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Professor Arnold Schilder
Chairman
International Auditing & Assurance Standards Board
529 Fifth Avenue 6th Floor
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Dear Professor Schilder

Comment Letter Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing

Crowe Horwath International is delighted to present a comment letter on *Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing*. Crowe Horwath International is a leading global network of audit and accounting firms, with members in some 115 countries.

We welcome the approach taken by the IAASB to develop a new model for audit reporting. The IAASB have proposed a solution that seeks to improve communication and transparency about the audit process. The audit report is presented to users of financial information as part of a larger package prepared by management and Those Charged With Governance. Therefore, it is important in completing the development of a new approach to audit reporting that it is recognised that audit report has to be read in the context of the full package of information, with clear cross-references from the audit report to assist understanding.

Key Audit Matters

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?

As an international network of independent audit firms, we believe that the introduction of the

new section in the auditor's report will enhance the usefulness of the report.

The explicit statement by the IAASB that "Key audit matters are selected from matters communicated with those charged with governance" is of critical importance in identifying the matters that are important to the user of the auditor's report.

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?

The proposed requirements and related guidance material are a good start in developing an appropriate framework to guide the auditor's judgment in determining key audit matters.

In completing the guidance the IAASB should be alert to a concern that some auditors might, through caution or lack of understanding, seek to include all matters communicated to TCWG as key audit matters. Some auditors may find it challenging to document why certain matters were communicated to TCWG but then were not included in the auditor's report. At some of the roundtable discussions, there were requests for a decision to be included in the application guidance. A decision tree could assist auditors in determining whether a matter communicated to TCWG should be included as a key audit matter.

Paragraph A2 makes a number of references to assessing key audit matters "in the context". It would be helpful if the Application Guidance contained more references to assist with the interpretation of "in the context". We understand that this point has been raised at the roundtables.

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?

As noted above, there is an initial concern that some auditors may seek to include all matters communicated to TCWG as key audit matters. Over time, the tendency to present standardised key audit matters on subjects such as impairment has to be avoided. This will result in over consistency and defeat the object of the proposals.

Consistency will be influenced by the extent and investment by auditors in developing techniques to apply their judgment and present key audit matters. We see this as a behavioural change management issue. Those auditors that make this investment will be able to use their skills as a differentiation tool.

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?

In general yes. However, we feel that the IAASB could make it clearer as to how much information should be given about the effect on the audit and the audit procedures undertaken. In complex areas, the audit approach cannot be described briefly. What constitutes "at a high level" (A39) will vary.

The IAASB should keep the application of this requirement under review, and be open to

preparing staff comments that provide supplementary guidance to auditors.

4. Which of the illustrative examples of key audit matters, or features of them, did respondents find most useful or informative, and why?

In all the examples, it is clear why the issue was selected as a key audit matter. The use of words such as “as a result”, “we focused on this transaction because” and “this is because” are effective pointers to the issue.

The goodwill and acquisition examples are generally well presented.

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.

The paragraphs should focus on the audit judgment, audit response and conclusion. There should be less comment on the details of policies, and the risks and uncertainties of the matter. These are addressed elsewhere in the Annual Report, and the use of note references and other cross-references will direct the reader to these.

We consider that the Valuation of Financial Instruments and Revenue Recognition examples are less effective. Both include piecemeal opinions on specific matters. The use of language such as “our audit procedures also included” or “based on the audit procedures performed, we did not find” does not assist with addressing the overall issue. In both cases, rewording could deliver a more effective example that is in line with the objectives of reporting a key audit matter.

The valuation of financial instruments example includes the words “we challenged management’s rationale”. There are more subtle ways to present a statement such as this.

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 agree with the approach taken by the IAASB.

Where national regulators and standard setters extend the requirement to present key audit matters to other entities, or where a voluntary decision is made to present key audit matters, proposed ISA 701 needs to be applied and the intent has to be addressed in the audit engagement letter.

We agree with the IAASB’s intention to address, at the post implementation review stage, to consider the potential for the broader application of ISA 701. In particular, there is a strong case for developing a definition of PIEs for audit reporting purposes, so that the scope of the standard can be extended beyond listed entities.

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 with the proposed requirements. As the mandatory scope of proposed ISA 701 extends to listed entities, we agree that the likelihood of there being no key audit matters is remote. The IAASB has given relevant illustrations of the remote cases where no key audit matters might arise.

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?

Yes.

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 this decision and we understand the argument presented by the IAASB for retaining emphasis of matter and other matters paragraphs. In practice, there may be some confusion, meaning that the IAASB needs to adequately differentiate between emphasis of matter and key audit matter. Making clear the reasons for the retention of emphasis of matter, particularly where the scope of key audit matter does not apply is important.

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 concern, including when such an uncertainty has been identified (see the Appendix of proposed ISA 570 (Revised))?

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 agreed with the approach proposed by the IAASB.

Stakeholders have been seeking additional comment from auditors about going concern. The proposed wording enables auditors to present a comment regarding the application of the going concern concept, and the procedures that auditors are required to perform by ISA 570. Clearly there is the potential for the wording presented to become “boilerplate”, but the IAASB have achieved a balance, with additional comment by auditors, but no change in the nature of the auditor’s opinion.

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?

There are potential concerns about including a statement such as this, which refers to both “management” and “auditor”. Management presents their statements about the going concept within the Annual Report package. However, given the degree of discussion in recent years about responsibilities and reporting of going concern, we see the need for this statement. The statement communicates to users that “there is no guarantee”, which is 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?

We consider this a reasonable suggestion. This is already a requirement in some jurisdictions.

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 acknowledge that the naming the engagement partner is already established practice in many countries. Issues can arise from national legislation and legal practice, and therefore, whilst we encourage the name of the partner to be given, it is best left to individual jurisdictions to determine policy on this.

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?

These are reasonable proposals. Relocating “descriptions of the responsibilities of the auditor and key features of the audit” to an appendix or appropriate website has proved successful in the United Kingdom.

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?

It is appropriate not to mandate the ordering of sections. National regulators and standards may see the merits of adopting an order at the national level, so that additional national reporting requirements are accommodated, and national consistency in reporting is achieved.

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?

The approach taken is reasonable.

We trust that our comments assist the IAASB in their project to develop a new standard on audit report. We shall be pleased to discuss our comments further with you.

Kind regards

Yours sincerely

A handwritten signature in black ink, appearing to read "David Chitty". The signature is written in a cursive, slightly stylized font.

David Chitty
International Accounting and Audit Director