesher, Burkett & Flesher (1996) emphasized that by 1933 auditing and accounting were still in a state of change and it was declared that the company should be responsible for its own actions. It was observed that during that period, the wording of the opinion paragraph was stated: "its financial statements fairly presents, in accordance with accepted principles of accounting, the financial position of a company"

Macneal (1939) defended the accounting profession and further criticized it stating that "though the accounting profession is not dishonest, yet upon the passage of a law, their profession, without a single important exception, felt impelled to change its form of certificate from one which states that "its financial statements fairly present in accordance with accepted principles of accounting, the financial position of a company" to the one that "presents fairly". He further exclaimed that accounting principles and the truth do not make good bedfellows".

Baxter and Davidson (1959) further stated that since the accountants changed the opinion paragraph from what it previously was "We certify that the above balance sheet in our opinion is a correct statement of the financial position of the company as of 31st Dec 19xx and the accompanying profit and loss statement is correct" to "In our opinion, the accompanying balance sheet and profit and loss statements fairly presents in accordance with accepted principles of accounting consistently maintained by the company under examination, its position and results of the operation for the year". It has shown that the statement presented in the financial statement is stating the opinion of the auditor but are not factual. And with that change, the financial statement will be viewed as a report that does not carry true information.

Prior to the year 1950, the audit report including the opinion paragraph were reduced in length to a single paragraph which was called bookkeeping audit. Due to lack of operational standards, most times, circumstances were the main causes of change to the report. This was because, after the amendment stated above, the reports were amended again to suit the situations at hand. This time it was the ultramares case that brought about the change in the reports (Solomon, (1968) and PCAOB, 2010). And this time the term "certify" began to disappear from the reports in an attempt to clarify that the report was an opinion and not a guarantee (Samsom, 1970). Thereafter, the wordings were then reverted to "In our opinion, the financial statement presents fairly"

By 1960, the wordings of the opinion paragraph were stated thus: In our opinion, the accompanying balance sheet and profit and loss statements present fairly the financial operations of the company from the date of inception to 19xx. At this point, the word "certify" had been removed and the word "In our opinion" was used. By the year 2000, which is before the year (2001) when IFRS was introduced all over the world as the global language. the wordings were seen as "In our opinion, the financial statements present fairly in all material respect, the financial position of XYZ as at 20XX and the results of their operation…. in conformity with accounting principles generally accepted in the country".

By the year 2016, the wordings of the opinion paragraph was stated as "In our opinion, the financial statements give a true and fair view (presents fairly) of the financial position of XYZ as at 20XX and its financial performance, changes in equity and cash flow in accordance with IFRS, CAMA and the FRCN Acts 2011". This has shown that there were little changes in the opinion paragraph before and after IFRS was introduced, the only significant changes were in Financial Regulations and standards. All the changes poured out above are aimed at limiting expectation gap and to emphasize that audit report (in line with Zeff, (2007) recommendation) should be an opinion and not a guarantee.

As a matter of emphasis, the change shown above from "we certify" to "in our opinion" had long been debated. This argument went on and it is worthy of note that by the year 1933, it was declared by some special committee that though auditing was in its infant stages, great liability should be imposed on the accountant because accounting was a profession concerned with the declaration of opinion. The accountant or auditor should be looked at as a watch dog and must be ready to work through all working papers tirelessly. Impliedly, the auditor's report is not in its entirety a statement of fact but are expressions of opinion based partly on conventions, assumptions and judgments which can vary at will, but can be relied upon because it is based on accounting conventions and assumptions which are reliable judgments.

In conformity with why the changes made in the opinion paragraph were necessary, this was clearly stated in a paper written by Institute of Chartered Accountants England and Wales (ICAEW, 2009) on changes in financial reporting and audit practice. It was stated that the problem with auditing could be because "Some things are objectively very much harder to audit than others, but auditors make them auditable: auditing is an art; the auditing profession takes responsibility for developing practice in new areas. However, not all items are auditable and it would be better for the auditors to acknowledge that such items are un-auditable due to paucity of information". In other words, whatever is un-auditable should be fairly disclosed to the parties involved and this will minimize litigation cases and corporate business failure.

The historical background of the term "Presents Fairly" (Pass/Fail Model)

The presents fairly model which first appeared in US Financial Reporting Regulations in 1939 was introduced as a result of audit expectation gap. Though the true and fair view is seen to be an equivalent of presents fairly, but it is believed that true and fair view does not comply with the GAAP, and that the word fair stands for partial assurance (Ngaire, 2006)

Wiesen, (1978) stated that between 1933 and 1934 there was a remarkable change in the accounting and auditing standards for listed companies on the US stock Exchange. as written in 1934 in a document called Audits of Corporate Account. This document led to the development of accounting principles. It was this same document that introduced the popular terms used in today's auditor's reports such as "accepted principles of accounting" and "accounting principles". And the document paved way for a standard form of auditing report and incorporated in the reports the term "presents fairly (pass/fail model)" and eliminated the words "we certify" in favor of "in our opinion" (McEnroe & Martens, 1998, Parker & Nobes, 1994).

Looking at the meaning of the term "presents fairly" it gives just one meaning but to the auditor, it could mean more than that. In the words of Zeff, (2007), he stated that when the words "presents fairly and were prepared in conformity with generally accepted accounting principles" are being used, it obliges the external auditor to give two opinions or is looked at as separate opinions and not just a single opinion (Mano, Mouritsen, and Pace, 2006). Due to this inconsistency facing the accounting profession, by 1939 the word "fairly presents" and "in accordance with accepted principles of accounting" were altered to "presents fairly … , in conformity with generally accepted accounting principles" by the AIA's Committee on Auditing Procedure (Stewart, (2015), Previte & Flesher (2015), Zeff, (2007).

According to Al Sommer, (1975) in Zeff, (2007) they described fairness as truthfulness because fairness of financial statements poses an opportunity to move away from the rigidities of generally accepted accounting principles and other deterrents to meaningful financial disclosure. According to Aguolu, (2008) he described "true" as consistency with relevant facts and described "fairness" as a word that is imprecise because it involves a number of thoughts; fairness means expectation, relevance, objectivity and freedom of bias. In the light of this, the term "presents fairly" could be extended to mean "a true and fair view" and that showcases the reason why the auditors have decided to now parenthesize the opinion paragraph to stand as this: "In our opinion, the financial statements give a true and fair view of (or "presents fairly, in all material respects,") the financial position of the company as of Dec 19XX, and of the financial performance and its cash flow for the year then ended in accordance with international financial reporting standard".

Further on this, Ngaire, (2006) espoused that the American Institute of Certified Public Accountants (AICPA) recommended that "presents fairly" be deleted from the auditor's report because fairness "is not a property that can be objectively measured by the auditor". In 1980, due to the pressure from different bodies on the removal of the word "fairly", the Auditing Standards Board "proposed the deletion of "fairly" from the auditor's report stating that the word "fairly" is subjective and is interpreted differently by different users of the auditor's report but after considering so many issues, the board decided not to delete the word from the report. To this end, the word was actually in contention because some believed that the auditor only uses it to hide behind the GAAP which means shying away from responsibilities and preventing litigation issues but they forget that to be a perfect accountant, one has to have the sense of dignity, integrity, honesty, being impartial etc (Turner, 2005, Ngaire, 2006).

To addition to the above, Zeff (2007) reported that the comma in the word "present fairly" kept appearing and disappearing as time went on. It was seen that by the year 1988 the comma was removed and by 1992 it appeared and disappeared again in the year 2000 signifying that the comma had no substantial value in the opinion paragraph since it can be used at will (Zeff, 2007).

Above all, this study agrees with Baxter and Davidson, (1959) that the accounting profession is not dishonest and as much as IFRS is the global language, the true and fair view remains a fundamental issue in the accounting profession. This is because the overriding objective in the profession, as well as the aim of the audit report, is basically to achieve a view that is original and without bias. Hence, other changes from the disappearing of the comma to changes in the term presents fairly were evidences of improvement in the profession which has gotten the accounting world to greater achievements today.

SUMMARY/CONCLUSION

Auditing has passed through series of changes which has watered down the **heart** and **substance** for a proper audit. The evolutionary phases in the opinion paragraph of the auditor's report in the 1840's in the United States and in Great Britain started as a free form audit. Thereafter, the opinion paragraph which stood as the heart of the report was showcased firstly in 1903 and the wordings were stated as:

> *"We have verified cash and securities by actual inspection, and full provision has been made for bad and doubtful accounts receivable and for all ascertainable liabilities"*
>
> *By the year 1920 it was thus: "we certify that the above balance sheet in our opinion is a correct statement of the financial position of the company as of 31st Dec 19xx and the accompanying profit and loss statement is correct."*

By 1933 the wordings were seen as

> *"its financial statements fairly present, in accordance with accepted principles of accounting, the financial position of a company". This time the wordings were not faulted but the phrase "fairly present"*

By 1960, the wordings of the opinion paragraph were stated thus:

> *In our opinion, the accompanying balance sheet and profit and loss statements present fairly the financial operations of the company from the date of inception to 19xx.*

But in the year 2000 and up till the emergence of International Financial Reporting Standard (IFRS), the wordings were:

> *"In our opinion the financial statements present fairly, in all material respect, the financial position of XYZ as at 20XX and the results of their operation, in conformity with accounting principles generally in the country"*

And with the introduction of IFRS, the wordings of the opinion paragraph became

> *"In our opinion the financial statements gives a true and fair view (presents fairly) of the financial position of XYZ as at 20xx and its financial performance changes in equity and cash flow in accordance with IFRS, CAMA and the FRCN Act 2011".*

From the above, the auditor's opinion paragraph has undergone several changes and adjustments. The change from "**we certify**...." which ensured that the auditors did their job with maximum devotion to a mere expression of opinion "**in our opinion ... present fairly ....**"

It is obvious that these changes destroyed the heart and soul of auditing, and therefore has taken a toll on the credibility of the accounting profession, and by extension widened the audit expectation gap.

RECOMMENDATIONS

Auditing, and by extension accounting profession has known no peace since the changes in the opinion paragraph of the auditor's report due to many cases of audit failures which has led to the collapse of many giant corporations and companies.

The resultant effect is that these audit failures took a toll on the creditability of the accounting profession. Therefore, it is being recommended that for auditing to recover its balance, it is important and pertinent for the profession to revert back to the previously used wordings of the opinion paragraph which were

> *"We certify that the above balance sheet (financial statement) in our opinion is a correct statement of the financial position of the company as of 31st Dec xxx and the accompanying profit and loss statement is correct"*

By so doing, it will limit the expectation gap created; and will further force the auditors to roll up their sleeves and do the work they are being paid for. This is because financial regulations and code of ethics alone have not and will not solve this huge problem.

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