

International Auditing and Assurance Standards Board  
529 5th Avenue  
6th Floor  
New York  
New York  
10017

21 November 2013

Dear Sirs

**Response to Exposure Draft – Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing (ISAs)**

We welcome the opportunity to respond to the above exposure draft and wish to express our appreciation at the responsiveness of the International Auditing and Assurance Standards Board (“the IAASB”) to comments it received during the initial Invitation to Comment (“ITC”).

There has been tremendous progress since the ITC, and the current exposure draft goes a long way to achieving enhanced communicative value in the auditor’s report which will benefit all stakeholders. We believe however that there are still some matters which need to be addressed before the new and revised ISAs are released, as discussed below and as detailed in the appendix to this letter. Our main concerns relate to:

- Some of the proposals will simply lead to further boiler plate language being incorporated in the audit report, specifically a statement about the appropriateness of the use of going concern. It is also possible that auditors will err on the side of caution, and develop certain “standard” key audit matters for inclusion in the auditor’s report. This will be contradictory to the objectives of the proposals to enhance the value of auditor reporting.
- We believe it possible that the proposals could result in a delay in financial reporting in some cases. There will necessarily be discussions between the auditor and those charged with governance (“TCWG”) and management about the key audit matters to be reported by the auditor. This is likely to require significantly more time in some cases. There may be an added risk that it could deter open and honest two-way communication between the auditor and the client.
- Requiring comment on going concern separately in all cases may lead to additional confusion amongst users and add to the expectation gap, real or perceived. We also believe this could be considered a “piece-meal” opinion on an isolated area relevant to the financial statements. The need for positive conclusions on the appropriateness of the use of going concern is one that should be addressed by accounting standard setters, as it is management that makes this assertion in the first instance. We encourage the IAASB to address this through its outreach activities, rather than placing requirements on auditors to clarify an accounting concept which may not be well understood by users.

- Clarification is required on how key audit matters relate to significant risks, matters communicated to TCWG and completion memoranda, as non-inclusion of these areas as key audit matters could lead to continual challenge of the auditor's judgment by regulators and expose the auditor to litigation.
- The proposals acknowledge that there may be instances where no key audit matters are identified and reported. There is however potentially contradictory language in the exposure draft, as key audit matters are described as the matters the auditor determined to be of "most significance" in the audit. This implies that there will always be matters that are more significant than others, even where such matters are not considered particularly significant.
- Clarity is required for non-listed entities when the auditor needs to signal intent to report "key audit matters" in the engagement letter, as this suggests that the auditor will know of the existence of key audit matters before the audit has been started. While reporting of such matters may be agreed by engagement, audit results could prompt the auditor to include such matters even when not agreed in advance.

Finally, in light of the Public Company Accounting Oversight Board ("PCAOB") project on the same topic, we are of the view that it would be best for the public interest and the profession as a whole if the projects from the two standard setters were as consistent as possible. While we appreciate the independence of each standard setter, differences in approach will have negative consequences, and we encourage the board to make every effort to align the outcomes of its project with those of the PCAOB. We will urge the PCAOB to do the same.

If you would like to discuss any of our concerns and comments, do not hesitate to contact me.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Theo Vermaak', with a horizontal line underneath it.

**Theo Vermaak**

Chairman: PKF International Professional Standards Committee  
PKF International Limited

## Matters of Concern

### Scope of Requirements

There have been calls to expand the scope of the proposed **requirement** to report on key audit matters to include public interest entities (“PIEs”). We are of the opinion, due to the lack of a single definition of a PIE and the difficulties involved in determining what constitutes a PIE within different jurisdictions, that the mandatory disclosure of key audit matters be limited to listed entities, as is currently proposed. Should PIEs or their auditors wish to disclose key audit matters, or where mandated within their jurisdictions, the proposed standard adequately allows for such voluntary or jurisdictional reporting.

### Effective date

No effective date has yet been suggested in the proposed standard. As a final standard is likely to be released in 2014 we recommend an effective date of no earlier than 31 December 2015 to allow time for training and communication between companies and their auditors.

### Key audit matters

There is a risk that the requirement to include key audit matters in the audit report will in certain circumstances deter management and TCWG from engaging in proper and open discussions and two-way communication with their auditors where they don't want matters to be included in the audit report. In isolation this may not be enough reason not to require such reporting, although the overall risk and impact on audit quality should be considered by the IAASB.

## Responses to Specific Questions

### Key Audit Matters

**Question 1. Do users of the audited financial statements believe that the introduction of a new section in the auditor's report describing the matters the auditor determined to be of most significance in the audit will enhance the usefulness of the auditor's report? If not, why?**

We are of the view that the introduction of a new section describing matters that the auditor has determined to be of most significance during the audit will provide useful additional information to users of the financial statements. We do however have some concerns regarding the use of the term “most significant”. The proposals acknowledge that there may be instances where no key audit matters are identified and reported. The term “most significant” is potentially contradicting as it implies that there will always be matters that are more significant than others, even where such matters are not considered particularly significant.

We also believe that further guidance on the application of this section in practice is required as outlined in Question 2 below.

**Question 2. Do respondents believe the proposed requirements and related application material in proposed ISA 701 provide an appropriate framework to guide the auditor's judgment in determining the key audit matters? If not, why?**

**Do respondents believe the application of proposed ISA 701 will result in reasonably consistent auditor judgments about what matters are determined to be the key audit matters? If not, why?**

## Appendix – Matters of concern and responses to specific questions

The proposed requirements and related application material contained in proposed ISA 701 provide a good basis for an applicable framework when determining the key audit matters. However, whilst there exists good application guidance explaining an appropriate framework [A1 to A24], there is a lack of guidance illustrating situations where an auditor would or would not include a matter as a key audit matter (and the reasoning behind the decision). Inclusion of example situations would enable the auditor to better assess matters when determining whether they are key audit matters.

Clarification is also required on how key audit matters relate to significant risks, matters communicated to TCWG and completion memoranda, as non-inclusion of these areas as key audit matters could lead to continual challenge of the auditor's judgment by regulators and expose the auditor to litigation.

Inclusion of further examples would lead to sufficient clarity within the standard to result in reasonably consistent auditor judgements. A lack of further examples would result in individual interpretations of when to include a matter that may be considered to be a key audit matter.

**Question 3. Do respondents believe the proposed requirements and related application material in proposed ISA 701 provide sufficient direction to enable the auditor to appropriately consider what should be included in the descriptions of individual key audit matters to be communicated in the auditor's report? If not, why?**

The requirements and related application material in proposed ISA 701 in conjunction with the illustrative examples given in proposed ISA 700 (Revised) provide sufficient direction to enable the auditor to appropriately consider and conclude on what should be included in the description of individual key audit matters that are being communicated within the auditor's report.

**Question 4. Which of the illustrative examples of key audit matters, or features of them, did respondents find most useful or informative, and why? Which examples, or features of them, were seen as less useful or lacking in informational value, and why? Respondents are invited to provide any additional feedback on the usefulness of the individual examples of key audit matters, including areas for improvement.**

We are of the view that all six examples of key audit matters included in Illustrations 1 and 2 of the appendix to proposed ISA 700 (Revised) contain useful information on the way in which key audit matters should be communicated within the audit report.

However, as noted in our response to Question 2 above, the usefulness of the illustrations would be enhanced by providing background information on each key audit matter illustrated, giving further details of the matter along with discussion of the judgements made by the auditor in determining that these were key audit matters. This will help illustrate the process around the decision on whether or not to include a particular matter, and how the auditor decided which details to communicate, rather than just showing the actual communications.

**Question 5. Do respondents agree with the approach the IAASB has taken in relation to key audit matters for entities for which the auditor is not required to provide such communication – that is, key audit matters may be communicated on a voluntary basis but, if so, proposed ISA 701 must be followed and the auditor must signal this intent in the audit engagement letter? If not, why? Are there other practical considerations that may affect the auditor's ability to decide to communicate key audit matters when not otherwise required to do so that should be acknowledged by the IAASB in the proposed standards?**

We are in agreement with the approach taken by the IAASB in proposed ISA 701 in relation to key audit matters. We note however that proposed amended wording in ISA 201 p10 (e) could be read as requiring the auditor to communicate key audit matters rather than giving the auditor the option to report. This interpretation could imply the auditor knows before the start of the audit of the key audit matters to be

## **Appendix – Matters of concern and responses to specific questions**

reported and would be contrary to proposed ISA 701 p13. We suggest a slight rewording of the sentence to clarify this matter.

Clarity is required for non-listed entities when the auditor needs to signal intent to report “key audit matters” in the engagement letter, as this suggests that the auditor will know of the existence of key audit matters before the audit has been started. While reporting of such matters may be agreed by engagement, audit results could prompt the auditor to include such matters even when not agreed in advance.

**Question 6. Do respondents believe it is appropriate for proposed ISA 701 to allow for the possibility that the auditor may determine that there are no key audit matters to communicate? (a) If so, do respondents agree with the proposed requirements addressing such circumstances? (b) If not, do respondents believe that auditors would be required to always communicate at least one key audit matter, or are there other actions that could be taken to ensure users of the financial statements are aware of the auditor’s responsibilities under proposed ISA 701 and the determination, in the auditor’s professional judgment, that there are no key audit matters to communicate?**

We agree that there is a possibility of the auditor determining that there are no key audit matters to communicate and further agree with the proposed requirements addressing such circumstances. There is however potentially contradictory language in the exposure draft, as key audit matters are described as the matters the auditor determined to be of “most significance” in the audit. This implies that there will always be matters that are more significant than others, even where such matters are not considered particularly significant.

**Question 7. Do respondents agree that, when comparative financial information is presented, the auditor’s communication of key audit matters should be limited to the audit of the most recent financial period in light of the practical challenges explained in paragraph 65? If not, how do respondents suggest these issues could be effectively addressed?**

We are in agreement with the limitation on communication of key audit matters to the most recent financial period in light of the practical challenges outlined in paragraph 65.

**Question 8. Do respondents agree with the IAASB’s decision to retain the concepts of Emphasis of Matter paragraphs and Other Matter paragraphs, even when the auditor is required to communicate key audit matters, and how such concepts have been differentiated in the Proposed ISAs? If not, why?**

We agree with the IAASB’s decision to retain the concepts of Emphasis of Matter paragraphs and Other Matter paragraphs, even when the auditor is required to communicate key audit matters and are of the view that the application guidance contained within the proposed ISAs provide sufficient clarity to adequately differentiate these concepts from the concept of key audit matters.

### **Going Concern**

**9. Do respondents agree with the statements included in the illustrative auditor’s reports relating to:**

**(a) The appropriateness of management’s use of the going concern basis of accounting in the preparation of the entity’s financial statements?**

**(b) Whether the auditor has identified a material uncertainty that may cast significant doubt on the entity’s ability to continue as a concern, including when such an uncertainty has been identified (see the Appendix of proposed ISA 570 (Revised))?**

## Appendix – Matters of concern and responses to specific questions

**In this regard, the IAASB is particularly interested in views as to whether such reporting, and the potential implications thereof, will be misunderstood or misinterpreted by users of the financial statements.**

We do not agree with the inclusions of such statements. Including explicit statements about both the appropriateness of management's use of the going concern basis of accounting and whether the auditor has identified a material uncertainty is likely to be misinterpreted by users of the financial statements.

Our concern relates to the situation where a material uncertainty has been identified but the going concern basis of accounting is appropriate. Users are likely to place more emphasis on the auditor's judgement of the going concern basis than is appropriate, seeing the positive statement about appropriateness of the going concern basis of accounting as diminishing any material uncertainty that may be reported. If the IAASB decides to retain the requirement to include an explicit statement about the appropriateness of the use of the going concern basis of accounting, wording should be added to the illustrative examples so as to clarify that the going concern basis is considered appropriate assuming that the material uncertainty does not arise (a reference to the note on material uncertainties or an explanation of the effect of the material uncertainty arising may be given).

More importantly, the ISAs already require very specific additions to the auditor's report in the event that material uncertainties around going concern are identified. If going concern uncertainties are identified, but the auditor concludes that they do not require an emphasis of matter paragraph to be added to the auditor's report, it is likely that this would meet the definition of a key audit matter, and should therefore be included as a "regular" key audit matter under the other proposals contained in the exposure draft. We refer to the PCAOB exposure draft on auditor reporting, under which going concern would only be included if identified as a critical audit matter.

We are in summary supportive of including mention of material uncertainties where a possible material uncertainty arose which was dismissed, along with how this conclusion was reached. This approach is consistent with the treatment of other matters that are only included where they are a key audit matter.

Where going concern uncertainty does arise as a key audit matter, we are supportive of separating it out under its own heading as currently proposed. This will further focus users' attention to the matter in situations where that information is important to their understanding of the financial statements.

**10. What are respondents' views as to whether an explicit statement that neither management nor the auditor can guarantee the entity's ability to continue as a going concern should be required in the auditor's report whether or not a material uncertainty has been identified?**

As stated above, we do not agree with the proposal to include a statement on the appropriateness of the use of going concern in all cases. As a result, we believe that this proposed statement about guarantee is not appropriate in all cases either. Such an explicit statement as illustrated in ISA 570 - A22 when no material uncertainty has been identified will cause confusion amongst users who may attach higher emphasis to the statement that no material uncertainty has been identified than the disclaimer of guarantee, seeing the disclaimer as applying solely to other unpredictable future events (e.g. an industrial accident causing the company's failure) rather than applying to the inherent limitations of a financial audit, such.

Where a going concern uncertainty has been reported as a key audit matter in line with our proposed changes, then a statement about guarantee would be appropriate.

## Compliance with Independence and Other Relevant Ethical Requirements

**11. What are respondents' views as to the benefits and practical implications of the proposed requirement to disclose the source(s) of independence and other relevant ethical requirements in the auditor's report?**

## **Appendix – Matters of concern and responses to specific questions**

While we are supportive of considering further work in this area, we do question the practical value of such information. We are further of the opinion that the IAASB needs to conduct further research on the practical implications of this requirement when applied to group situations, and consider the practical need to limit these declarations to jurisdictions that apply to the group auditor only, and to significant components of the group.

### **Disclosure of the Name of the Engagement Partner**

**12. What are respondents' views as to the proposal to require disclosure of the name of the engagement partner for audits of financial statements of listed entities and include a "harm's way exemption"? What difficulties, if any, may arise at the national level as a result of this requirement?**

We are in agreement with the proposal to require disclosure of the name of the engagement partner for audits of financial statements of listed entities and believe that the inclusion of the "harm's way exemption" will adequately respond to matters that would otherwise arise as a consequence of this requirement.

We do not perceive any difficulties arising at national level after the application of the harm's way exemption.

### **Other Improvements to Proposed ISA 700 (Revised)**

**13. What are respondents' views as to the appropriateness of the changes to ISA 700 described in paragraph 102 and how the proposed requirements have been articulated?**

We are in agreement with the changes to ISA 700 as described in paragraph 102 of the exposure draft.

**14. What are respondents' views on the proposal not to mandate the ordering of sections of the auditor's report in any way, even when law, regulation or national auditing standards do not require a specific order? Do respondents believe the level of prescription within proposed ISA 700 (Revised) (both within the requirements in paragraphs 20–45 and the circumstances addressed in paragraphs 46–48 of the proposed ISA) reflects an appropriate balance between consistency in auditor reporting globally when reference is made to the ISAs in the auditor's report, and the need for flexibility to accommodate national reporting circumstances?**

We agree with the proposal not to mandate the ordering of sections within the auditor's report in order to allow compliance with the requirements of national laws and regulations, and believe that the requirements and circumstances outlined in the ISA in conjunction with the illustrative examples will lead to sufficient global consistency in auditor reporting.