AT A GLANCE
January 2015

New and Revised Auditor Reporting Standards and Related Conforming Amendments

This summary provides an overview of the International Auditing and Assurance Standards Board's (IAASB) new and revised Auditor Reporting standards and related conforming amendments.

Project Objectives: The objectives of the IAASB's Auditor Reporting project were to:

- Appropriately enhance the communicative value and relevance of the auditor's report through revisions to the International Standards on Auditing (ISAs) that address its structure and content; and
- Modify, in their design, the IAASB's reporting ISAs to accommodate evolving national financial reporting regimes, while at the same time ensuring that common and essential content is being communicated.

Effective Date: Audits of financial statements for periods ending on or after December 15, 2016.

For More Information: Visit the IAASB's website at www.iaasb.org/auditor-reporting.

Why change the auditor's report now and what ISAs are changing?

Enhanced auditor reporting is viewed as critical to the perceived value of the financial statement audit and thus to the continued relevance of the auditing profession.

The new and revised Auditor Reporting standards lay the foundation for the future of global auditor reporting and improved auditor communications.

An illustrative auditor's report for an audit of financial statements of a listed entity, showing the application of the IAASB's new and revised Auditor Reporting standards, is included as an **Appendix** to this At a Glance.

Why change the auditor's report now?

The auditor's report is the key deliverable addressing the output of the audit process. While users of the financial statements have signaled that the auditor's opinion on the financial statements is valued, many have called for the auditor's report to be more informative and relevant.

IAASB's deliberations in developing these standards have been informed by international research, public consultation, and stakeholder outreach, including:

- Jointly commissioned international academic research on user perceptions;
- Public consultations in May 2011, June 2012, and July 2013;
- Global roundtables and additional outreach activities; and
- Continued monitoring of, and interaction with, policymakers and national auditing standard setters with auditor reporting initiatives, such as the European Commission, the UK Financial Reporting Council, the US Public Company Accounting Oversight Board, and others.

What ISAs are changing?

The new and revised Auditor Reporting standards comprise:

- ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*;
- New ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*;
- ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*;
- ISA 706 (Revised), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*;
- ISA 570 (Revised), *Going Concern*;
- ISA 260 (Revised), *Communication with Those Charged with Governance*; and
- Conforming amendments to other ISAs.

Coming soon – ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information* includes new and revised reporting requirements relating to **other information** that is included in an entity's annual report.[1]

The IAASB will also propose changes to auditor's reports on special purpose financial statements in a soon to be released **exposure draft**.

[1] ISA 720 (Revised) which as was approved by the IAASB at its December 2014 meeting. Subject to the Public Interest Oversight's Board consideration of due process followed, ISA 720 (Revised) will be issued in April 2015 and will come into effect at the same time as the new and revised Auditor Reporting standards.

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How will changes to the auditor's report affect investors, audit committees and preparers?

The primary beneficiaries of the IAASB's work on auditor reporting will be investors, analysts and other users of the auditor's report and the audited financial statements.

The implementation of the new and revised standards will represent a significant change in practice, with collaboration needed by all participants in the financial reporting supply chain to ensure the IAASB's objectives of the auditor reporting project will be realized.

Expected benefits of the changes to the ISAs and the auditor's report

The auditor's report is the key deliverable addressing the output of the audit process. The IAASB intends for its new and revised Auditor Reporting standards to result in an auditor's report that increases the confidence in the audit and the financial statements, which is in the public interest.

The IAASB believes that in addition to the **increased transparency** and **enhanced informational value** of the auditor's report, changes to auditor reporting will also have the benefit of:

- **Enhanced communications** between the auditor and investors as well as between auditors and those charged with governance;
- **Increased attention** by management and those charged with governance (e.g., the audit committee) **to the disclosures** in the financial statements to which reference is made in the auditor's report; and
- **Renewed focus of the auditor** on matters to be reported, which could indirectly result in an increase in professional skepticism.

Effect on the financial reporting process

- The enhancements to the auditor's report **build upon the underlying concepts in an ISA audit** addressing how a risk-based audit is performed and what is required to be communicated with those charged with governance.
- The changes to the ISAs **do not change the underlying work effort** required in an ISA audit, but rather focus on increasing transparency about the audit that was performed.
- While auditor communications in the auditor's report are expected to be entity-specific in order to be informative to users, it remains the responsibility of management, with the oversight of those charged with governance, to communicate relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework.

What are the key enhancements to the auditor's report?

The auditor's opinion on the financial statements is valued; however, in the wake of the global financial crisis, many have called for the auditor's report to be more informative – in particular, for auditors to provide more relevant information to users based on the audit that was performed.

The new and revised Auditor Reporting standards and related conforming amendments respond to that call.

Key enhancements

Mandatory for audits of financial statements of listed entities, voluntary application for entities other than listed entities:

- New section to communicate **key audit matters** (KAM). KAM are those matters that, in the auditor's judgment, were of most significance in the audit of the current-period financial statements.
- Disclosure of the **name of the engagement partner**, with a "harm's way" exemption.

For all audits:

- **Opinion section** required to be **presented first**, followed by the Basis for Opinion section, unless law or regulation prescribe otherwise.
- Enhanced auditor reporting on **going concern** (GC), including:
  - o Description of the respective responsibilities of management and the auditor for GC;
  - o A separate section **when a material uncertainty exists**, and is adequately disclosed, under the heading "Material Uncertainty Related to Going Concern"; and
  - o New requirement to challenge adequacy of disclosures for "**close calls**" in view of the applicable financial reporting framework when events or conditions are identified that may cast significant doubt on an entity's ability to continue as a GC.
- Affirmative **statement about the auditor's independence** and fulfillment of **relevant ethical responsibilities**, with disclosure of the jurisdiction of origin of those requirements or reference to the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants*.
- **Enhanced description of the responsibilities of the auditor** and key features of an audit, together with the provision that certain components of this description may be presented in an appendix to the auditor's report or, where law, regulation or national auditing standards expressly permit, by reference in the auditor's report to a website of an appropriate authority.

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How are KAM determined?

The purpose of communicating KAM is to enhance the communicative value of the auditor's report by providing greater transparency about the audit that was performed.

KAM provide intended users of the financial statements with additional information about those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period.

The communication of KAM may also provide intended users a basis to further engage with management and those charged with governance.

Consistency versus relevance

The IAASB acknowledged the importance of achieving an appropriate balance between the need for prescription in the standard to promote consistency in which matters are determined and communicated as KAM, with the need to allow for auditor judgment to ensure that the KAM communicated in the auditor's report are as entity-specific and relevant as possible.

Accordingly, ISA 701 sets out a **decision framework for auditors** using the communications with those charged with governance as a starting point. From the matters communicated with those charged with governance, the auditor determines those **matters that required significant auditor attention**. In fulfilling this requirement, the auditor is always required to explicitly consider:

- Areas of higher assessed risks of material misstatement, or significant risks identified in accordance with ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*.
- Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty.
- The effect on the audit of significant events or transactions that occurred during the year.

From the matters that required significant auditor attention, the auditor determines which were of the **most significance** in the audit of the financial statements of the current period and therefore are KAM.

Sensitive matters

The IAASB addressed specific concerns raised about the communication of matters for which information has not been publicly disclosed by the entity ("sensitive matters"). The IAASB agreed to add a requirement in ISA 701 to allow for the possibility, in **extremely rare circumstances**, that the auditor might decide not to communicate a matter determined to be a KAM in the auditor's report. Importantly, the IAASB agreed that such a requirement should not be overly permissive in this regard or explicitly prohibit the communication of certain types of sensitive matters in the auditor's report.

What is included in the description of a KAM?

The description of a KAM should be clear, concise, understandable, and entity-specific, and should provide relevant information for the intended users of the financial statements.

ISA 701 provides flexibility to describe more broadly "how the matter was addressed in the audit", rather than specifically requiring a description of the auditor's response, findings, or procedures. The amount of detail necessary to do so is a matter of professional judgment.

The **description of a KAM** is always required to include:

- Why the matter was considered to be one of most significance in the audit and therefore determined to be a KAM;
- How the matter was addressed in the audit; and
- Reference to the related disclosure(s).

Describing how a matter was addressed in the audit

The auditor may include in the description of a KAM:

- Aspects of the auditor's response or approach that were most relevant to the matter or specific to the assessed risk of material misstatement;
- A brief overview of procedures performed;
- An indication of the outcome of the auditor's procedures; or
- Key observations with respect to the matter,

or some combination of these elements.

Care may be necessary so that the language used in the KAM description:

- Relates the matter directly to the specific circumstances of the entity, while avoiding generic or standardized language.
- Does not imply that the matter has not been appropriately resolved by the auditor in forming the opinion.
- Takes into account how the matter is addressed in the related disclosure(s) in the financial statements, if any.
- Does not contain or imply discrete opinions on separate elements of the financial statements ("piecemeal opinion").

Other matters relevant to KAM

- Should the auditor determine that there are no KAM to communicate, the auditor's report would continue to include a KAM section, but specifically highlight that the auditor has determined that there are no KAM.
- The concepts of Emphasis of Matter and Other Matter paragraphs are retained. However, when KAM are communicated, such paragraphs cannot be used as a substitute for communicating a matter determined to be a KAM.

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How has the IAASB addressed the topic of going concern (GC)?

The topic of GC is of significant interest in light of the global financial crisis. Stakeholders have called for increased focus on GC matters by management and auditors.

However, many stakeholders believe that, rather than simply requiring auditor reporting on GC, a more holistic approach is necessary. The IAASB has therefore found it necessary to adapt how the auditor's report addresses GC from what was initially proposed in its July 2013 exposure draft.

Enhanced auditor work effort on GC

Investors and others have requested **earlier warning** of potential issues that may exist with respect to an entity's ability to continue as a GC. This is particularly the case in situations where events or conditions were identified that may cast significant doubt on the entity's ability to continue as a GC, but after considering management's plans to deal with these events or conditions, management and the auditor conclude that no material uncertainty exists (i.e., "close call" situations).

Communication about GC issues is primarily the responsibility of management and those charged with governance in view of the requirements of the applicable financial reporting framework. However, the IAASB believes that there is a role for auditors to play in considering the adequacy of these disclosures.

Accordingly, ISA 570 (Revised) now includes:

- New guidance to support the auditor's **evaluation of disclosures** when a material uncertainty exists.
- A new requirement for the auditor to evaluate the adequacy of disclosures in "**close call**" situations.

ISA 701 also highlights that matters related to GC may be determined to be KAM. The IAASB acknowledges this may be a significant or difficult auditor judgment in forming the opinion on the financial statements as a whole.

New required separate section when a material uncertainty related to GC exists

The auditor's report is required to **highlight the existence of any materiality uncertainties** and will either include:

- If the disclosures are adequate, a separate section under the heading "Material Uncertainty Related to Going Concern" drawing attention to those disclosures; or
- If the disclosures are inadequate, a modified opinion as the first section of the auditor's report.

New required descriptions of management's and the auditor's responsibilities in relation to GC

All auditor's reports will include descriptions of the responsibilities of the auditor and management in relation to GC to provide an additional focus on GC.

Activities to Promote Awareness, Understanding and Effective Implementation

The IAASB is committed to ensuring the success of these new and revised standards in view of the public interest importance of the auditor reporting enhancements.

Efforts to support effective implementation of the standards will focus on promoting awareness, informing and educating users about the changes, and opening a dialogue to learn about the experiences of those responsible for adopting and implementing the standards.

Auditor reporting toolkit

The IAASB's revamped Auditor Reporting website includes access to resources aimed at promoting awareness, understanding and effective implementation of the new and revised Auditor Reporting standards. It includes:

- An Auditor Reporting Fact Sheet titled, *The New Auditor's Report: Greater Transparency into the Financial Statement Audit*, that further summarizes key aspects of the new and revised Auditor Reporting Standards
- A staff-prepared Basis for Conclusions explaining the IAASB's rationale in finalizing its Auditor Reporting standards.

During 2015 and 2016, publications and additional resources will be developed to explain various aspects or key topics in the new and revised Auditor Reporting standards, including:

- The nature and intent of KAM, including the relevant requirements in ISA 701;
- Limited number of illustrative KAM examples;
- Auditor reporting requirements related to GC;
- Listings and extracts of illustrative ISA auditor's reports; and
- Webcast and podcasts.

Post-implementation review

The IAASB intends to undertake a post-implementation review after a period of two years from the effective date. The objective will be to assess if the new and revised Auditor Reporting standards have achieved their intended effect; and to assist the IAASB in, among other matters:

- Understanding the way in which the requirements in the standards have been adopted and implemented by jurisdictions;
- Determining whether wider application of the enhancements to auditor reporting would be in the public interest;
- Identifying implementation challenges and possible areas for improvement within the standards; and
- Considering whether further enhancements to auditor reporting are necessary.

Planned outreach activities

The IAASB is planning to undertake extensive outreach, including participation in activities related to auditor reporting planned by other stakeholders.

Appendix

Illustration of an Auditor's Report on Consolidated Financial Statements of a Listed Entity Prepared in Accordance with a Fair Presentation Framework[2]

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- Audit of a complete set of consolidated financial statements of a listed entity using a fair presentation framework. The audit is a group audit of an entity with subsidiaries (i.e., ISA 600*, Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors*) applies.
- The consolidated financial statements are prepared by management of the entity in accordance with International Financial Reporting Standards (IFRSs) (a general purpose framework).
- The terms of the audit engagement reflect the description of management's responsibility for the consolidated financial statements in ISA 210, *Agreeing the Terms of Audit Engagements*.
- The auditor has concluded an unmodified (i.e., "clean") opinion is appropriate based on the audit evidence obtained.
- The relevant ethical requirements that apply to the audit comprise the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* together with the ethical requirements relating to the audit in the jurisdiction, and the auditor refers to both.
- Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with ISA 570 (Revised).
- Key audit matters have been communicated in accordance with ISA 701.
- The auditor has obtained all of the other information prior to the date of the auditor's report and has not identified a material misstatement of the other information
- Those responsible for oversight of the consolidated financial statements differ from those responsible for the preparation of the consolidated financial statements.
- In addition to the audit of the consolidated financial statements, the auditor has other reporting responsibilities required under local law or regulation.

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of ABC Company [or Other Appropriate Addressee]

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of ABC Company and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at December 31, 20X1, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

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[2] For purposes of this illustration, this auditor's report has been prepared assuming IFRSs is the applicable financial reporting framework. All references to IFRSs (or requirements under IFRSs) would be tailored to reflect the application of another financial reporting framework.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, (or *give a true and fair view of*) the consolidated financial position of the Group as at December 31, 20X1, and (*of*) its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants (IESBA Code)* together with the ethical requirements that are relevant to our audit of the consolidated financial statements in [*jurisdiction*], and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

[*Description of each key audit matter in accordance with ISA 701.*]

Other Information [or another title if appropriate such as "Information Other than the Consolidated Financial Statements and Auditor's Report Thereon"] [3]

Coming soon

Management[4] is responsible for the other information. The other information comprises the [*information included in the X report (i.e., a more specific description of the other information, such as "the management report and chairman's statement," may be used to identify the other information), but does not include the financial statements and our auditor's report thereon.*]

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRSs, and for such internal control as management determines is necessary to enable the

[3] See footnote 1 above.

[4] Throughout this illustrative auditor's report, the terms management and those charged with governance may need to be replaced by another term that is appropriate in the context of the legal framework in the particular jurisdiction.

preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements [5]

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

[5] ISA 700 (Revised) explains that the shaded text in the "Auditor's Responsibilities for the Audit of the Consolidated Financial Statements" section above can be located either: in the body of the auditor's report; an Appendix to the auditor's report; or when law, regulation or national auditing standards expressly permit, reference can be made to a website of an appropriate authority that contains a description of the auditor's responsibilities.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on Other Legal and Regulatory Requirements

[*The form and content of this section of the auditor's report would vary depending on the nature of the auditor's other reporting responsibilities prescribed by local law, regulation, or national auditing standards. The matters addressed by other law, regulation or national auditing standards (referred to as "other reporting responsibilities") shall be addressed within this section unless the other reporting responsibilities address the same topics as those presented under the reporting responsibilities required by the ISAs as part of the Report on the Audit of the Consolidated Financial Statements section. The reporting of other reporting responsibilities that address the same topics as those required by the ISAs may be combined (i.e., included in the Report on the Audit of the Consolidated Financial Statements section under the appropriate subheadings) provided that the wording in the auditor's report clearly differentiates the other reporting responsibilities from the reporting that is required by the ISAs where such a difference exists.]*

The engagement partner on the audit resulting in this independent auditor's report is [*name*].

[*Signature in the name of the audit firm, the personal name of the auditor, or both, as appropriate for the particular jurisdiction*]

[*Auditor Address*]

[*Date*]