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Technical Director
International Auditing and Assurance Standards Board
545 Fifth Avenue, 14th Floor
New York, New York 10017

Subject: *International Auditing and Assurance Standards Board July 2013 Exposure Draft "Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing (ISAs)"*

This letter provides the U.S. Government Accountability Office's (GAO) comments on the International Auditing and Assurance Standards Board's (IAASB) exposure draft.

We support efforts to improve the quality of financial reporting and increase the confidence users have in the audit of financial statements. However, we do not believe that certain of the proposed enhancements to the auditor's report, such as key audit matters and the disclosure of the name of the engagement partner are critical to the perceived value of the financial statement audit or add value to the user of the financial statements. We also do not believe that it is appropriate to include statements in the auditor's report for all audits related to the determination of going concern. Further, we encourage the IAASB to work closely with other standard setters, such as the Public Company Accounting Oversight Board and the Auditing Standards Board, to ensure a consistency of practice by harmonizing their standards on reporting key audit matters, absent any compelling reasons that would require different practice. For example, the standard setters should determine thresholds or other guidance that facilitates the consistent reporting of key audit matters.

Requests for Specific Comments

The IAASB is seeking comments on a number of areas in the proposed standards. We have provided discussion on the areas listed in the exposure draft below. Our responses to the specific questions included in the exposure draft are included in the enclosure to this letter.

Key Audit Matters

We do not support the requirement for a new section in the auditor's report describing matters the auditor determines to be of most significance in the audit (key audit matters), and believe that this requirement will not enhance the usefulness of the auditor's report or add value to the user. We believe that such requirements will result in auditors reporting key audit matters that are already included in the notes to the financial statements, and the audit reports would add little value to the user. We are also concerned that the incentives for consistent reporting of key audit matters across entities would likely lead to "boilerplate" reporting language for each type of key audit matter. Further, we believe that such a requirement may increase the risk of blurring the roles of entity management and auditor, as it requires the auditors to comment on elements that are management's responsibility to discuss or disclose.

We are also concerned about the application of the requirement for reporting the "most" significant matters to be reported as key audit matters. Certain matters, while being the most significant to the auditor, may be unimportant to financial statement users and the requirement may lead to the reporting of an extensive discussion of matters unimportant to financial statement users.

An additional concern is the potential inconsistency about when to inform management of a non-listed entity that the auditors will be reporting an issue as a key audit matter. As it is currently written in the exposure draft of International Standards on Auditing (ISA) 210, a statement must be included in the engagement letter if the auditor intends to communicate key audit matters. However, the auditors may identify certain key audit matters in the course of performing their audit that were previously unknown to management, or undisclosed to the auditors, and the intent to identify them was not previously included in the audit engagement letter. We suggest that Emphasis of Matter paragraphs would be a more useful approach to reporting these issues for non-listed entities.

Although the illustrative examples of key audit matters included in the exposure draft, particularly the goodwill example, are generally useful and informative, we generally find that the requirements and application material related to these matters is unclear and we believe that this could lead to inconsistent key audit matter reporting. In particular, we believe that the exposed ISA 701 should be further developed to help auditors in their determination of the significance of audit matters. Tools such as threshold determinations and a description of qualitative and quantitative factors would be useful, and we encourage further development and expansion of examples to assist auditors in their identification of key audit matters and the consistent reporting of these matters.

We believe that, if a requirement is kept for statements from the auditor regarding key audit matters, the auditor's communication of such matters should be limited to the audit of the most recent financial period when comparative financial information is presented. However, we would be concerned about the presentation in instances when a key audit matter is no longer being reported in the comparative financial statements, as this may cause the user of the auditor's report to believe that the key audit matters previously described are no longer significant.

We support the IAASB's decision to retain the concepts of Emphasis of Matter paragraphs and Other Matters paragraphs, as we see these paragraphs as adding value to the user of financial statements by providing additional information not included elsewhere in the report.

Going Concern

We do not support a requirement that the audit reports include statements relating to the appropriateness of management's use of the going concern statement. We question whether users of financial statement information will understand the going concern statement, and are concerned that users may make decisions based on an incorrect interpretation of that statement. Further, we are concerned that users may become desensitized to going concern statements if they are included in every report, and may fail to identify going concern issues when they are reported. Accordingly, we do not support a requirement for an explicit statement in the auditor's report that neither management nor the auditor can guarantee the entity's ability to continue as a going concern, regardless of whether a material uncertainty has been identified. In addition, we believe that the going concern statement is problematic for those in the government sector, as we are not convinced that this concept is relevant to national and many sub-national public sector entities. For example, the US government will not have a continued existence issue, but may have questions on long-term financial sustainability. However, we recognize that going concern may be an issue at the municipality level.

We encourage the accounting standard setters to continue their consideration of whether the accounting standards related to the going concern statement should require disclosures concerning management's assessment, and if necessary, should provide management with enhanced guidance on preparing these disclosures. Such disclosures could be combined with other risks and uncertainties that could affect the going concern assumption. Consistent with current auditing standards, auditors would then evaluate management's assessment of the entity's ability to continue as a going concern, and would then evaluate the fair presentation and sufficiency of management's enhanced disclosures.

Compliance with Independence and Other Relevant Ethical Requirements

We do not support the proposed requirement to disclose the source(s) of independence and other relevant ethical requirements in the auditor's report, and we question whether such additional disclosures would benefit the user. Auditors are required to comply with the independence and other ethical requirements in order to issue an opinion, and the auditor's independence is already noted in the title "Independent Auditor's Report". We also question whether the user of the financial statements would understand the implications of the ethical requirements described in the auditor's report, and believe that the user may be misled by such disclosures. As an alternative, we would support the inclusion of a statement in the auditor's responsibility section that describes the methods by which the auditor maintains independence and meets other ethical requirements, and we believe that statement may help the users better understand the auditor's ethical responsibilities.

Disclosure of the Name of the Engagement Partner

GAO typically identifies the engagement partner and provides contact information for that engagement partner in our published financial statement and other audit reports. As such, we do not object, in principle, to the practice of disclosing the name of the engagement partner. However, we have concerns that such a disclosure may lead to financial statement users misunderstanding the diversified responsibility of an audit engagement in the private sector. The user of the audit report may not understand that the firm performing the audit is responsible for the audit work, rather than solely the engagement partner.

We strongly encourage the IAASB, if requiring the disclosure of the name of the audit partner, to preface the disclosure of the name of the engagement partner with a statement to inform the user that an audit is not conducted by one individual (the engagement partner), but a group of auditors, and possibly specialists, represented by the engagement partner.

Other Improvements to Proposed ISA 700 (Revised)

We believe that the improved description of the responsibilities of the auditor and the key features of the audit will enhance the usefulness of the auditor's report for the user of the financial statements. In regard to the other improvements mentioned in the exposed ISA, we believe that this information is already included in other sections of the report or could be misleading to the user of the financial statements who may be confused by the inclusion of a description of the auditor's other reporting responsibilities.

Regarding the ordering and presentation of the audit report, we appreciate the flexibility given to the ordering and presentation, particularly because of the regulations and mandates with which government audit reports must often comply. However, we have concerns that financial statement users may have difficulty understanding the elements included in an auditor's report when the order of the information is presented inconsistently. Accordingly, we support the use of descriptive headers identifying the different elements in the audit report to facilitate the user's identification of the different report elements when the ordering of sections in an audit report diverges from the ordering in other published reports.

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We thank you for considering our comments on these important issues as the board continues its effort to enhance the value of auditor reporting.

James R. Dalkin
Director
Financial Management and Assurance

Enclosure

Enclosure

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?

We do not believe the introduction of a key audit matters section will enhance the usefulness of the auditor's report. We believe that, in practice, such requirements will result in entities reporting the substance of key audit matters in the footnotes, to the extent they are not already included, and the audit reports would add little value to the user. Also, we are concerned that incentives for consistent reporting of like matters across entities would likely lead to "boilerplate" report language for each potential type of key audit matter.

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?

We are also concerned about the application of the requirement for reporting the "most" significant matters to be reported as key audit matters. Certain matters, while being the most significant to the auditor, may be unimportant to financial statement users and the requirement may lead to the reporting of an extensive discussion of matters unimportant to financial statement users.

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?

We find the requirements and application material related to the description of the matters the auditor determined to be of most significance to the audit unclear, and we believe this could lead to an inconsistency in the practice of key audit matter reporting. In particular, in ISA 701, paragraph A2, p.88 of the exposure draft we believe that the discussion of significance needs to be further developed to help auditors in their determination of the significance of audit matters. Tools such as threshold determination, in addition to qualitative and quantitative factors, may be useful as application material.

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 believe that the illustrative examples of key audit matters included in the exposure draft, particularly the goodwill example, are generally useful and informative.

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 have a concern over a potential inconsistency about when to inform management of a non-listed company that the auditors will be reporting an issue as a key audit matter or in an Emphasis of Matter paragraph. For example, the auditor may identify certain key audit matters in the course of performing their audit that were previously unknown to management, or undisclosed to the auditors, and the intent to identify them was not signaled in the audit engagement letter. As it is currently written in ISA 210 paragraph 10 (e), p. 190 of the exposure draft, if the auditor intends to communicate key audit matters a statement must be included in the engagement letter. We suggest that Emphasis of Matter paragraphs would be a more useful approach to reporting for non-listed companies.

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 may be circumstances in which no matters may rise to the level of significance that would warrant reporting as key audit matter in the auditor's report. We agree with the requirements listed in paragraph 13 of ISA 701 with the exception of 13 (c). We find a requirement for a disclosure that no key audit matters were identified to be unnecessary, and possibly could lead the user of the financial statement to draw incorrect conclusions from the disclosure.

7. Do respondents agree that, when comparative financial information is presented, the auditors' 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 no, how do respondents suggest these issues could be effectively addressed?

We agree that the auditor's communication of key audit matters should be limited to the audit of the most recent financial period when comparative financial information is presented.

8. Do respondents agree with 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 support the IAASB's decision to retain the concepts of Emphasis of Matter paragraphs and Other Matter paragraphs.

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 the proposed ISA 570 (Revised)?

We do not support a requirement that the audit reports of certain companies include statements relating to the appropriateness of management's use of going concern. We are concerned that some users of financial statement information may not understand the going concern statement, and are concerned that users may make decisions based on an incorrect interpretation of the going concern statement. Further, we are concerned that users may become desensitized to going concern statements if they are included in every report and fail to identify going concern issues when they are reported.

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?

We do not support a requirement for an explicit statement in the auditor's report of listed companies that neither management nor the auditor can guarantee the entity's ability to continue as a going concern, regardless of whether a material uncertainty has been identified.

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 do not support the proposed requirement to disclose the source(s) of independence and other relevant ethical requirements in the auditor's report, and we question whether such disclosure will benefit the user. Auditor independence is noted in the title "Independent Auditor's Report", and we believe that to also include independence requirements are redundant. Further, the auditor should be in compliance with the independence and other ethical requirements in order to issue an opinion on the financial statements as an independent auditor. We question the value to users of making a public assertion/statement of such information. We also question whether the user of the financial statements would understand the implications of the ethical requirements described in the auditor's report, and believe that the user may be misled as to the auditor's role by such disclosures.

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?

GAO typically identifies the engagement partner, and provides contact information for that engagement partner in our published financial statement and other audit reports. As such, we do not object, in principle, to the practice of disclosing the name of the engagement partner. However, we have concerns that it may lead to users misunderstanding the diversified responsibility of an audit engagement in the private sector for some audits. The user of the audit report may not understand that the firm that performed the audit is responsible for the audit work, rather than solely the engagement partner. We strongly encourage the IAASB, if requiring the disclosure of the name of the audit partner, to preface the disclosure of the name of the engagement partner with a statement to inform the user that an audit is not conducted by one individual (the engagement partner), but a group of auditors, and possibly specialists, represented by the engagement partner.

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 believe the improved description of the responsibilities of the auditor and the key features of the audit will enhance the usefulness of the auditor's report for the user of the financial statements. In regard to the other improvements mentioned in paragraph 102, we believe that this information is already included in other sections of the report or could be misleading to the user of the financial statements who may be confused by the inclusion of a description of other reporting responsibilities.

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 appreciate the flexibility given to the ordering and presentation of the audit report, particularly because of the regulations and mandates with which government audit reports must comply. However, we have concerns that financial statement users may have difficulty understanding the elements included in an audit report if the ordering is inconsistent. Accordingly, we support the IAASB in requiring the use of descriptive headers that identify the different elements in the audit report to facilitate the user's identification of the different report elements when the ordering of sections in an audit report diverges from the ordering in other published reports.