



Meeting: IAASB Consultative Advisory Group

Meeting Location: Brussels

Meeting Date: March 6–7, 2012

Agenda Item

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Auditor Reporting—Building Blocks

Objective of Agenda Item

1. To consider a new auditor reporting framework aimed at enhancing the communicative value of the extant ISA 700¹ auditor's report while accommodating the financial reporting needs of various entities across various jurisdictions.

Papers to Be Referred to during Discussion

2. The discussion on this topic will follow the structure of this CAG Paper. Within this paper, reference is made to **Agenda Item L.1** to facilitate the discussion. Discussion of the general approach to the auditor reporting project is provided in **Agenda Item G** and the project proposal approved by the IAASB in December 2011 is provided in **Agenda Item G.1**.

Background

3. Users of financial statements and CAG representatives have indicated that consistency is an important feature in auditor reporting of all entities across jurisdictions. ISA 700 was developed recognizing a desire for consistent and comparable auditor's reports. Respondents to responses from the May 2011 Consultation Paper (CP) on auditor reporting:
 - Suggested that there is a lack of consistency in current auditor reporting under extant ISA 700.²
 - Noted that there is not a common understanding by what is meant by the term consistency among users of audited financial statements.
 - Indicated a need for more relevant auditor reporting and for auditor's reports to include more tailored and engagement specific information.³

¹ ISA 700, *Forming an Opinion and Reporting on Financial Statements*

² Discussions with National Standard Setters (NSS) indicate that ISA 700 has not been adopted in certain jurisdictions, or has been modified, due to the need to provide for national circumstances (such as corporate governance regime) and regulatory requirements (for example, reporting on other information), suggesting an inherent lack of consistency in auditor reporting across jurisdictions.

³ As further discussed at Agenda Paper H.1, while providing more tailored and engagement specific information in auditor's reports are likely to make auditor's reports more relevant, doing so may also possibly make them less comparable even for the same type of entity within the same jurisdiction.

- Expressed concern that it would be unhelpful for the IAASB, U.S. Public Company Accounting Oversight Board (PCAOB), European Commission (EC), and U.K. Financial Reporting Council (FRC) to move in different directions in relation to auditor reporting.
 - Indicated that users of SME reports have easy access to the additional information sought by some investors and that any incremental costs associated with providing such information within the SME community would outweigh the benefits.
4. Paragraphs 22–27 of **Agenda Item G.1** note the need for a flexible “building blocks” approach in developing a revised ISA 700 auditor’s report. The premise of such an approach is in response to the varied responses to calls for change in auditor reporting - particularly the desire among users for auditor reporting to be consistent while at the same time providing customized entity-specific information about each audit.
5. As further discussed at **Agenda Item L.1**, the building blocks approach would facilitate the communications in auditor’s reports to be:
- Consistent, but relevant – providing core and conditional elements that may be tailored to meet the varied needs of financial statement users in various jurisdictions and of various entities irrespective of size and complexity.
- Proportional and scalable – accommodating differences in the information needs that may exist between users of audited financial statements of small- and medium-sized entities (SMEs) and those of listed or publicly interest entities (PIEs). Such an approach might be helpful in mitigating concerns that perceived shortcomings in the auditor’s reports of listed entities and PIEs may unnecessary increase audit costs for SMEs.
- Flexible – accommodating the necessary differences that currently exist, as well as those that may exist in the future, in corporate financial reporting and auditor reporting regimes across various jurisdictions as a result of local laws and regulations.

Matters for CAG Consideration

6. Following on from the project proposal, **Agenda Item L.1**⁴ represents the Auditor Reporting Task Force’s (TF) initial proposals in further considering the building blocks framework. These proposals reflect the debates of the TF, informed by the discussions of the Building Blocks Sub-committee, and will be considered by the IAASB for the first time at its upcoming March 2012 meeting. The TF’s recommendations are as follows:
- A flexible “building blocks” approach is needed to ensure that consistent, useful and relevant information is communicated in auditor’s reports across jurisdictions about audits of various types of entities.⁵

⁴ Agenda Item L.1 is substantively the same as IAASB March 2012 Meeting **Agenda Item 4-E** available at www.ifac.org/auditing-assurance/meetings/50th-meeting-iaasb-march-12-16-2012-toronto-canada.

⁵ IAASB December 2011 meeting materials **Agenda Items 5-A**, *Project Proposal* paragraphs 22-27 and **Agenda Item 5- B**, paragraphs 73-76, further describe the building blocks approach. Both agenda papers are available at <http://www.ifac.org/auditing-assurance/meetings/los-angeles-california>.

- The minimum required reporting elements specified in extant ISA 700⁶ when auditor reporting is otherwise specified by law or regulation should be retained as “core auditor reporting requirements.”⁷
- New core auditor reporting requirements to be required in a revised ISA 700 should be determined based on what is deemed appropriate for audits of all entities.
- A different presentation of the auditor’s report should be explored, moving the auditor’s opinion to the beginning of the auditor’s report, thereby making it more prominent, followed by those requirements that are tailored to the particular engagement, and then those that provide more standardized information about the audit process.
- Flexibility and relevance in auditor reporting should be facilitated by:
 - Allowing for “*conditional auditor reporting requirements*” that are achieved by the IAASB mandating overarching communication requirements to users:
 - (a) For some entities based on their type (i.e., listed or public interest entities (PIEs)) but allowing the national standard setters (NSS) the ability to further prescribe the level of detail needed about the specified auditor reporting element; or
 - (b) About specific matters (for example a general description of the auditor’s responsibility), but allowing flexibility in regard to whether some of those matters are included in the auditor’s report as a whole or incorporated by reference and maintained elsewhere (for example, a NSS website) provided that the messaging is consistent with the requirements of a revised ISA 700.
- The Other Reporting Responsibilities section that currently exists under extant ISA 700 should be retained in principle, as it allows for auditor reporting on other matters that are supplementary to the auditor’s responsibility under the ISAs to report on the financial statements.
- The impact on both the consistency and relevance of auditor reporting under a flexible building blocks framework will need to be further explored through discussions with users, regulators, and other stakeholders to evaluate the consequences of operationalizing revisions to the current auditor reporting framework (for example, reduced comparability of auditor’s reports across entities and jurisdictions).

Matters for CAG Consideration

The Representatives are asked for their views on these recommendations. For purposes of the discussion, attention is drawn to:

1. Whether the concept of a building blocks approach is clearly articulated and understood, including the implications of moving towards an auditor reporting framework that is likely to reduce comparability in auditor’s reports across audited entities even within the same jurisdiction (see

⁶ ISA 700, *Forming an Opinion and Reporting on Financial Statements*

⁷ ISA 700, paragraph 43

paragraphs 4-8 of **Agenda Item L.1**).

2. Whether the Representatives support the change in the placement of the auditor's opinion in a revised auditor's report (see paragraph 9 of **Agenda Item L.1**).
3. Whether the Representatives agree with the core auditor reporting requirements (see paragraph 13 and Appendix 1 of **Agenda Item L.1**).
4. Taking into account the TF's recommendations described at **Agenda Items H.1, K.1, K.2 and M.1**, do the Representatives agree with the conditional reporting requirements, including the TF's proposed categorization? Are there conditional requirement that should be required for all entities (see paragraphs 14-22, and Appendix 1 of **Agenda Item L.1**?
5. Do the Representatives believe that the IAASB should address reporting for PIEs under a new auditor's reporting standard, recognizing the various definitions that currently exist for the term PIEs (see paragraphs 14-18 of **Agenda Item L.1**)?

Material Presented – IAASB CAG PAPER

Agenda Item L.1 Auditor Reporting—Building Blocks (IAASB March 2012 Agenda Item 4-E)