

PROPOSED INTERNATIONAL STANDARD ON AUDITING (ISA) 701

COMMUNICATING KEY AUDIT MATTERS IN THE INDEPENDENT AUDITOR'S REPORT

(Effective for audits of financial statements for periods [beginning/ending on or after date])

CONTENTS

	Paragraph
Introduction	
Scope of this ISA	1–4
Effective Date	5
Objectives	6
Definition	7
Requirements	
Determining Key Audit Matters	8
Communicating Key Audit Matters	9–12
Circumstances in which the Auditor Has Determined There Are No Key Audit Matters	13
Documentation	14
Application and Other Explanatory Material	
Determining Key Audit Matters	A1–A24
Communicating Key Audit Matters	A25–A46
Circumstances in which the Auditor Has Determined There Are No Key Audit Matters	A47–A48
Documentation	A49

Proposed International Standard on Auditing (ISA) 701, *Communicating Key Audit Matters in the Independent Auditor's Report*, should be read in conjunction with ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*.

Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the auditor's responsibility to communicate key audit matters in the auditor's report.
2. Communicating key audit matters provides additional information to users of the financial statements to assist them in understanding those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Communicating key audit matters may also assist users of the financial statements in understanding the entity and areas of significant management judgment in the audited financial statements, as such matters are areas of focus in performing the audit.
3. The communication of key audit matters in the auditor's report may also provide users of the financial statements a basis to further engage with management and those charged with governance about certain matters relating to the entity and the audited financial statements.
4. This ISA applies to audits of complete sets of general purpose financial statements of listed entities. It is intended to address both the auditor's judgment as to what to communicate in the auditor's report and the form and content of such communication. This ISA also applies when auditors of financial statements of entities other than listed entities communicate key audit matters in the auditor's report.

Effective Date

5. This ISA is effective for audits of financial statements for periods [beginning/ending on or after date].

Objectives

6. The objectives of the auditor are to determine key audit matters and, having formed an opinion on the financial statements, communicate those matters by describing them in the auditor's report.

Definition

7. For purposes of the ISAs, the following term has the meaning attributed below:

Key audit matters—Those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Key audit matters are selected from matters communicated with those charged with governance.

Requirements

Determining Key Audit Matters

8. The auditor shall determine which of the matters communicated with those charged with governance are the key audit matters. In making this determination, the auditor shall take into account areas of significant auditor attention in performing the audit, including: (Ref: Para. A1–A14, A24)
 - (a) Areas identified as significant risks in accordance with ISA 315 (Revised)¹ or involving significant auditor judgment. (Ref: Para. A15–A19)
 - (b) Areas in which the auditor encountered significant difficulty during the audit, including with respect to obtaining sufficient appropriate audit evidence. (Ref: Para. A20–A21)
 - (c) Circumstances that required significant modification of the auditor's planned approach to the audit, including as a result of the identification of a significant deficiency in internal control. (Ref: Para. A22–A23)

Communicating Key Audit Matters

9. The auditor shall communicate the key audit matters determined in accordance with paragraph 8 in a separate section of the auditor's report under the heading "Key Audit Matters." The auditor's report shall state that:
 - (a) Key audit matters are those matters that, in the auditor's professional judgment¹, were of most significance in the audit of the financial statements [of the current period];
 - (b) Key audit matters are selected from matters communicated with [those charged with governance], but are not intended to represent all matters that were discussed with them;
 - (c) The auditor's procedures relating to these matters were designed in the context of the audit of the financial statements as a whole; and
 - (d) The auditor's opinion on the financial statements is not modified with respect to any of the key audit matters, and the auditor does not express an opinion on these individual matters. (Ref: Para. A25–A29)
10. The auditor shall describe each key audit matter in the Key Audit Matters section using an appropriate subheading, except in the circumstances explained in paragraph 11. The description of each key audit matter shall include: (Ref: Para. A30)
 - (a) An explanation of why the auditor considered the matter to be one of most significance in the audit and, to the extent the auditor considers it necessary as part of this explanation, its effect on the audit; and (Ref: Para. A31–A41)
 - (b) A reference to the related disclosure(s), if any, in the financial statements. (Ref: Para. A42–A43)

¹ ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

Interaction between Descriptions of Key Audit Matters and Other Elements Required to Be Included in the Auditor's Report

11. A matter giving rise to a qualified or adverse opinion in accordance with proposed ISA 705 (Revised),² or the existence of a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern (hereinafter referred to as "material uncertainty") in accordance with proposed ISA 570 (Revised),³ is by its nature a key audit matter. However, the auditor shall:
- (a) Report on these matter(s) in accordance with the applicable ISA(s);
 - (b) Not describe these matter(s) in the Key Audit Matters section of the auditor's report; and
 - (c) Include a reference to the Basis for Qualified (or Adverse) Opinion or the Going Concern section(s) in the introductory language of the Key Audit Matters section. (Ref: Para. A44–A45)

Communication with Those Charged with Governance

12. The auditor shall communicate with those charged with governance those matters the auditor has determined are the key audit matters to be included in the auditor's report. (Ref: Para. A46)

Circumstances in which the Auditor Has Determined There Are No Key Audit Matters

13. If the auditor determines that there are no key audit matters to communicate in the auditor's report, the auditor shall:
- (a) Discuss this conclusion with the engagement quality control reviewer, for those engagements where one has been appointed;
 - (b) Communicate this conclusion with those charged with governance; and
 - (c) Explain in the auditor's report that this section of the auditor's report is intended to describe the matters communicated with those charged with governance that the auditor has determined, in the auditor's professional judgment, were of most significance in the audit of the financial statements and the auditor has determined that there are no matters to report. (Ref: Para. A47–A48)

Documentation

14. The auditor shall document the matters that will be communicated as key audit matters, and the significant professional judgments made in reaching this determination, in accordance with ISA 230.⁴ This includes, where applicable, the rationale for the auditor's determination that there are no key audit matters to communicate in the auditor's report. (Ref: Para. A49)

² Proposed ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*, paragraphs 7–8

³ Proposed ISA 570 (Revised), *Going Concern*, paragraphs 21–23

⁴ ISA 230, *Audit Documentation*, paragraphs 8(c) and A10

Application and Other Explanatory Material

Determining Key Audit Matters

The Auditor's Decision-Making Process to Determine Key Audit Matters (Ref: Para. 8)

- A1. Determining the key audit matters to communicate in the auditor's report is a matter of the auditor's professional judgment. The auditor's decision-making process in determining key audit matters is designed to select a smaller number of matters, from the matters communicated with those charged with governance, based on the auditor's judgment about which matters were of most significance in the audit.
- A2. Significance can be described as the relative importance of a matter, taken in context. The significance of a matter is judged by the auditor in the context in which it is being considered. Significance can be considered in the context of quantitative and qualitative factors, such as relative magnitude, the nature and effect on the subject matter and the expressed interests of intended users or recipients. This involves an objective analysis of the facts and circumstances, including the nature and extent of communication with those charged with governance. For example, the auditor may have had more in-depth and frequent communications with those charged with governance on more difficult and complex matters.
- A3. ISA 320⁵ notes that it is reasonable for the auditor to assume that users of the financial statements:
- (a) Have a reasonable knowledge of business and economic activities and accounting and a willingness to study the information in the financial statements with reasonable diligence;
 - (b) Understand that the financial statements are prepared, presented and audited to levels of materiality;
 - (c) Recognize the uncertainties inherent in the measurement of amounts based on the use of estimates, judgment and the consideration of future events; and
 - (d) Make reasonable economic decisions on the basis of the information in the financial statements.

Because the auditor's report accompanies the audited financial statements, the users of the auditor's report are considered to be the same as the users of the financial statements.

- A4. Users of the financial statements have expressed an interest in those matters about which the auditor and those charged with governance had the most robust dialogue as part of the two-way communication required by proposed ISA 260 (Revised)⁶ and have called for additional transparency about those communications. Therefore, a focus on "matters of most significance in the audit" and the application of the requirement in paragraph 8 of this ISA is intended to result in the auditor reporting on matters that are likely to be of interest to users.
- A5. Of the matters communicated with those charged with governance, users have expressed particular interest in understanding areas of significant auditor attention in performing the audit because they are often related to the areas of significant management judgment in preparing the financial statements. Users have also called for greater transparency about significant judgments made by the auditor in forming the opinion on the financial statements as a whole.

⁵ ISA 320, *Materiality in Planning and Performing the Audit*

⁶ Proposed ISA 260 (Revised), *Communication with Those Charged with Governance*

- A6. The auditor may develop a preliminary view at the planning stage about matters that are likely to be the key audit matters in the audit and may communicate this with those charged with governance when discussing the planned scope and timing of the audit in accordance with proposed ISA 260 (Revised).
- A7. The number of key audit matters to be included in the auditor's report may be affected by the size and complexity of the entity, the nature of its business and environment, and the facts and circumstances of the audit engagement. In general, the greater the number of key audit matters, the less useful the auditor's communication of key audit matters may be. When the auditor has determined a long list of key audit matters, the auditor may need to reconsider whether each of these matters meets the definition of a key audit matter.
- A8. The auditor's determination of key audit matters is limited to those matters of most significance in the audit of the financial statements of the current period, even when comparative financial statements are presented (i.e., even when the auditor's opinion refers to each period for which financial statements are presented).⁷ When comparative financial information is presented, as required by paragraph 9(a) the introductory language of the Key Audit Matters section is tailored to draw attention to the fact that the key audit matters described relate to only the audit of the financial statements of the current period, and may include reference to the specific period covered by those financial statements (e.g., "for the year ended December 31, 20X1").
- A9. Notwithstanding that the auditor's communication of key audit matters is for the audit of the financial statements of the current period, it may nevertheless be useful for the auditor to consider whether a matter that was a key audit matter in the audit of the financial statements of the previous period continues to be a key audit matter in the audit of the financial statements of the current period. For example, the auditor may consider whether any economic conditions or entity-specific circumstances that led to a matter being determined as a key audit matter in the prior period continue to exist. It may also be appropriate for the auditor to consider whether the significance of a key audit matter in the prior period has diminished, for example if the effects of a significant unusual transaction in the prior period are not material in the current period. Finally, it may be the case that, while a matter communicated as a key audit matter in the prior period continues to affect the financial statements of the current period, other matters arising during the current period audit may be considered to be relatively more significant and the prior period key audit matter may not, in the auditor's judgment, be considered to be among those of most significance in the current period's audit.

Relationship between Key Audit Matters and the Auditor's Opinion (Ref: Para. 8)

- A10. As explained in paragraph 11, matters giving rise to a modification of the auditor's opinion are, by their nature, key audit matters, notwithstanding that such matters are not presented in the Key Audit Matters section of the auditor's report.
- A11. When the auditor is expressing a qualified or adverse opinion, a discussion of any other key audit matters would still be relevant to enhancing users' understanding of the audit and therefore the requirement in paragraph 8 applies. However, proposed ISA 705 (Revised) prohibits the auditor from communicating key audit matters when the auditor disclaims an opinion on the financial statements.⁸

⁷ See ISA 710, *Comparative Information—Corresponding Figures and Comparative Financial Statements*.

⁸ Proposed ISA 705, paragraph 29

Areas of Significant Auditor Attention (Ref: Para. 8)

- A12. The concept of significant auditor attention relates to the fact that an audit is risk-based and focuses on areas of higher assessed risks of material misstatement, including significant risks, and areas of complexity. This affects the allocation of resources or extent of audit effort in relation to such matters, in particular in relation to the extent of involvement of senior personnel on the audit engagement. The auditor may also have considered it necessary to involve persons with expertise in a specialized area of accounting or auditing, whether engaged or employed by the firm, on the engagement, to address these areas. Matters that required significant hours by the engagement partner, or an auditor's expert, may be key audit matters.
- A13. ISA 220 establishes requirements for the engagement partner in relation to undertaking appropriate consultation on difficult or contentious matters.⁹ The auditor may have consulted with others within the firm or outside the firm on a significant technical matter, which may be an indicator that it is a key audit matter. The engagement partner is also required to discuss, among other things, significant matters arising during the audit engagement with the engagement quality control reviewer.¹⁰ Key audit matters are likely to have been discussed with, or evaluated by,¹¹ the engagement quality control reviewer, in particular those involving consultation.
- A14. Paragraph 8 includes certain areas of significant auditor attention that may be indicative of key audit matters. As the areas may be interrelated, the applicability of more than one of them in the context of a particular matter communicated with those charged with governance may increase the likelihood of the auditor identifying that matter as a key audit matter.

Significant risks (Ref: Para. 8(a))

- A15. Proposed ISA 260 (Revised) requires the auditor to communicate with those charged with governance an overview of the planned scope and timing of the audit, which includes communicating about the significant risks identified by the auditor.¹² Areas of significant management judgment and significant unusual transactions may often be identified as significant risks. However, the identification of a matter as a significant risk, including a matter identified as a significant risk due to fraud, does not necessarily mean that such a matter will be determined to be a key audit matter.
- A16. In determining whether significant risks are key audit matters, it is likely that the auditor will give greater consideration to significant risks that have been specifically identified in the context of the entity, rather than to those that have been so identified only because they are presumed in the ISAs to be significant risks. For example, ISA 240 presumes that there are risks of fraud in revenue recognition and requires the auditor to treat those assessed risks of material misstatement due to fraud as significant risks.¹³ In addition, ISA 240 indicates that, due to the unpredictable way in which management override of controls could occur, it is a risk of material misstatement due to fraud and thus a significant risk.¹⁴

⁹ ISA 220, *Quality Control for an Audit of Financial Statements*, paragraph 18

¹⁰ ISA 220, paragraph 19

¹¹ ISA 220, paragraph 20

¹² Proposed ISA 260 (Revised), paragraph 15

¹³ ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*, paragraphs 26–27

¹⁴ ISA 240, paragraph 31

- A17. Proposed ISA 260 (Revised) requires the auditor to communicate with those charged with governance the auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates, and financial statement disclosures.¹⁵ In many cases, this relates to critical accounting estimates and related disclosures, which are likely to be areas of significant auditor attention, and therefore may be identified as significant risks. Accounting estimates with high estimation uncertainty are of interest to users of the financial statements because, among other things, they are highly dependent on judgment, may require the involvement of both a management's expert and an auditor's expert, and may be identified as significant risks.¹⁶ As a result, these areas of the audit may be considered key audit matters.
- A18. Significant unusual transactions, including significant transactions with related parties, and the auditor's response to them, also may be key audit matters about which communication in the auditor's report would be useful. When such a transaction exists, management or those charged with governance may have communicated the matter with the auditor prior to undertaking the transaction and at various stages throughout the audit. The auditor may have assessed the transaction as a significant risk and there may have been difficult judgments both by management and the auditor in relation to recognition, measurement, presentation or disclosure of the transaction.
- A19. Paragraph A12 of proposed ISA 260 (Revised) explains that the auditor may also communicate with those charged with governance about assessed risks of material misstatement other than identified significant risks that are anticipated to have the greatest effect on the overall audit strategy or on the audit plan, including on the efforts of the engagement team. Such matters may also be determined to be key audit matters.

Significant difficulty during the audit (Ref: Para. 8(b))

- A20. Proposed ISA 260 (Revised) requires the auditor to communicate significant difficulties, if any, encountered during the audit with those charged with governance.¹⁷ The ISAs acknowledge potential difficulties in relation to, for example:
- Related party transactions,¹⁸ in particular limitations on the auditor's ability to obtain audit evidence that all other aspects of a related party transaction (other than price) are equivalent to those of a similar arm's length transaction.
 - Limitations on the group audit, for example, where the group engagement's team's access to information may have been restricted.¹⁹
 - Extensive unexpected effort required to obtain sufficient appropriate audit evidence.²⁰

¹⁵ Proposed ISA 260 (Revised), paragraph 16(a)

¹⁶ See paragraph 11 of ISA 540, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*.

¹⁷ Proposed ISA 260 (Revised), paragraph 16(b)

¹⁸ ISA 550, *Related Parties*, paragraph A42

¹⁹ ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*, paragraph 49(d)

²⁰ Proposed ISA 260 (Revised), paragraph A18

The auditor may also communicate with those charged with governance about significant difficulties encountered when obtaining sufficient appropriate audit evidence relating to critical accounting estimates made by management or a management's expert.

- A21. In some circumstances, difficulties encountered during the audit may constitute a scope limitation that requires a modification of the auditor's opinion.²¹ As explained in paragraph A10, a matter giving rise to a modification of the auditor's opinion is, by its nature, a key audit matter. However, because of the importance of communicating to users the reasons for the modifications of the opinion, the description of the key audit matter leading to the modified opinion is presented in the Basis for Qualified (or Adverse) Opinion section of the auditor's report instead of the Key Audit Matters section (see paragraph 11).

Circumstances that required significant modification of the auditor's planned approach to the audit (Ref: Para. 8(c))

- A22. Revision to the auditor's risk assessment and reevaluation of the planned audit procedures with respect to a particular area of the financial statements (i.e., a significant change in the audit approach, for example, when a significant deficiency in internal control has been identified) may lead the auditor to determine that area to be a key audit matter. ISA 315 (Revised) notes that the auditor's assessment of the risks of material misstatement at the assertion level may change during the course of the audit as additional audit evidence is obtained.²² Difficulties in obtaining audit evidence, as contemplated by paragraph 8(b), may cause the auditor to reevaluate the planned audit approach. Further, if during the audit the auditor's risk assessment is significantly revised, the auditor may consider the facts and circumstances giving rise to the changed assessment to be a key audit matter. In particular, if the auditor encounters circumstances that cause the auditor significant difficulty in applying necessary audit procedures, the auditor may need to obtain audit evidence by performing additional audit procedures beyond those originally contemplated.
- A23. ISA 265 requires the auditor to communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis.²³ The auditor is not required by the ISAs to report externally on significant deficiencies in internal control identified during the audit. However, the identification of a significant deficiency may be an indicator of a key audit matter relating to the area(s) of the financial statements affected by the significant deficiency.

Other considerations relevant to determining the significance of individual matters

- A24. In addition to the factors included in paragraph 8 and others that may be indicative of an area of significant auditor attention (see paragraph A14), considerations that may be relevant to determining the significance of a matter communicated with those charged with governance and whether such a matter is a key audit matter include:
- The industry in which the entity operates. There may be areas of complexity in financial reporting that are specific to a particular industry, or accounting policies unique to that industry.

²¹ See paragraph A8 of proposed ISA 705 (Revised).

²² ISA 315 (Revised), paragraph 31

²³ ISA 265, *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management*, paragraph 9

- Recent significant economic, accounting, regulatory or other developments. For example, significant changes to the economic environment that affected management's assumptions or judgments, or the auditor's approach, may cause the auditor to determine that a matter is a key audit matter.
- Whether the matter involved a number of separate, but related, auditing considerations. For example, long-term contracts may involve significant auditor attention with respect to revenue recognition, litigation or other contingencies, and may have an effect on other accounting estimates.
- Whether the auditor determined it was necessary to obtain written representation from management to support other audit evidence relevant to the matter or one or more specific assertions in the financial statements relating to the matter.²⁴ For example, such written representations may include representations about plans or intentions that may affect the carrying value or classification of assets and liabilities.

Communicating Key Audit Matters (Ref: Para. 9–12)

A25. The objective of communicating key audit matters in the auditor's report is in the context of the auditor having formed an opinion on the financial statements as a whole. Communicating key audit matters in the auditor's report is not intended to:

- (a) Express an opinion on individual matters; or
- (b) Be a substitute for the auditor expressing a qualified opinion or an adverse opinion when required by the circumstances of a specific audit engagement (see proposed ISA 705 (Revised)).

A26. Proposed ISA 706 (Revised)²⁵ establishes mechanisms for auditors of financial statements of all entities to include additional communication in the auditor's report through the use of Emphasis of Matter and Other Matter paragraphs when the auditor considers it necessary to do so. The use of such paragraphs is not a substitute for a description of individual matters as key audit matters determined in accordance with paragraph 8 of this ISA.²⁶

A27. Illustrations 1 and 2 of the Appendix to proposed ISA 700 (Revised)²⁷ include descriptions of key audit matters in the auditor's report when the auditor of financial statements of a listed entity expresses an unmodified opinion on the financial statements.

Placement of the Key Audit Matters Section in the Auditor's Report

A28. Placement of the Key Audit Matters section in close proximity to the auditor's opinion is intended to give prominence to such information, and to acknowledge the perceived value of engagement-specific information to users.

A29. The order of presentation of individual matters within the Key Audit Matters section is a matter of professional judgment. Such information may be best organized in order of relative importance,

²⁴ See ISA 580, *Written Representations*.

²⁵ Proposed ISA 706 (Revised), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*

²⁶ Proposed ISA 706 (Revised), paragraphs 8(b) and 10(b)

²⁷ Proposed ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

based on the auditor's judgment, and the requirement in paragraph 10 to include subheadings is intended to further differentiate the matters.

Nature and Extent of the Description of a Key Audit Matter in the Auditor's Report (Ref: Para. 10)

A30. The sufficiency and appropriateness of the description of a key audit matter is a matter of professional judgment, but the description is intended to provide a succinct explanation to enable users of the financial statements to understand why the matter was one of most significance in the audit and, to the extent the auditor considers it necessary, its effect on the audit. Limiting the use of highly technical auditing terms helps to enable users who do not have a reasonable knowledge of auditing to understand the basis for the auditor's focus on particular matters during the audit.

Explaining Why the Auditor Considered the Matter to Be One of Most Significance in the Audit (Ref: Para. 10(a))

A31. The description of a key audit matter in the auditor's report is intended to provide insight as to why the matter was determined to be a key audit matter. The description may make reference to the following:

- Factors that may have influenced the auditor's risk assessment, for example:
 - High estimation uncertainty.
 - Economic conditions that affected the auditor's ability to obtain audit evidence, for example illiquid markets for certain financial instruments.
 - New or emerging accounting policies, for example entity-specific or industry-specific matters on which the engagement team consulted within the firm.
 - Changes in the entity's strategy or business model that had a material effect on the financial statements.
- The auditor's approach to the matter, for example whether the auditor used an expert to obtain audit evidence, for example the use of actuaries or other experts to evaluate management's assumptions.
- Whether the matter involved significant management judgment.
- Key communications with those charged with governance.

A32. Written communications, or the auditor's documentation of oral communications, with those charged with governance and other audit documentation provides a useful basis for the auditor's communication in the auditor's report. This is because audit documentation in accordance with ISA 230 is intended to address the significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions, and serves as a record of the nature, timing and extent of the audit procedures performed, the results of those procedures, and the audit evidence obtained. Such documentation may assist the auditor in developing a description of key audit matters that explains the significance of the matter and also in applying the requirement in paragraph 14.

A33. The factors in paragraph 8 and the related guidance in paragraphs A12–A24 related to determining key audit matters may also be helpful for the auditor in considering how such matters are to be communicated in the auditor's report. For example, explaining the factors that led the auditor to

conclude that a particular matter was the subject of significant auditor attention and therefore a key audit matter is likely to be of interest to users.

- A34. The discussion of key audit matters is not a substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or a remedy for material misstatement of the financial statements relating to non-disclosure of information required to be disclosed. In such cases, the auditor is required to express a modified opinion in accordance with proposed ISA 705 (Revised).
- A35. In addition, law, regulation or ethical standards may restrict the auditor's ability to communicate key audit matters because of investigations, auditor confidentiality or data protection requirements. The ISAs do not override law or regulation that governs an audit of financial statements or relevant ethical requirements, but potential conflicts between the auditor's legal and ethical obligations and obligations to communicate in accordance with this ISA may be complex. In such cases, the auditor may consider discussing the situation with those charged with governance and may consider obtaining legal advice.
- A36. Some matters that are determined to be key audit matters may be viewed as sensitive, because of their nature and the fact that such matters may not be disclosed in the financial statements, for example:
- A fraud risk specifically identified in the context of the entity.
 - A significant deficiency in internal control.

In such cases, the auditor may need to consider how best to describe the key audit matter in order to explain why the matter was one of most significance in the audit.

- A37. It is appropriate for the auditor to seek to avoid the description of key audit matters inappropriately providing original information about the entity that is the responsibility of the entity's management and those charged with governance unless, in the auditor's judgment, the additional information that the auditor may provide is critical to the auditor's description of the key audit matter and providing such information is not prohibited by law or regulation. In such circumstances, the auditor may encourage management or those charged with governance to make relevant disclosures in the financial statements that include such other information, so that reference can be made to those disclosures within the description of the key audit matters in the auditor's report, rather than the auditor providing original information.

The effect on the audit

- A38. In explaining why the auditor considered a matter to be one of most significance in the audit, the auditor may consider it necessary to describe its effect on the audit. This may include a brief overview of procedures performed or the auditor's approach to the matter, or may include an indication of the outcome of the auditor's procedures with respect to the matter.
- A39. There may be challenges in describing the auditor's procedures, particularly in complex, judgmental areas of the audit. In particular, it may be difficult to summarize the procedures performed in a succinct way that adequately communicates the nature and extent of the auditor's response to the assessed risks of material misstatement, and the significant auditor judgments involved. Nonetheless, the auditor may consider it necessary, or may be required to, describe certain procedures performed to appropriately communicate to users why the auditor considered the

matter to be of most significance in the audit. Such description typically would be at a high level, rather than include a detailed description of procedures.

- A40. Describing the audit approach in relation to a matter, in particular when the audit approach required significant tailoring to the facts and circumstances of the entity, may assist users in understanding unusual circumstances and significant auditor judgment required to address the risk of material misstatement. This may be appropriate, for example, when the auditor employed or engaged an auditor's expert or the auditor consulted on complex matters within or outside the firm. In addition, the audit approach in a particular period may have been influenced by entity-specific circumstances, economic conditions, or industry-developments (see paragraph A24). Noting these types of circumstances in the auditor's report and their effect on the audit assists users in understanding why matters were key audit matters in the audit.
- A41. In order to avoid creating uncertainty as to whether the matter was satisfactorily resolved, the auditor may also consider it necessary to address the specific outcome of the auditor's response in the description of the key audit matter in the auditor's report. However, if in explaining the effect on the audit, the auditor considers it necessary to indicate findings or a conclusion in relation to a matter, there is also a need for the auditor to avoid giving the impression that the discussion about key audit matters in the auditor's report is intended to convey an opinion on individual matters (see paragraph 9(d)).

Reference to Where the Matter Is Disclosed in the Financial Statements (Ref: Para. 10(b))

- A42. Paragraph 10 requires the description of each key audit matter to explain why the auditor considered the matter to be one of most significance in the audit. Accordingly, the description of key audit matters cannot merely reiterate what is disclosed in the financial statements. However, a reference to any related disclosures enables users to understand both management's and the auditor's perspectives on these matters.
- A43. In addition to referring to related disclosure(s), the auditor may draw attention to key aspects of them. More robust disclosure by management about specific aspects or factors in relation to how a particular matter is affecting the financial statements of the current period may help the auditor in pinpointing particular aspects of how the matter was addressed in the audit such that users can understand why the matter is a key audit matter. For example, when an entity includes robust disclosure about accounting estimates, the auditor may draw attention to the disclosure of key assumptions and other sources of estimation uncertainty, the disclosure of the range of possible outcomes, and other qualitative and quantitative disclosures relating to key sources of estimation uncertainty or critical accounting estimates, as part of explaining why the matter was one of most significance in the audit.

Interaction between Descriptions of Key Audit Matters and Other Elements Required to Be Included in the Auditor's Report (Ref: Para. 11)

- A44. Presenting the description of matters for which the auditor has concluded it is necessary to modify the opinion separately in the Basis for Qualified (or Adverse) Opinion section helps to promote users' understanding and to identify such circumstances when they occur. Separating the discussion of these matters from other key audit matters therefore gives them the appropriate prominence in the auditor's report. The Appendix in proposed ISA 705 (Revised) includes illustrative examples of how the introductory language in the Key Audit Matters section is affected in such circumstances.

A45. The existence of a material uncertainty relating to going concern is, by its nature, a key audit matter. However, the auditor's statements relating to going concern are required to be presented in a separate section of the auditor's report under the heading "Going Concern."²⁸ When a material uncertainty has been identified and adequate disclosure is made in the financial statements, proposed ISA 570 (Revised) requires the auditor to include a statement in the auditor's report to draw attention to the note in the financial statements that discloses a material uncertainty relating to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern.²⁹ When a material uncertainty has been identified and adequate disclosure is not made in the financial statements, proposed ISA 570 (Revised) requires the auditor to modify the auditor's opinion and describe this in the Basis for Qualified (or Adverse) Opinion paragraph as well as the Going Concern section of the auditor's report.³⁰ The Appendix in proposed ISA 570 (Revised) includes illustrative examples of how the introductory language in the Key Audit Matters section is affected in such circumstances.

Communication with Those Charged with Governance (Ref: Para. 12)

A46. The communication required by paragraph 12 enables those charged with governance to be made aware of the key audit matters that the auditor intends to communicate in the auditor's report, and provides them with an opportunity to obtain further clarification where necessary. As explained in paragraph A37, in some cases, management or those charged with governance may decide to include new or enhanced disclosures in the financial statements relating to the key audit matter, for example to provide more robust disclosures about sensitivity of key assumptions used in accounting estimates or the entity's rationale for a particular accounting practice or policy when acceptable alternatives exist under the applicable financial reporting framework.

Circumstances in which the Auditor Has Determined There Are No Key Audit Matters (Ref: Para. 13)

A47. Except in certain limited circumstances (e.g., a listed entity that has very limited operations or assets), it is expected to be rare that the auditor of financial statements of a listed entity would not determine at least one key audit matter from the matters communicated with those charged with governance. In addition, the requirements in paragraph 13(a)–(b) may provide an opportunity for those most familiar with the significant matters arising during the audit to provide input that may cause the auditor to re-evaluate the auditor's determination that there are no key audit matters.

A48. The following illustrates the presentation in the auditor's report if the auditor has determined there are no key audit matters to report:

Key Audit Matters

This section of our auditor's report is intended to describe the matters selected from those communicated with [*those charged with governance*] that, in our professional judgment, were of most significance in our audit of the financial statements. [Except for the matter described in the *Basis for Qualified (or Adverse) Opinion* section and the material uncertainty described in the *Going Concern* section,] We have determined that there are no such matters to report.

²⁸ Proposed ISA 570 (Revised), paragraph 19

²⁹ Proposed ISA 570 (Revised), paragraph 22

³⁰ Proposed ISA 570 (Revised), paragraph 23

Documentation (Ref: Para. 14)

A49. The professional judgments for the matters determined to be key audit matters are likely to be supported by the documentation of the auditor's communications with those charged with governance and the audit documentation relating to each individual key audit matter (see paragraph A32), as well as certain other audit documentation of the significant matters arising during the audit (e.g., a completion memorandum). The documentation of the significant professional judgments made in determining the key audit matters draws upon this documentation. Such documentation also may provide an indication that other matters communicated with those charged with governance are not key audit matters.