

November 19, 2013

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

Submitted electronically at: <https://www.ifac.org/publications-resources/submit-comment?exposure-draft=21415>

Re: Exposure Draft, *Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing (ISAs)*

The New York State Society of Certified Public Accountants (NYSSCPA), representing more than 29,000 CPAs in public practice, industry, government and education, welcomes the opportunity to comment on the above captioned exposure draft.

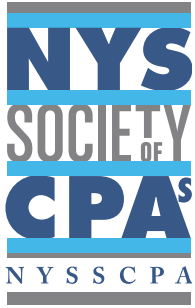
The NYSSCPA's Auditing Standards Committee deliberated the exposure draft and prepared the attached comments. If you would like additional discussion with us, please contact Julian Jacoby, Chair of the Auditing Standards Committee at (646) 644-4482, or Ernest J. Markezin, NYSSCPA staff, at (212) 719-8303.

Sincerely,

A handwritten signature in blue ink that reads "J. Michael Kirkland". The signature is written over a faint, semi-transparent version of the NYSSCPA logo.

J. Michael Kirkland
President

Attachment



**NEW YORK STATE SOCIETY OF
CERTIFIED PUBLIC ACCOUNTANTS**

COMMENTS ON

**EXPOSURE DRAFT, *REPORTING ON AUDITED FINANCIAL STATEMENTS:
PROPOSED NEW AND REVISED INTERNATIONAL STANDARDS
ON AUDITING (ISAs)***

November 19, 2013

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New York State Society of Certified Public Accountants

Comments on

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

General Comments

We commend the International Auditing and Assurance Standards Board (IAASB) for responding in its current proposal, *Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing (ISAs)* (the Exposure Draft), to the concerns expressed by many respondents to its June 2012 invitation to comment, *Improving the Auditor's Report* (the ITC), by proposing a discussion of "key audit matters" in audit reports in lieu of the "Auditor Commentary" suggested in the Consultation Paper. We responded to the ITC in a letter dated October 2, 2012, and understand those concerns to be rooted in the desire to preserve the purity of the attest function by not requiring auditors to speak about financial statement matters in a way that should be reserved for management. The key audit matters discussion currently proposed apparently is intended to be limited to matters of auditor judgment which we believe (despite our reservations set forth in our responses to Questions 1-8 of the Exposure Draft) would be far more appropriate than the broader Auditor Commentary described in the ITC.

Questions on 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?

Response: No, 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 not enhance the usefulness of the auditor's report. We believe that the expressions of demand for this kind of information by analysts and investor groups are largely exaggerated, lack credibility and are likely attributable to the "if you build it, they will come syndrome." We think that despite the perceived demand, there is little persuasive evidence that securities analysts and other investor groups will actually find such disclosures in audit reports useful or will rely on them for making or recommending investment decisions, or that such a section will result in more informed and better investment decisions.

We do not believe it would be productive, informative or appropriate for auditors to provide information in audit reports that is intended to help investors or other users to assess audit quality. Auditing is a highly complex, professional discipline that requires years of ongoing education and training, experience, intimate knowledge of the issuer's business and seasoned professional judgment to enable appropriate audit scope (*i.e.*, the nature, timing and extent of auditing procedures) and related judgments (*e.g.*, those regarding risk assessment) as necessary

to support an auditor's opinion. Moreover, as we have seen historically, there are numerous opportunities for legitimate disagreements on such judgmental matters between or among experienced and knowledgeable professionals (including, for example, regulators, expert witnesses and authors of nonauthoritative professional guidance). Accordingly, we believe that public disclosure of details of key auditor judgments would not help users make investment or credit decisions or enhance transparency in any meaningful way or serve any other useful purpose; rather it would negate or dilute the pass/fail message and, thereby diminish the value of an audit report. Without the opportunity for two-way dialog with auditors about such matters, these details are unlikely to contain enough information to help users to make meaningful assessments and useful judgments and quite probably would be misunderstood by many. We believe that financial statement users could never reasonably and meaningfully assess the effectiveness of such professional judgments in relation to possible alternatives without all the factual and technical knowledge that is available to the auditor.

Even if the potential for misunderstanding is partially mitigated for institutional financial statement users by employing trained experienced audit advisors to assist in their analyses, we believe the inherent limitations on the extent of detailed information that could be communicated effectively in writing is likely to prevent the realization of any meaningful potential benefit, and the costs to such users would substantially exceed any resultant value.

Therefore, it is unreasonable to create expectations that any form of written report, no matter how expanded it might be from the current model, would contain communications of sufficient factual and circumstantial details to help otherwise uninformed users who do not have direct access to the auditors for two-way dialog to make meaningful judgments as to such complex matters as risk assessments, audit scope and other auditor judgments.

Assessing audit quality is not the job of investors and other financial statement users; it is the job of the engagement quality reviewer, standard setters and regulators--including licensing authorities (to a lesser extent) and, perhaps most significantly, those charged with governance upon whom investors should be able to place their reliance as to such matters. Although not the responsibility of the IAASB, we see regulation of those charged with governance as the most relevant and the best alternative way to assure that investors' needs are served effectively.

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?

Response: No, we do not 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. As noted in our response to Question 1, we do not believe reporting key audit matters is likely to contribute in any meaningful way to achieving the objectives of providing relevant and useful information to investors and other financial statement users. However, in the event that the proposal for auditors to report key audit matters is retained in a final standard (which we oppose), we believe the factors described in paragraph 8 and the

related guidance in paragraphs A12–A24 of proposed ISA 701 for determining key audit matters are sufficiently clear to determine what would be reportable as a key audit matter consistent with the definition in paragraph 7 of proposed ISA 701. Should the IAASB require the discussion of key audit matters and the U.S. Public Company Accounting Oversight Board (PCAOB) require discussion in audit reports of what it terms *critical audit matters* (both proposals pending)? We do not believe so. In addition we believe the proposed IAASB definition in paragraph 7 is too narrow and should be broadened, along with conforming changes to the guidance in paragraphs 8, 9 and 13, to be more consistent with that contained in Appendix 1 of paragraph 8 of the PCAOB’s proposal.¹

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?

Response: Subject to our responses to Questions 1 and 2, we believe the guidance provided in paragraphs 9 through 11 would enable auditors to determine appropriately how to report key audit matters in accordance with proposed ISA 701, as it is now drafted.

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.

Response: The first two of four illustrative reports presented in the Appendix to proposed ISA 700 (Revised) appear adequately responsive with regard to key audit matters to the proposed requirements of ISA 701. Nevertheless, we believe these brief examples serve to illustrate the inherent lack of utility of such limited discussions that reinforces our views set forth in response to Question 10.

We noted that many of the discussions of key audit matters illustrated inappropriately contain conclusions none of which would be prescribed by the proposed standard (paragraph 10). Examples of these conclusions include the appropriateness of accounting or estimation methods or assumptions employed or the absence of adjustments or side agreements (each of which appears inappropriately to constitute positive assurance or piecemeal opinions in direct contradiction to the disclaimer expressed therein the illustrative introductory paragraph). In addition, the second sentence of the illustrative introductory paragraph that would be mandated by paragraph 9 of proposed ISA 701 (which we have suggested in our response to Question 2 is inappropriately limited) seems unnecessary “boilerplate” and would only serve to overburden the proposed standard report with excessive verbiage. Consequently, we believe this sentence should be removed from all examples presented in a final standard along with all conclusions.

¹ PCAOB Release No. 2013-005, dated August 1, 2013.

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?

Response: No, we do not 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 because we do not believe communication of key audit matters, as defined (or as would be defined if our recommendation in our response to Question 2 is accepted), is likely to provide information of value to any financial statement users. We do not support the suggestion implied by paragraph 4 of proposed ISA 701 that voluntary discussions of such matters should be permitted in reports on audited financial statements of unlisted entities. Alternatively, the IAASB might consider suggesting that such information may be provided only in private communications to selected users as may be authorized in writing (for confidentiality reasons) by management of the client entity along with permission to engage in oral dialog with the auditor.

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?**

Response: Yes, we 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. We are firmly of the view that any requirement for discussion of key audit matters should provide for the possibility that there are no matters that rise to a level of significance such as to become subject to this requirement (see our response to part (b), below). Accordingly, we concur with the guidance afforded by paragraph 13 of proposed ISA 701 except for that set forth in paragraph 13(c). Our objection is primarily because we are inherently opposed to the notion of burdening audit reports with defensive language about matters that are, in fact, inapplicable or insignificant in the circumstances. We see no potential benefit to financial statement users of such language. Moreover, we see reporting language that, in substance states that there are no matters “of most significance” to be more readily likely to be interpreted to mean that all matters were of equal significance and, therefore, inconsistent with discussing none, rather than there were no matters of sufficient significance to be reported.

If the proposed requirement to report key audit matters in circumstances that warrant it were to be adopted, we would be in favor of providing more extensive, nonprescriptive guidance than that presently contained in paragraphs A2 and A47 to facilitate reasonably consistent auditor's judgments, perhaps primarily by examples, regarding the level of significance of matters to be reported.

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?

Response: No, we do not 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. As indicated in our response to Question 1 and elsewhere, we are opposed to communicating key audit matters in audit reports. However, should the proposal for auditors to report key audit matters be retained in a final standard, we believe audit reports on comparative financial statements should be complete and should stand alone for all periods presented in all circumstances and that paragraph 9(a) of proposed ISA 701 should be revised accordingly. Therefore, all key audit matters included in the original audit report issued on prior period financial statements should be included when the statement presented subsequently in comparative form., In the event prior period financial statements have been restated, we believe the subject matter of the restatement should also be included in the discussion of key audit matters for that period and, would need not be included in an emphasis of matter paragraph as is the current practice (see also our response to Question 8).

We do not see the so-called "practical challenges" set forth in paragraph 65 of Exposure Draft as valid reasons to limit discussion of key audit matters to those of the current audit period only. On the contrary, in the event key audit matters were included in a prior period's audit report, we would expect users to be particularly interested in the matters discussed in paragraph 65. We believe, that if the proposed requirement to report key audit matters is retained in a final standard, reporting guidance with respect to such circumstances should be included.

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?

Response: No, we do not 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. However, we agree with the IAASB's decision to retain the concepts of ISA 706, *i.e.*, primarily the inclusion of such items in audit reports should continue to be at the auditor's discretion rather than mandatory. If discussion of key audit matters becomes a requirement as proposed, we would concur with the admonition in paragraph A26 of proposed ISA 701 that any such descriptions of emphasis or other matters pursuant to ISA 706 should not be viewed as a substitute for a discussion of key audit matters in accordance with proposed ISA 701. Because

we are not in favor of redundancies in audit reports, we believe both standards (*i.e.*, ISA 701 and 706) should contain language clearly advising auditors that key audit matters deemed reportable under ISA 701 should not also be reported pursuant to ISA 706.

Questions on 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 [sic], 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.

Response: No, we do not agree with the statements included in the illustrative auditor’s reports relating to the appropriateness of management’s use of the going concern basis of accounting in the preparation of the entity’s financial statements. Paragraphs 25-26 of International Accounting Standard (IAS) 1, *Presentation of Financial Statements*, as well as similar provisions of other commonly used financial reporting frameworks, set forth, as a basic underlying convention that the going concern assumption shall apply except in circumstances when the liquidation basis applies because “management either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so.”² As we previously stated in our letter of October 2, 2012, the proposed heightened focus on the use of the going concern assumption inappropriately elevates it from a normally expected condition (*i.e.*, a “default” value) that is now discussed in audit reports only on an exception basis (*i.e.*, when there is material uncertainty or when the alternative liquidation basis is appropriate), to a level of importance that rises above all other usual accounting conventions. We believe this is largely unjustified because (a) we do not believe the standard audit report is a place to inform financial statement users of basic, underlying accounting conventions or “fundamental principles,”³ (b) it is only one of many highly significant accounting conventions that is normal, expected and need not be singled out to the exclusion of all others, and (c) such a statement would be (and should be) of virtually no value to users when continuation of operations as a going concern is not viewed as materially uncertain. Accordingly, we remain in favor of retaining the *status quo* with regard to going concern matters and continuing to report only when there are material uncertainties or when the alternative liquidation basis is deemed appropriate pursuant to current standards or when taking exception to the adequacy of management’s evaluation⁴ or its related disclosures.

² Proposed ISA 570 (Revised), *Going Concern*, paragraph 2.

³ *Ibid.*, paragraph 2.

⁴ *Ibid.*

No, we do not agree with the statements included in the illustrative auditor's reports relating to whether the auditor has identified a material uncertainty that may cast significant doubt on the entity's ability to continue as a going concern, including when such an uncertainty has been identified (see the Appendix of proposed ISA 570 (Revised)). Despite many economic weaknesses that may remain common in many parts of the world today, many financial statement issuers in many places may no longer be seriously affected, and many continuing effects of such economic weaknesses may be temporary. For those reporting entities that are not experiencing financial difficulties, we believe the disproportionate emphasis on going concern matters in paragraphs 20(a)-(d) and illustrated in paragraph A22 of proposed ISA 570 and in the four illustrative reports presented in the Appendix to proposed ISA 700 (Revised) is unwarranted.

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?

Response: As we stated in our letter of October 2, 2012, we are opposed to including an absolute disclaimer of a guarantee of an entity's ability to continue as a going concern (its survival or its future performance) in an audit report as would be required by paragraph 20(f) of proposed ISA 570. We believe that such a disclaimer would be overly defensive and unnecessary because it is unlikely that any reasonable user would interpret an audit report as containing such an unstated guarantee (especially in the presence of a broader disclaimer of assurance as to future economic or financial performance in the absence of any positive statement on the propriety of the going concern basis which we would oppose). Further, we believe it is likely that such an overt disclaimer would give users a misleading impression that it is non-standard and represents something less favorable than (or contradictory to) an unqualified opinion. We would be in favor of adding a statement to the standard audit report stating that the financial statements are inherently historical in nature and are not necessarily predictive of any future performance.

Question on 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?

Response: We view the requirement of paragraph 28(c) of proposed ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, to disclose the source(s) of independence and other relevant ethical requirements in every auditor's report to be excessive and of no value to financial statement users. It is the responsibility of those charged with governance to obtain satisfaction of such matters, and users should be able to rely on that process. We believe the statement that would be required by paragraph 38(b) of proposed ISA 700 (Revised) should be adequate to address such matters.

Question on 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?

Response: For the reasons set forth in our letter of October 2, 2012, we continue to object to the requirement 42 of proposed ISA 700 (Revised) to disclose the name of the engagement partner in an audit report even though limited to those of listed entities. Those reasons include:

- We do not believe that such a requirement would provide any transparency or information that would be meaningful or of any value to users of audited financial statements.
- An audit is generally performed by a firm that takes full responsibility for determining the methods and procedures used and the quality control environment under which audits are conducted (including the "tone-at-the-top"), the actual conduct of the audit, and the resultant report that is issued.
- Although managed by the engagement partner, audits are generally conducted by an engagement team, including but not limited to engagement quality reviewers, various firm specialists, and other partners and professional staff, and firms generally have a quality control policy that effectively provides for resolution at the firm level of any significant disagreements among its professionals on engagement matters.
- Virtually all engagement team members play an integral role in the audit and in determining the conclusions reached and all of whom are individually accountable for their compliance with all professional ethics and other applicable professional standards, regulatory requirements and firm policies and procedures, and all are subject to serious consequences for failure to comply.
- Such a disclosure would likely be the creation of an unnecessarily exaggerated user impression of the extent of responsibility placed on the engagement partner in relation to the other members of the audit team and, more significantly, the entire audit firm.
- Identification of the engagement partner is not likely to contribute to any increased sense of responsibility for audit quality since possible consequences for failure to comply with professional and regulatory requirements already could include loss of licenses and livelihoods, damage to one's professional reputation, exposure to professional liability and related monetary penalties and imprisonment.

Questions on 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?

Response: We support the proposed changes to ISA 700 that are described in paragraph 102 of the Exposure Draft. However, because the term is not used in the referenced paragraphs 35-38 of proposed ISA 700 (Revised), we do not know what is intended by the reference in paragraph 102 of the Exposure Draft to “key features” of the audit.

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?

Response: We fully concur with this proposal.