

Auditor Reporting—Summary of Responses Relating to Auditor Commentary

The following represents the Task Force's (TF) preliminary views on the way forward based on responses to the Invitation to Comment (ITC) and feedback from the public roundtables. IAASB input on these matters, in the context of the detail that follows in this agenda paper, will be welcome.

- Continue to pursue the concept of auditor commentary (AC), in light of broad support across stakeholder groups for the concept, but recognizing the diversity of views about its nature and content and concerns about the auditor providing original information about the entity or the financial statements (see Question 1)
 - AC cannot solve all users' information needs on its own – there is likely a need for a more “holistic” approach to change in financial reporting, through enhancements to financial reporting frameworks and corporate governance regimes.
- Revise the objective and title of AC, bearing in mind the diversity of views about what AC is intended to achieve (see Questions 2(a)–(b)):
 - Some respondents support a focus on highlighting key matters related to the financial statements, including areas of significant management judgments using an expanded Emphasis of Matter (EOM) approach.
 - More support was noted for a focus on key audit areas and significant auditor judgment, by having the auditor explain why key matters are important from an audit perspective, including how the matters were considered in the auditor's risk assessment and response.
 - A minority of respondents would also like to know more about other “matters of audit significance”, for example matters of audit scope and strategy, including materiality, the use of experts and other auditors.
- Conduct further outreach with investors (in particular regarding the usefulness of additional information about the audit and the extent of information that is desired) and with other stakeholders (including auditors and lawyers) to ensure AC will deliver value to users and can be implemented without significant liability implications and other costs (see Question 2(c))
- Develop criteria for AC, considering whether significant risks (as defined in the ISAs) should be a primary criterion, taking into account that the matters that require the most significant auditor judgment are generally inclusive of those that require the most significant management judgment in preparing the financial statements
- Develop robust guidance to support the auditor's decision-making process in considering what matters to include in AC and how such matters should be addressed
- Consider retaining the concept of EOM paragraphs for all entities, and develop guidance to explain the relationship between EOM and AC, as well determine how to appropriately distinguish EOM from AC in the auditor's report (see Question 3)
- Consider pursuing a phased approach to requiring AC for listed entities, with the option for legislators or national standard setters (NSS) to require it for public interest entities (PIEs) or other entities, and a post-implementation review (e.g., 2 years after implementation) to obtain feedback on how AC is being used in practice and determine whether to expand requirements to other entities (see Questions 4–5)

I. Structure of this Paper

1. This paper addresses the key messages arising from the IAASB's extensive consultations and outreach relating to auditor reporting, including responses received to the June 2012 ITC. It is structured as follows to facilitate the IAASB's consideration of strategic decisions that will need to be taken to advance to an exposure draft of revised auditor reporting standards as planned in June 2013.
 - Overall Views whether the Concept of AC Is an Appropriate Response to User Demands
 - The Objective and Focus of AC
 - Developing Requirements and Guidance to Implement AC
 - Other Matters for Future Consideration, Including Alternative Approaches

II. Overall Views Whether the Concept of AC Is an Appropriate Response to User Demands (Question 3 of the ITC)

2. The three roundtables and many responses received on the ITC all acknowledge a need for the auditor to provide more information to enhance the value of the auditor's report, though diverse views continue to exist as to the objective, nature and extent of AC that can and should be provided. Appendix 1 illustrates respondents' overall views as to whether the concept of AC is an appropriate response to user demands.
3. While the ITC acknowledged that calls for AC initially came from institutional investors, it is increasingly clear that other types of investors, as well as regulators and oversight bodies, would find value in the auditor providing additional information in the auditor's report. In addition, a majority of accounting firms¹ that responded to the ITC indicated support for the broad concept of AC and offered suggestions on how such a concept should best be operationalized. For example:
 - All but one investor respondent² supported the concept as explained in the ITC, although diverse views exist in terms of what AC should cover and the usefulness of the examples in the ITC. This respondent was concerned that more information in the auditor's report opens up the possibility of different interpretation – in their view, tailored information does not support comparison across entities in a standardized and formulaic fashion, and investors, funders and regulators can routinely obtain additional information directly from management.³
 - It was explicitly noted during the roundtables and other outreach that the IAASB's work to enhance auditor reporting provides a unique opportunity to reinvigorate the public's trust and confidence in the independent auditor and increase the relevance of the audit. Investors rely on a vigorous external audit to strengthen the veracity and quality of financial reporting. Regulatory and investor respondents⁴ were of the view that AC as contemplated in the ITC

¹ *Accounting firms*: BDO, CCW-UK, CHI, DTT, EYG, GTI, KI, KPMG, MAZARS, PKF(UK), PWC, RSM, SNG, WK

² *Investors and analysts*: GCSPS

³ BT and NZAuASB also made similar comments to explain their lack of support for AC.

⁴ *Investors and analysts*: CalPERS, EUMEDION, HEOS, ICGN, IMA, S&P, SLI; *Regulators and oversight authorities*: CPAB, EBA, IOSCO, JSE, MAOB

would provide users with a good sense of how auditors fulfilled their professional responsibilities and would add value to the pass/fail opinion. These respondents seemed to be viewing AC as a means for understanding the quality of the underlying audit performed, recognizing that highlighting what the auditor considered to be key matters in planning and performing the audit provides a view on the most important aspects of the financial statements, due to the risk-based nature of an ISA audit. While the ITC noted the demands from investors to assist them in navigating increasingly complex financial statements, responses to the ITC indicate the value and focus of AC is likely more useful as a response to demands for auditors to provide greater transparency about audits performed in light of the role of the audit in enhancing the credibility of financial reporting.

4. A majority of respondents⁵ supported the concept of AC, echoing the benefits explained in the ITC. A few public sector respondents⁶ noted the similarities between AC and supplemental reporting by many Supreme Audit Institutions (SAI) to governments.
5. However, many respondents raised concerns about the potential implications of AC if not mitigated by the IAASB through appropriate standard-setting activities and language in the auditor's report. The primary concern of the majority of respondents across all stakeholder groups and geographic regions about AC as described in the ITC was that it may blur the roles and responsibilities of management, the auditor and those charged with governance (TCWG), especially if the auditor is seen as providing original information about the entity. Many respondents⁷ explicitly cited the need to retain the auditor's independent, objective assurance role and responsibilities.

⁵ *Investors and analysts:* ABI, BR, CalPERS, EUMEDION, HEOS, ICGN, IMA, JMahoney, NAPF, S&P, SAAJ, SLI; *TCWG:* ACAG, GSaucier, IBGC, IIA, KC, OECD; *Regulators and oversight authorities:* AFRC, BCBS, CPAB, CSIPPC, CSRC, DFSA, EAIG, EBA, HKFRC, IAIS, ICAC, IOSCO, IRBA, JSE, MAOB; *NSS:* CICPA, CNCC-CSOEC, HKICPA, IDW, JICPA, MAASB, NBA, UKFRC; *Accounting firms:* BDO, CCW-UK, CHI, DTT, EYG, GTI, KI, KPMG, MAZARS, PKF(UK), PWC, RSM, SNG, WK; *Public sector organizations:* ACAG, CNAO, GAO, NAOS, RD; *Member bodies and other professional organizations:* ACCA, ASSIREVI, BICA, CAI, CAQ, CNDCEC, DNR, EFAA, FACPCE, FAR, FEE, FSR, IBR-IRE, ICAEW, ICAN, ICAP, ICAS, ICASL, ICPAI, ICPAS, IMCP, KICPA, OROC, SMPC, TK, WPK; *Academics:* AAA, BCEM, HC, JCarcello, UofW, VMassarygina; *Individuals and Others:* ASaleem, CBarnard, DJuvenalMRejon, Finguru, IChandra, MAhmadi, RMahadevan, ROverweg, RRodil

⁶ *Public sector organizations:* ACAG, AGA, AGNZ, CIPFA, NAOS

⁷ *TCWG:* IIA; *Regulators and oversight authorities:* CSIPPC, WB; *NSS:* CAASB, JICPA, NZAuASB; *Accounting firms:* CB, CH-AU/NZ, MNP, PKF, PKF(UK), PWC; *Public sector organizations:* AGC; *Preparers:* BE, CBI, PAIB, USCC; *Member bodies and other professional organizations:* ICPAK, ICPAS, MICPA, NASBA, NYSSCPA, TK, ZICA; *Academics:* BMednick, RMoroney; *Individuals and others:* RRodil

6. Many respondents⁸ did not support the concept of AC, including some NSS, TCWG representatives and member bodies and other professional organizations. These respondents were of the view that AC:⁹
- May detract from the auditor’s clear pass/fail opinion or call it into question;¹⁰
 - Should not undermine the objective of the audit or users’ ability to understand that the opinion is on the financial statements as a whole;¹¹
 - May be misinterpreted by users as “piecemeal” opinions or “soft qualifications”;¹²
 - May be used by auditors inappropriately to avoid modifying an opinion or as a substitute for disclosures that management should make;¹³ and
 - Could increase the expectations gap.¹⁴
7. On the whole, no preparers supported the concept of AC as described in the ITC, because they were of the view that the auditor is not equipped to make business judgments about, or “tell the story” of, the entity, and it is the role of management to highlight matters that are important to users,

⁸ *Investors and analysts:* GCSPS; *TCWG:* AICD, HICG; *Regulators and oversight authorities:* CSA CAC, WB; *NSS:* ASB, CAASB, NZAuASB; *Accounting firms:* BT, CB, CH-AU/NZ, GC, MNP, PKF, PP, TL, WBLI; *Public sector organizations:* AGA, AGC, AGM, AGNZ, AGQ, BC, CIPFA; *Preparers:* BE, BP, CBI, CNRL, Gof100-A, Gof100-UK, QCA, USCC, VNO-NCW; *Member bodies and other professional organizations:* CalCPA, CGAC, CIMA, CPAA, CPRB/SCAG, ICAA, ICAI, ICPAK, ICPAU, IE, KWT, MIA, MICPA, NASBA, NYSSCPA, ZICA; *Academics:* BMednick, KJamalSSunder, PGillis; *Individuals and others:* JHodgeZMurray, JKelly, KPastakia, SGiang

⁹ The footnotes to the bullets that follow also include reference to respondents who supported the concept of AC, but raised these areas as concerns the IAASB would need to take into account in developing an appropriate way forward for AC, including its objective. These respondents also cited a need to develop guidance to ensure effective implementation, as well as a need to further consider whether additional language in the introductory paragraph of the AC section is necessary to place it into appropriate context and explain why AC is being provided.

¹⁰ *Regulators and oversight authorities:* CSA CAC, DFSA, IOSCO; *NSS:* CAASB, CICPA, FAP, JICPA; *Accounting firms:* GTI, MNP, PP, SRA, TL; *Public sector organizations:* ACAG, AGC, AGQ; *Preparers:* BE, USCC; *Member bodies and other professional organizations:* DNR, FACPCE, FEE, IBR-IRE, ICAEW, ICPAS, NYSSCPA, SMPC, TK; *Academics:* UofW; *Individuals and others:* JHodgeZMurray

¹¹ *Investors and analysts:* BR; *Regulators and oversight authorities:* BCBS, DFSA, EAIG, EBA, HKFRC, IRBA; *NSS:* AUASB, CICPA, JICPA; *Accounting firms:* CCW-UK, DTT, KPMG; *Preparers:* CNRL, VNO-NCW; *Member bodies and other professional organizations:* IE; *Academics:* RMoroney; *Individuals and others:* KPastakia, RRodil

¹² *Regulators and oversight authorities:* CSA CAC, IRBA; *NSS:* CAASB, HKICPA, NBA; *Accounting firms:* BT, MAZARS, RSM, TL; *Public sector organizations:* AGA, AGQ; *Preparers:* BE, CNRL, Gof100-A; *Member bodies and other professional organizations:* CalCPA, ICAEW, ICAI, ICPAK, KICPA, NYSSCPA, SMPC; *Academics:* UofW; *Individuals and others:* KPastakia

¹³ *Investors and analysts:* CalPERS; *Regulators and oversight authorities:* BCBS, CSA CAC, DFSA, EBA, IAIS, IOSCO; *NSS:* JICPA, UKFRC; *Accounting firms:* BDO, BT, PP, PWC; *Public sector organizations:* ACAG, AGNZ; *Preparers:* USCC; *Member bodies and other professional organizations:* BICA, CAI, CIMA, MICPA, NYSSCPA, SMPC, WPK; *Academics:* VMassarygina; *Individuals and others:* JKelly

¹⁴ *Regulators and oversight authorities:* CSA CAC; *NSS:* CAASB, HKICPA, JICPA, NZAuASB; *Accounting firms:* CH-AU/NZ, MNP, PP; *Preparers:* Gof100-A, USCC; *Member bodies and other professional organizations:* CGAC, CPAA, ICAI, ICPAK, TK;

a point supported by other respondents.¹⁵ One preparer,¹⁶ however, was of the view that in order to respond to calls for auditors to enhance the value of their reports, auditors could include more in the Auditor's Responsibility section of the auditor's report, highlighting the significant risks identified in the individual audit. Respondents¹⁷ who supported AC, in particular regulators, offered a contrasting view, suggesting that management's disclosures would be enhanced by the dialogue that would result between management, TCWG and the auditor as a result of the auditor being required to include AC and possibly making reference to specific disclosures, a point also made by the European Commission (EC) representative at the Brussels roundtable.

8. Regional and smaller accounting firms who did not support AC¹⁸ were primarily concerned that the costs of including AC outweighed the benefits to their clients. These respondents reiterated the IAASB's acknowledgment in the ITC that users of small- and medium-sized entities' (SME) and not-for-profits' financial statements may obtain information directly from management. A few firm respondents¹⁹ explicitly noted that implementing the concept of AC and possibly other suggested improvements may make audits inaccessible for some entities due to their cost, leading them to instead opt for a review engagement if not otherwise required to have an audit.
9. From a geographic perspective, there appeared to be a concentrated lack of support from Canadian respondents of all stakeholder groups, with the exception of one respondent.²⁰ The ITC highlighted that the global financial crisis has spurred users, in particular institutional investors and financial analysts, to want to know more about individual audits and to gain further insights into the audited entity and its financial statements. It was suggested by a few respondents²¹ that Canada had not been exposed to the effects of the global financial crisis to the extent that other countries or regions had been and that Canadian stakeholders were not calling for an expanded auditor's report, having recently acclimated to the adoption of ISAs. Other geographic influences are discussed in more detail later in this paper.

Matters for IAASB Consideration

1. Based on the responses and feedback received, does the IAASB agree the TF should continue to pursue the concept of AC in some form, by which the auditor would provide more information in the auditor's report?

¹⁵ TCWG: AICD; NSS: HKICPA, NZAuASB; Accounting firms: BT, CB, CH-AU/NZ, TL; Public sector organizations: AGNZ, AGQ; Preparers: CBI, Gof100-A; Member bodies and other professional organizations: CIMA, CPRB/SCAG, ICPAK, KWT, NASBA, NYSSCPA, PAIB; Individuals and others: JKelly

¹⁶ Preparers: BE

¹⁷ Investors and analysts: EUMEDION, HEOS, NAPF; Regulators and oversight authorities: CPAB, EAIG, EBA, IAIS, IOSCO, JSE; NSS: AUASB, UKFRC; Accounting firms: EYG, KPMG; Member bodies and other professional organizations: ACCA, CAQ, EFAA, ICAEW, SMPC

¹⁸ Accounting firms: CB, CH-AU/NZ, GC, MNP, PP, TL, WBLI, WK

¹⁹ Accounting firms: GC, TL, WBLI

²⁰ Regulators and oversight authorities: CPAB

²¹ Regulators and oversight authorities: CSA CAC; NSS: CAASB

The Objective and Focus of AC

10. The ITC included the following as a possible objective of AC:

The objective of AC is to highlight matters that are, in the auditor's judgment, likely to be most important to users' understanding of the audited financial statements or the audit.

General Concerns Relating to the Objective of AC

11. While respondents generally acknowledged the need for the IAASB to respond to calls for change in auditor reporting, fundamental questions have been raised across all stakeholder groups about the appropriateness of the auditor providing additional information in the auditor's report, particularly about the financial statements and the entity. A majority of respondents across all stakeholder groups were concerned about the auditor providing "original information" about the entity and the financial statements in AC, consistent with the IAASB's position in the ITC that it is necessary to preserve the separate roles of the auditor, management and TCWG. Many respondents²² explicitly noted that TCWG had a significant role to play in improving financial reporting, through a strengthened oversight role as well as enhanced reporting responsibilities. This was particularly noted in responses from the European region, where the UKFRC has put in place proposals with respect to company stewardship, and in the context of the EC's proposals on long-form reporting to audit committees of PIEs. A few respondents²³ also felt the auditor may be better focused on enhancing discussion with TCWG as they would be more likely to be "audit literate", rather than reporting externally, and referenced the EC's recent proposals to enhance reporting to TCWG as a possible basis for strengthening ISA 260²⁴ in relation to discussion of relevant matters about the audit, including the auditor's views on management's judgments.
12. There are also differing views as to what users' responsibilities are as consumers of the financial statements. A few respondents²⁵ cited the underlying premise in the accounting and auditing standards that users are expected to be knowledgeable people who bear personal responsibility to be financially literate about both financial reporting frameworks and the nature and scope of an audit. However, other respondents²⁶ felt that users were actually unlikely to have a minimum competence in the field of auditing to interpret meaningfully and accurately any additional information in the auditor's report describing the auditor's approach to assessed risks. These and

²² *Investors and analysts:* ABI, CalPERS, HEOS; *TCWG:* GSaucier; *Regulators and oversight authorities:* CSA CAC, EBA, HKFRC, IRBA, WB; *NSS:* IDW, NBA, NZAuASB, UKFRC; *Accounting firms:* BT, CCW-UK, CHI, DTT, PKF(UK), PWC, RSM; *Public sector organizations:* AGQ, CIPFA, NAOS; *Preparers:* BE, BP, CBI, Gof100-UK, QCA; *Member bodies and other professional organizations:* ACCA, ASSIREVI, CAI, CalCPA, CPAA, FACPCE, FEE, FSR, ICAEW, ICPAS, MICPA, NYSSCPA, TK; *Academics:* UofW; *Individuals and others:* RRodil

²³ *Regulators and oversight authorities:* WB; *NSS:* CAASB; *Accounting firms:* BT, MNP; *Preparers:* BE; *Member bodies and other professional organizations:* FEE, KWT; *Academics:* BMednick

²⁴ ISA 260, *Communication with Those Charged with Governance*

²⁵ *TCWG:* IIA; *Regulators and oversight authorities:* IBGC; *NSS:* AUASB; *Accounting firms:* MNP, TL

²⁶ *Regulators and oversight authorities:* WB; *NSS:* MAASB; *Accounting firms:* GC, MNP, TL; *Member bodies and other professional organizations:* IBR-IRE, ICAI, NYSSPA; *Individuals and others:* JKelly, KPastakia, RRodil

many other respondents²⁷ highlighted the need for separate educational efforts either in lieu of, or as a supplement to, changes to the auditor's report, and explicitly noted that post-implementation efforts would be needed to ensure that all stakeholders understand the objectives and purpose of the changes so that the expectations gap was not inadvertently widened. It was suggested that NSS and professional accountancy bodies, as well as regulators and academics, had a role to play in this regard.

13. Many respondents²⁸ also highlighted the challenges of general purpose financial reporting (which is designed to meet the needs of a broad set of users rather than the demands of any particular group) with the view that no one other than users themselves can determine which areas are "most important". Users, which was noted to be a wider group than investors, have identified a wide range of differences in information needs, driven largely by the region, regulatory environment and industry in which the entities they are interested in operate.

Need for Further Refinement of the Objective of AC

14. A key question therefore will be whether it is appropriate and possible for AC to achieve the dual objective as explained in the ITC, or whether the IAASB should explore alternatives to meet the diverse needs of these stakeholders, bearing in mind the impediments that were identified by the IAASB in the ITC and confirmed by respondents. Appendix 2 provides an illustration of the diversity of views on key matters relating to AC, in particular views from respondents as to whether the focus should be on the financial statements or the audit, based on Staff's analysis of all the questions in the ITC. Previous TF and IAASB discussions indicated the likely overlap between areas of significant management judgment (resulting in disclosures in the financial statements) and "matters of audit significance," in particular matters of significant auditor judgment, due to the risk-based nature of an ISA audit. This overlap was seen in the responses to the ITC, as respondents were not explicitly asked, and did not necessarily comment specifically on, whether the objective of AC should focus on matters in the financial statements or matters about the audit (or both).
15. There continues to be diversity of views in terms of what AC is intended to achieve, which is based in part on differing needs of different types of investors and other users, the availability of this information via other means, and the financial reporting framework applied by the entity. There is also a widely acknowledged need for any proposals relating to AC to preserve the roles of management, TCWG and the auditor.

²⁷ TCWG: AICD; *Regulators and oversight authorities*: IOSCO, MAOB, WB; NSS: AUASB, CICPA, HKICPA, NZAuASB; *Accounting firms*: GTI, KMPG, MNP, PP, PWC, SRA; *Public sector organizations*: AGNZ; *Preparers*: BP, Gof100-A, USCC, VNO-NCW; *Member bodies and other professional organizations*: BICA, CalCPA, CPAA, EFAA, ICAI, ICPAS, NASBA, ZICA

²⁸ TCWG: IIA, KC; NSS: CAASB, IDW, NZAuASB; *Accounting firms*: CB, MNP, PKF, PKF(UK); *Public sector organizations*: ACAG; *Member bodies and other professional organizations*: ACCA, ASSIREVI, CGAC, FEE, ICAEW, ICAA, ICAI, ICPAS, MICPA, NYSSCPA; *Individuals and others*: JKelly

16. Paragraph 45 of the ITC suggested that auditors could consider the following, at a minimum, in determining which matters to include in AC:
- Areas of significant management judgment (e.g., in relation to the entity’s accounting practices, including accounting policies, accounting estimates, and financial statement disclosures);
 - Significant or unusual transactions (e.g., significant related party transactions or restatements); and
 - Matters of audit significance, including areas of significant auditor judgment in conducting the audit, for example:
 - Difficult or contentious matters noted during the audit, or other audit matters that would typically be discussed with an engagement quality control reviewer or TCWG; and
17. Other issues of significant related to the audit scope or strategy Areas of potential focus in AC relating to matters disclosed in the financial statements (beyond those specifically mentioned as potential considerations in paragraph 45 of the ITC) included:
- An assessment of management’s critical accounting estimates and judgments, to focus on explaining the nature of the audit work done in order to provide users with a view of the level of risk associated with valuations or estimates.²⁹
 - Structure of the entity³⁰
 - Areas of significant leverage or exposure³¹
 - Emphasis on matters affecting cash flow statements³²
 - New or emerging accounting matters or policies³³
 - Loan loss provisioning and other matters of high estimation uncertainty, including critical accounting estimates³⁴
 - A specific assertion that accounts are prepared on a neutral basis³⁵

Respondent’s Views about the Auditor Providing More Information about Matters Disclosed in the Financial Statements

18. Many respondents,³⁶ including those who did not support the concept of AC, noted that the ISAs by design already allow for auditors to include more context in their reports when the auditor considers

²⁹ *Investors and analysts: CalPERS, JM; Regulators and oversight authorities: IAIS; Member bodies and other professional organizations: CAQ, ICAN*

³⁰ *TCWG: IIA; Accounting firms: EYG*

³¹ *TCWG: IIA*

³² *Investors and analysts: S&P, SAAJ*

³³ *TCWG: IIA; Accounting firms: EYG*

³⁴ *Regulators and oversight authorities: BCBS; Accounting firms: EYG*

³⁵ *Investors and analysts: HEOS, NAPF*

it necessary to do so, through the use of EOM and Other Matter (OM) paragraphs, so a new vehicle that would likely result in additional cost with questionable benefit is not needed. These respondents thought the IAASB should promote increased use of these paragraphs and education about what they were intended to achieve. One respondent³⁷ was of the view that it is unclear how the concept of AC differs from the current concepts of EOM and OM paragraphs.

19. Many respondents³⁸ also either believe it is not the auditor's role to provide such a roadmap or that the objective of this approach would be better achieved by accounting standard setters working to ensure the disclosures prepared in accordance with a financial reporting framework are addressing user needs, in part by reducing the complexity of such disclosures. It was noted at the New York roundtable that nothing in the accounting standards prevents management from providing such a roadmap, although this is not currently done in practice. Related to this point, many respondents³⁹ were of the view that, in addition to expanding the auditor's report, a more holistic approach to change is necessary to reduce financial reporting complexity and disclosure overload; better explain the concept of "estimation uncertainty," including that more imprecise information may result; and ensure that financial reporting results in a focus on the most significant matters of interest to users. It was suggested that accounting standard setters, regulators and oversight authorities had roles to play in this regard.
20. As noted in paragraph 7, a number of respondents were of the view that, if specific disclosures in the financial statements were referred to in AC, a residual effect would be enhanced focus on these disclosures by management and TCWG. This "healthy tension," which was particularly noted in response to the IAASB's May 2011 consultation paper on auditor reporting, is seen to be a benefit to improving financial reporting overall. One respondent⁴⁰ noted that a requirement for the auditor to publicly report on matters of interest to investors and other users may provide the auditor with a lever to incentivize directors themselves to provide more focused and insightful corporate reporting and provide pointers to matters on which investors would wish to engage with TCWG or other directors.

³⁶ *TCWG: AICD, HICG; Regulators and oversight authorities: CSRC; Accounting firms: CH-AU/NZ, GC, PKF, PKF(UK); Public sector organizations: AGM, AGNZ, AGQ, BC, CIPFA; Preparers: BE, Gof100-UK, USCC; Member bodies and other professional organizations: ASSIREVI, CalCPA, CGAC, ICPAK, ICPAU, MICPA, NYSSCPA, ZICA*

³⁷ *Regulators and oversight authorities: IOSCO*

³⁸ *Regulators and oversight authorities: IOSCO, IRBA, WB; NSS: IDW, NBA, UKFRC; Accounting firms: CH-AU/NZ, MAZARS, MNP, PP, SRA, TL, WKC; Public sector organizations: ACAG, AGA, AGC, AGNZ, CIPFA; Preparers: BE, BP, PAIB, USCC, VNO-NCW; Member bodies and other professional organizations: CalCPA, CPAA, FAR, FEE, ICAI, KWT, NYSSCPA, WPK; Academics: JCarcello; Individuals and others: JKelly*

³⁹ *Investors and analysts: CalPERS, ICGN, IMA; TCWG: GSaucier; Regulators and oversight authorities: AFRC, EAIG, IOSCO, IRBA, WB; NSS: ASB, CAASB, CICPA, JICPA, MAASB, NBA, NZAuASB, UKFRC; Accounting firms: BDO, BT, CB, CCW, CH-A/NZ, CHI, DTT, EYG, GTI, KPMG, MNP, PKF, PKF (UK), PWC, RSM, SNG, SRA, WKC; Public sector organizations: ACAG, AGA, AGC, AGNZ, CIPFA; Preparers: BE, BP, Gof100-A, Gof100-UK, QCA, USCC, VNO-NCW; Member bodies and other professional organizations: ACCA, ASSIREVI, CAI, CAQ, CNDEC, CPAA, DNR, EFAA, FEE, FSR, IBR-IRE, ICAA, ICAEW, ICAS, ICPAS, ICPAU, IDW, IE, KWT, MICPA, NYSSCPA, WPK; Academics: PGillis; Individuals and others: CBarnard, KPastakia*

⁴⁰ *NSS: UKFRC*

21. However, many respondents⁴¹ were of the view that AC should not describe auditor impressions or perspectives on subjective financial reporting matters assessed during the audit (e.g., the quality of the entity's accounting policies or whether the entity's estimates or judgments are conservative or aggressive). This is because, in their view:
- Such information could compete with management's disclosures and could be a shift from the auditor's attestation role.
 - Financial reporting frameworks are not geared to being able to objectively judge shades of gray or a scale of the extent to which the financial statements are fairly presented.
 - These insights are already discussed with TCWG who, by nature of their role, have the appropriate context and the benefit of the two-way communication necessary to consider this information.

Respondents' Views about an Audit Context for Matters Disclosed in the Financial Statements

22. The ITC recognized that the use of a "roadmap" would be enhanced if the auditor were to provide additional context to the matters highlighted, such as explaining why the auditor considered the matter to be important from an audit perspective. As noted in paragraph 3, many respondents,⁴² in particular investors and regulators, emphasized that more information about the auditor's judgments and the audit using the vehicle of AC would be appropriate. Many of these respondents suggested that auditors could disclose significant matters considered in conducting the audit, and how the auditor was satisfied that the matters had been appropriately addressed in order to form an opinion on the financial statements as a whole. A number of these respondents' comments on the usefulness of the illustrative examples in the ITC reiterated this point, as they noted that the examples in illustrative reports (some of which were intended to call attention to matters of significant management judgment or significant unusual transactions disclosed in the financial statements) should also provide more of an indication of why the auditor thought the matters were important in the context of the audit.
23. It was noted that AC used in this way could provide vital insights into the quality of the audit and enable investors to assess the value they are getting from an audit, as well as serve as a helpful basis for dialogue between investors and an entity's management and TCWG. This approach was also supported by a preparer⁴³ who noted that if the goal of the IAASB's suggested improvements is to narrow the information gap, then the focus should be on the work performed by the auditor, similar to a point echoed at the New York roundtable – that preparers and TCWG are experts about

⁴¹ *Investors and analysts:* ABI; *TCWG:* IIA; *Regulators and oversight authorities:* IRBA; *NSS:* AUASB, CAASB, JICPA, NZAuASB; *Accounting firms:* BDO, EYG, KPMG, MAZARS, MNP, PKF, PP, PWC, SNG; *Public sector organizations:* NAOS; *Preparers:* USCC; *Member bodies and other professional organizations:* ASSIREVI, BICA, CAQ, CIMA, ICAA, ICAI, ICPAS, MICPA, IMCP, KICPA, NYSSCPA; *Individuals and others:* JKelly, KPastakia, RRodil

⁴² *Investors and analysts:* CalPERS, EUMEDION, HEOS, ICGN, IMA, S&P, SLI; *Regulators and oversight authorities:* CPAB, EBA, IOSCO, JSE, MAOB, OECD; *NSS:* AUASB, UKFRC; *Accounting firms:* CHI, MAZARS; *Member bodies and other professional organizations:* CAI, KWT, NASBA, WPK; *Academics:* HC

⁴³ *Preparers:* BE

the entity, as the auditor is the expert about the audit and may be able to provide additional information on that basis.

Respondents' Views about the Auditor Highlighting Other Matters of Audit Significance

24. There is less explicit support for AC to focus on “matters of audit significance” that are not directly related to matters disclosed in the financial statements, for example, information related to the overall planning and scoping of the audit. A rationale raised by one respondent⁴⁴ for having the auditor provide such information was that it could help reduce the misunderstanding that some users have about the scope of an audit, quantifying the work of the auditor and highlighting that not all transactions and locations were examined. Two respondents⁴⁵ suggested that the auditor should always *consider* including in AC information on the important aspects of the audit, such as materiality and the scope of the audit, and important findings on the financial statements, recognizing it is vital to allow flexibility for the auditor to determine which key audit matters are most relevant to users' understanding of the audit.
25. A number of respondents believed auditors could provide more information about the audit beyond what is disclosed in the financial statements in the following areas:
- Scope, strategy and key planning judgments, including audit process and methodology, for example:
 - Materiality (as discussed further below)
 - Extent to which the auditor used third-party experts⁴⁶
 - Group audits / use of other auditors (addressed through Question 13 of the ITC – to be further analyzed by the TF for discussion at the February 2013 IAASB meeting)
 - Important management representations⁴⁷
 - Key audit findings
 - Significant audit adjustments and the auditor's evaluation of unadjusted differences⁴⁸
 - Context on significant accounting policies that reflect a choice among alternatives and therefore are in compliance with the financial reporting framework but, in the auditor's view, need further disclosure to increase users' understanding of their effects on the financial statements⁴⁹

⁴⁴ *Preparers: Gof100-UK*

⁴⁵ *Investors and analysts: EUMEDION, ICGN*

⁴⁶ *TCWG: ACGA; Regulators and oversight authorities: EAIG; Preparers: Gof100-A*

⁴⁷ *Regulators and oversight authorities: BCBS*

⁴⁸ *NSS: CICPA; Individuals and others: MAhmedi*

⁴⁹ *Investors and analysts: S&P*

- The auditor's approach to the entity's control environment and deficiencies identified by the auditor⁵⁰
26. A few respondents⁵¹ believed AC should include an explanation of the auditor's approach to materiality, specific to the audit in question, with quantification of the thresholds used by the auditor. Of these respondents, preparers suggested materiality could be discussed in AC because they were of the view that AC should be limited to audit matters not disclosed in the financial statements. A discussion of materiality was favored by a number of investor respondents based in the UK, as the UKFRC developed an illustrative example relating to materiality for use in their outreach.
27. However, other respondents⁵² explicitly noted they did not support disclosing materiality in the auditor's report. One investor respondent⁵³ provided specific rationale as to why, noting that auditor materiality thresholds involve a number of quantitative and qualitative considerations, including assessment of individual financial statement line items, disclosures in the context of the overall financial statements, and the level to which audit differences are a result of factual errors versus judgmental considerations involving estimates or assumptions or directional input factors.
28. In addition to the specific views on materiality, many respondents,⁵⁴ including some who expressed strong views, did not believe that AC should be used to describe "purely audit" matters (e.g., related to scope, strategy, procedures or results), because in their view:
- Matters linked to the audit strategy are likely not relevant to investors.
 - Users will not possess the appropriate context necessary to consider this information in the same way as TCWG, because they will not have the benefit of the robust dialogue that occurs between management, TCWG and the auditor. Including Auditor Commentary without the ability to engage in a robust two-way communication will not enhance an investor's overall understanding of the financial statements; in fact, there is a real danger that the additional commentary may be misunderstood and taken out of context by users. To mitigate this, a few respondents suggested the auditor should participate in the annual meeting of stakeholders.⁵⁵

⁵⁰ *Investors and analysts: S&P; TCWG: IBGC; Regulators and oversight authorities: BCBS, NSS: CICPA; Accounting firms: SRA; Member bodies and other professional organizations: FEE; Individuals and others: ASaleem, ROverweg*

⁵¹ *Investors and analysts: HEOS, IMA, NAPF, SLI; TCWG: ACGA; Regulators and oversight authorities: EAIG; NSS: UKFRC; Accounting firms: BT; Preparers: BP, Gof100-A, Gof100-UK; Member bodies and other professional organizations: ICAS; Academics: BCEM; Individuals and others: ASaleem*

⁵² *Investors and analysts: BR; NSS: MAASB, NBA; Accounting firms: MAZARS, MNP; Member bodies and other professional organizations: MICPA; Academics: VMassarygina*

⁵³ *Investors and analysts: BR*

⁵⁴ *Investors and analysts: SAAJ; Regulators and oversight bodies: CSRC, EBA, IAIS, WB; NSS: CAASB, FAP, NZAuASB; Accounting firms: BDO, EYG, KPMG, MAZARS, MNP, PKF, PWC, SNG, SRA; Preparers: USCC; Member bodies and other professional organizations: ASSIREVI, BICA, CAQ, CPAA, EFAA, IMCP, MICPA, NYSSCPA, TK*

⁵⁵ *NSS: AUASB; Public sector organizations: NAOS; Preparers: Gof100-A, USCC; Member bodies and other professional organizations: IBR-IRE*

- Users are actually unlikely to have a minimum competence in the field of auditing to interpret meaningfully and accurately any additional information in the auditor’s report describing the auditor’s approach to assessed risks.
 - Public reporting of these matters undermines the role of TCWG and could result in less robust discussion with them and the auditor if there was an expectation that all matters discussed between auditors and TCWG could be subject to inclusion in AC.
 - These matters could be discussed in a report by TCWG; doing so would keep the auditor’s report to a reasonable length, as it would be unreasonable to expect that a written report could contain communications of sufficient factual details to enable users to make meaningful judgments as to such complex matters and to assess audit strategy, risks and other matters of audit scope.
 - While audit quality is likely to be enhanced by AC due to increased auditor focus on matters that may be reported, AC in and of itself cannot be used to gauge audit quality – there is an important role for firms’ quality control systems and the audit inspection process.
29. A number of respondents⁵⁶ specifically expressed a view that the example in the ITC relating to audit strategy was not useful – it was suggested that users may not understand why the auditor had included this information and it was unclear how investors would use this type of information in their decision making. In addition, the majority of respondents, including a number of investors and analysts, agreed that the auditor should not be required to include a detailed description of audit procedures in relation to individual matters included in AC, noting the following views:
- It will be difficult for auditors to summarize procedures in a succinct and non-technical way that would provide the user with an understanding of the full scope of those procedures, the significant judgments involved, and the quantitative and qualitative factors considered in reaching their conclusions in a particular area.
 - A brief summary of procedures would not fairly reflect the skill and knowledge demonstrated by the auditor in performing the audit, and may divert attention away from the auditor’s opinion on the financial statements as a whole.
 - Inclusion of audit procedures, in one investor’s view, does not provide meaningful information to financial statement users.

Respondents’ Views on Approaches to Moving Forward with AC

30. One respondent⁵⁷ suggested that, to respond to demands to move as quickly as possible, the IAASB could amend ISA 706⁵⁸ on a priority basis as an incremental change to lower the bar on reporting to “most important” from “fundamental” so that EOM and OM paragraphs would be used

⁵⁶ *Regulators and oversight bodies:* IAIS; NSS: CAASB, CNCC-CSEOC, CICPA, JICPA, UKFRC; *Accounting firms:* KPMG; *Public sector organizations:* AGC, AGQ; *Preparers:* QCA; *Member bodies and other professional organizations:* ASSIREVI, CGAC, CNDEC, FACPCE

⁵⁷ *Accounting firms:* GTI

⁵⁸ ISA 706, *Emphasis of Matter and Other Matters Paragraphs in the Independent Auditor’s Report*

more. However, two regulators⁵⁹ were unsure whether changing the terms would amount to a lower threshold for reporting.

31. To meet user demands while mitigating the possibility of the auditor providing original information about the entity or its financial statements, another suggestion made by respondents,⁶⁰ particularly the larger accounting firms, is for an expanded EOM approach to operationalize AC. A similar approach was discussed at the recent US Public Company Accounting Oversight Board (PCAOB) Standing Advisory Group (SAG) meeting.
32. Respondents who supported this approach were of the view that the primary focus of AC should be to highlight disclosures within the financial statements relating to matters that the auditor judges likely to be most important in the context of a user's understanding of the financial statements taken as a whole (for example, in relation to significant management judgments or significant financial reporting judgments).⁶¹ These respondents were of the view that the information in the auditor's report should provide a brief, factual and objective description of the matter, drawn from management's disclosure within the audited financial statements, and should refer the reader to where the matter has been disclosed in the financial statements. Two respondents⁶² suggested auditors should always draw attention to the note in the financial statements where the entity's critical accounting estimates are described, as users should always pay particular attention to this disclosure.
33. However, anticipating the feedback described in paragraph 22, a few respondents⁶³ believed, if this approach were to be pursued, it would also be necessary for the auditor to highlight the significance of these matters to the performance of the audit when it would be important to users. Further discussion of possible criteria that could be used under this approach is discussed in Section III, including the suggestion that AC could be rooted in the concept of significant risks.
34. An alternative approach, supported by a few respondents,⁶⁴ emphasized the view that AC should start from the basis of the auditor's approach to the audit and describe significant matters arising from the audit, including the auditor's risk assessment and response. One respondent⁶⁵ suggested the auditor could describe in AC:
 - The nature of each significant risk;

⁵⁹ *Regulators and oversight authorities:* IOSCO, WB

⁶⁰ *Investors and analysts:* BR; *TCWG:* ACAG, IIA; *Regulators and oversight authorities:* CSRC; NSS: HKICPA, NZAuASB; *Accounting firms:* BDO, DTT, EYG, KPMG, MNP, PWC, RSM; *Public sector organizations:* GAO; *Member bodies and other professional organizations:* ASSIREVI, CAQ, IMCP

⁶¹ PWC suggested that significant financial reporting judgments would be in areas where management had to exercise significant judgment in determining an appropriate accounting treatment or in dealing with significant management uncertainty. This could also include management's judgments in relation to the treatment and disclosure of significant or unusual transactions, and may be grounded in industry-specific matters or be unique to the industry.

⁶² *Accounting firms:* PP; *Public sector organizations:* GAO

⁶³ *Accounting firms:* CCW-UK, DTT, EYG, GTI, KPMG; *Member bodies and other professional organizations:* ACCA

⁶⁴ *Investors and analysts:* EUMEDION, HEOS, ICGN, S&P; *TCWG:* ACGA; NSS: IDW, UKFRC; *Preparers:* BE, Gof100-A; *Member bodies and other professional organizations:* FEE

⁶⁵ *Member bodies and other professional organizations:* FEE

- The audit approach undertaken in response to this significant risk; and
- The key findings from that audit work.

This respondent was of the view that a clear reference to the related disclosure in the financial statements should be provided, to help users to link the point raised by the auditor to the disclosures, but would not be intended as a navigational tool. It was noted that further consideration may need to be given as to whether there may be circumstances in which certain significant risks should not be disclosed externally.

35. Another respondent⁶⁶ noted the benefits of basing AC on the audit, in particular significant risks, as follows:

- Areas of significant management judgment, significant or unusual transactions, and significant auditor judgments will often have been identified as significant risks, and therefore the broad objective of the ITC for AC would be achieved in relation to reporting about the audit;
- These risks are already identified during the audit and therefore no additional audit effort is required to identify matters that would be addressed in AC;
- These risks relate to the audit, and therefore addressing them would focus AC on matters related to the audit that are disclosed in the financial statements.

Retaining EOM and OM Paragraphs

36. While a few respondents⁶⁷ explicitly supported the view in the ITC that the concepts of EOM and OM paragraphs could be subsumed into the broader concept of AC, many respondents⁶⁸ were of the view that EOM and OM paragraphs should be retained and presented separately from AC in the auditor's report. In these respondents' views, their use sends an appropriately strong signal to readers of the auditor's report that may be lost if such matters are simply included in AC among other matters that may be of less importance. It was also suggested that retaining EOM and OM paragraphs would be necessary if AC was not required for all entities. Regarding OM, two respondents⁶⁹ were of the view that the current OM model needed to be retained, both for factual matters regarding the audit that are required to be disclosed in the ISAs today (e.g., identification of a predecessor auditor) and to continue to give auditors a means of communicating very significant matters affecting the audit. These respondents did not believe that including such matters in AC would be useful.

37. Given the support noted above for retaining the concept of OM paragraphs, an alternative to requiring AC for matters of audit scope or strategy could be to provide additional guidance in ISA

⁶⁶ NSS: IDW

⁶⁷ *Investors and analysts:* EUMEDION, ICGN; *Regulators and oversight authorities:* IAIS; NSS: AUASB, CICPA, JICPA, NZAuASB; *Member bodies and other professional organizations:* DNR, FACPCE

⁶⁸ *Regulators and oversight authorities:* IOSCO, IRBA; NSS: UKFRC; *Accounting firms:* CH-AU/NZ, MAZARS, PKF(UK), SRA; *Public sector organizations:* ACAG, AGA, AGM, AGQ, BC, CIPFA; *Member bodies and other professional organizations:* ACCA, EFAA, FAR, FEE, ICAA, ICAEW, ICAI, KWT, SMPC

⁶⁹ *Accounting firms:* KPMG, PWC

706 to encourage greater use of OM paragraphs in certain circumstances. Finally, as noted above, there may be scope for strengthening material within ISA 260, for example in relation to materiality, corrected misstatements, and the auditor's work in relation to the entity's control environment, to ensure this two-way communication is improved, either in addition to, or as a substitute for, AC on these matters.

Matters for IAASB Consideration

2. Does the IAASB have views as to how the objective of AC could be further refined and whether a different title than AC would be appropriate? In particular:
 - (a) Should the TF continue to explore how auditors could draw attention to key matters in the financial statements? If so, is there a need for auditors to provide additional context about the audit (e.g., by requiring the auditor to explain why the matter is important from an audit perspective) rather than simply referring to the relevant disclosure in the financial statements? If this could be done, might this also achieve the objective of providing more information about the audit?
 - (b) In light of the mixed support for including AC relating to matters of audit scope or strategy, what are the IAASB's suggestions about a way forward? For example, should the TF conduct further outreach to determine whether other illustrative examples may be useful to investors?
 - (c) How and when should the TF obtain feedback and reaction from investors, in particular to a revised proposed objective of AC and any criteria that the IAASB may develop, as well as a revised illustrative auditor's report with new examples of AC?
3. What are the IAASB's views about possibly retaining the concepts of EOM and OM paragraphs separate from AC?

III. Developing Requirements and Guidance to Implement AC

Support for AC Based on Professional Judgment with Appropriate Guidance (Question 4 of the ITC)

38. The majority of respondents across all stakeholder groups, including all investors who supported the concept of AC, were of the view that matters to be addressed in AC should be left to the judgment of the auditor, with guidance in the standards to inform the auditor's judgment, for the reasons explained in the ITC, in particular that:
 - Too much prescription and standardization will diminish the effectiveness of AC – only by being judgment-based can it bridge the information gap and add value to the auditor's report.
 - Prescription without allowing for auditor judgment risked AC being incomplete, in particular if an auditor did not discuss a significant matter because it was not expressly required.

But respondents also acknowledged there was a need for sufficient guidance to ensure that the auditor's decision-making process is robust and diversity in judgments is limited.

39. A few respondents⁷⁰ were of the view that more specific criteria, potentially in the form of detailed requirements, was needed to ensure auditors and management were clear on what is to be addressed in AC and to promote consistency in reporting. The IAASB was also encouraged to clarify in the auditor's report for whom AC was intended, in particular in relation to whom the auditor's report is addressed (e.g., existing stakeholders or a broader group of users), to determine what criteria was necessary.

Support for Significant Risks as the Starting Point for AC

40. It was noted that an expanded EOM approach (as described in paragraphs 31–32) would require an effective framework to appropriately guide the auditor's assessment of what matters should be emphasized and the form and content of such paragraphs. For this reason, respondents who supported this approach suggested that a two-tiered approach may be necessary: first, the auditor would consider matters similar to paragraph 45 in the ITC, which were developed based on factors the auditor considers in defining significant risks in the individual audit as well as matters that are typically discussed with TCWG in accordance with ISA 260.⁷¹ The auditor would then consider those matters that were the subject of significant engagement with TCWG and/or considered the most significant or challenging from an audit perspective. One respondent⁷² noted that, in order for such a framework to be implemented, the IAASB would need to emphasize the importance of the auditor considering the complexity and pervasiveness of matters that may be included in AC, whether these matters were communicated to TCWG, and the level of audit effort related to the matter, including the extent to which the matter required the involvement of the engagement quality control reviewer and others within the firm.
41. Many respondents⁷³ believed AC generally should be rooted in the concept of significant risks and other matters communicated to TCWG, and supported the matters described in paragraph 45 of the ITC. One respondent⁷⁴ who supported AC focusing on matters that are most important to users' understanding of the audit recognized that a byproduct of doing so is that such an approach helps users understand the audited financial statements. A few respondents were of the view that, within

⁷⁰ *Investors and analysts:* GCSPPS; *TCWG:* IIA; *Regulators and oversight authorities:* CSA CAC, FAP; *NSS:* CAASB, CICPA; *Accounting firms:* CB, TL; *Public sector organizations:* AGC; *Preparers:* VNO-NCW; *Member bodies and other professional organizations:* BICA, CNDEC, ICAN, NFCPAAROC; *Academics:* AAA

⁷¹ At its recent SAG meeting, the PCAOB explored whether their Auditing Standard No. 16, *Communications with Audit Committees*, could serve as the basis for enhancements to the auditor's report through required emphasis paragraphs related to the financial statements.

⁷² *Accounting firms:* KPMG

⁷³ *Investors and analysts:* CalPERS, IMA; *TCWG:* ACGA, GSaucier; *Regulators and oversight authorities:* BCBS, CPAB, EAIG; *NSS:* AUASB, CAASB, CICPA, HKICPA, IDW, JICPA, UKFRC; *Accounting firms:* BDO, BT, DTT, EYG, GTI, KPMG, MAZARS, PKF(UK), SRA; *Public sector organizations:* ACAG, CIPFA, NAOS; *Preparers:* BE, PAIB; *Member bodies and other professional organizations:* ACCA, ASSIREVI, CAQ, DNR, EFAA, FAR, FEE, FSR, ICAEW, KWT, SMPC, WPK; *Academics:* BCEM

⁷⁴ *NSS:* IDW

AC a description of the overall audit approach in relation to identified risks⁷⁵ would be meaningful to investors.

Areas where Guidance Is Likely Needed to Support the Auditor's Decision-Making

42. It will likely be necessary for the IAASB to develop guidance for auditors to ensure that the concerns expressed in paragraph 6 in relation to how AC could be operationalized, including how it is described in the auditor's report. Specifically, it was also suggested by two NSS⁷⁶ that guidance would be needed for auditors on how to:
- Determine user needs;
 - Determine what is significant, especially in the context of the FS taken as a whole;
 - Consider the potential for misinterpretation;
 - Determine the accuracy and completeness of AC information;
 - Determine consistency of AC with other information provided by management, avoiding duplication of, or contradiction with, information available elsewhere;
 - Determine the extent of information to be provided in AC (e.g., the level of detail, key points only or exceptions);
 - Deal with commercial sensitivities of information;
 - Avoid the risk of implying the auditor is predicting future events or conditions;
 - Avoid the risk of implying the auditor is providing some form of guarantee or additional assurance;
 - Deal with legal considerations, especially matters relating to legal professional privilege; and
 - Ensure completeness and accuracy of plain English wording and use of terminology.
43. Mixed views were expressed on the need for the IAASB to clarify its expectations as to the number of matters that would be addressed in AC. The following points were raised in this regard:
- Smaller entities may only have one key matter, while 10 matters for any entity could be too many.⁷⁷
 - A few respondents⁷⁸ agreed it would be rare for the auditor to determine that there are no matters that would warrant inclusion in AC, and that the auditor should be required to always say something.

⁷⁵ *Regulators and oversight authorities:* IOSCO; *NSS:* IDW; *Accounting firms:* SRA; *Member bodies and other professional organizations:* DNR, FEE, FSR, ICPAS, OROC

⁷⁶ *NSS:* AUASB, NZAuASB

⁷⁷ *NSS:* JICPA

⁷⁸ *Investors and analysts:* IMA; *Member bodies and other professional organizations:* FAR

- One respondent⁷⁹ felt a smaller range of 3-5 matters would be more appropriate, focused on significant financial reporting judgments, including going concern, whereas other respondents⁸⁰ were of the view that discussion of five matters would likely be appropriate.
- Another respondent⁸¹ did not think it was appropriate to specify a minimum number of matters.

Further consideration will be given to this feedback, including whether reference to the number of matters should be included in a revised ISA 700, as the objective of, and criteria for, AC is refined.

Feedback on Illustrative Examples (Question 5 of the ITC)

44. The majority of respondents generally did not support the illustrative examples in the ITC for the following reasons:
- Merely repeating management's disclosures without additional context was not seen as useful (i.e., there was a desire for more specific information about the auditor's risk assessment and response, as noted above).
 - Disclosure of difficult matters, including items discussed with TCWG and the engagement quality control reviewer, may not be necessary if these matters had been resolved to the auditor's satisfaction.
 - Reference to management commentary (i.e., other information) may imply that more work has been done than is required by ISA 720⁸² and that it was not appropriate to refer to highly subjective or unauditible information.
 - The examples as included in the ITC are likely to become boilerplate over time.
 - A detailed description of the auditor's procedures is likely not useful to investors and other users.
45. Some suggestions were made to strengthen the introduction to AC to educate investors and provide background information about the intent of AC (with reference to an expanded description of auditor's responsibilities), namely that:
- It is not a substitute for reading the financial statements in their entirety.
 - It is not a complete picture of the auditor's work effort and is unique to the entity.
 - Matters highlighted by the auditor often represent some of the most difficult and subjective areas of the audit; accordingly, the auditor tailors procedures to address the identified risks.
 - Other auditors' views might differ on the matters.
 - Matters addressed in AC may change from year to year.

⁷⁹ *Accounting firms: PWC*

⁸⁰ *Member bodies and other professional organizations: ACCA, BICA, CAQ*

⁸¹ *Accounting firms: EYG; Preparers: BE*

⁸² *ISA 720, The Auditor's Responsibilities Relating to Other Information Included in Documents Containing Audited Financial Statements*

46. Further consideration will be given to the detailed suggestions for improvement in relation to both the introductory language and the illustrative examples as the objective of, and criteria for, AC is refined.

Views on the Implications for the Financial Reporting Process of Including AC (Question 6 of the ITC)

47. Benefits of AC most frequently cited include:

- Communications with management and TCWG would be strengthened by earlier and more extensive discussions, in particular in relation to the auditor's risk assessment (and as individual matters arose that could potentially be included in AC).
- Increased confidence in corporate reporting, both in terms of demonstrating the value and relevance of the audit and the important role of the auditor, as well as an increased focus by management and TCWG on disclosures to which the auditor may refer in AC.
- Audit quality, through enhanced auditor behavior in areas on which the auditor may be expected to report.
- Promoting capital market efficiency, by providing users with more relevant information and potentially a greater awareness of risk, which may lead to a reduction in the cost of capital.

48. Consistent with the roundtables, there are varying views about the effect of AC on timing of finalizing the audit and the costs that would be incurred by auditors, management and TCWG investing time in an iterative process. For example:

- Many respondents,⁸³ primarily investors and regulators, are of the view that AC should not have significant impact on cost or timing, as the premise of AC is related to things disclosed in the financial statements and addressed already in the audit file and communicated to TCWG (e.g., matters about the audit strategy, risk assessment and response).
- However, the majority of respondents are of the view that there would be an increase in cost and time commitment as a result of AC, in part because of the need for firms to develop quality control and risk management processes. While no respondents quantified their views on possible increases in costs, it was noted that the level of cost would be directly correlated to the size and complexity of the entity and the nature of AC (e.g., the more tailored, entity-specific and subjective AC may be, the greater the cost). The IAASB was encouraged to conduct further outreach to better understand the detailed cost implications.
- Cost inefficiencies in initial years of implementation are likely, as firms and entities work to establish policies and procedures that are efficient and effective – for this reason, the IAASB is encouraged to consider whether incremental change (e.g., a staged approach) and field testing (e.g., with investors, auditors and lawyers) may be appropriate.
- Some AC may only be able to be completed once the financial statements and all other reports by management and TCWG have been completed, which could impact the potential

⁸³ *Investors and analysts:* ABI, CalPERS, EUMEDION, HEOS, ICGN, NAPF, SAAJ, SLI; *TCWG:* IBGC; *Regulators and oversight authorities:* CPAB, CSA CAC, CSIPPC, DFSA, FAP, IAIS, OECD; *Accounting firms:* RSM; *Member bodies and other professional organizations:* FAR, ICAS

release of the financial reporting package. One respondent⁸⁴ cautioned that an enhanced focus on reporting may take time away from the performance of the audit at a detriment to audit quality. One investor⁸⁵ thought that any information that delays the financial statements from being released publicly is by nature less valuable.

49. The IAASB was also encouraged to aim to more fully understand the potential implications of the proposals on auditor liability, as it was acknowledged that the potential impact varies depending on the legal environment in particular jurisdictions. Relevant points relating to auditor liability include:
- Auditors may provide a lengthy list of redundant disclosures to avoid liability. On the other hand, auditors would be inclined to report on as few matters as possible in light of the decision-making framework provided in the revised ISAs.
 - Auditors may also be affected if matters that were not cited in AC later had significant negative effects on the entity, its financial performance, or its stock price.
 - There is a risk in increasing auditor liability at a time when auditors are being held to account for decisions made by TCWG and management; AC may lead to the perception of increasing the role of the audit and the auditor.

Views on Requiring AC for Public Interest Entities (PIEs) (Question 7 of the ITC)

50. There were mixed views on whether AC should be required for PIEs, listed entities only, all entities, or some other category of entities. Responses on the applicability of AC to specific entities were directly influenced by respondents' views as to the objective of AC (i.e., whether it should address the financial statements, the audit, or both). Of note are the following views:
- Concerns about extending the requirement to include AC to PIEs were consistent with the difficulties outlined in the ITC (i.e., a lack of a globally accepted definition on PIEs, the implications for smaller PIEs, etc.)
 - The EC's proposed definition of PIEs may be too broad – it may be preferable to focus on entities of systemic importance, in particular banks.
 - Consideration needs to be given whether public sector entities are seen to, or should, be included in the definition of PIEs, as these entities often have separate long-form reporting requirements that may achieve the objective of AC.
 - Having different forms of the auditor's report for different types of entities could lead users to draw inappropriate conclusions about the relative quality of the financial statements and goes against the concept that "an audit is an audit." AC could be designed to be sufficiently scalable so as to be required for all entities.
 - There is recognition that requiring AC could be done in phases (i.e., for listed entities first) and after a post-implementation review, the IAASB could decide whether to extent the requirement to other entities or allow NSS to determine whether to do so.

⁸⁴ NSS: JICPA

⁸⁵ *Investors and analysts*: GCSPS

51. Because the discussions regarding the nature and extent of AC, as well as its applicability to certain entities, will need to follow the strategic direction that must be taken in terms of the objective of AC, the above matters are being highlighted for the IAASB's initial reaction and the TF will further consider the detailed responses about applicability of AC as the proposals evolve.

Matters for IAASB Consideration

4. What are the IAASB's suggestions as to how the differing views might best be reconciled regarding the entities for which AC should be required? For example:
- (a) Does the IAASB believe the TF should seek to develop a global definition of PIEs on which to base requirements for AC?
 - (b) Or does the IAASB believe the focus should be to require AC for listed entities, with the option for legislators or NSS to require it for the broader group of PIEs as defined in their jurisdiction?
5. What are the IAASB's views about whether the concept of a post-implementation review should be explored? Such an approach could, for example:
- (a) Subject to the approach taken in response to Question 4, provide the IAASB with further input to determine whether wider application of requirements for AC would be appropriate (e.g., for PIEs, or all entities)
 - (b) Enable the IAASB to ensure that the proposals relating to AC are achieving their intended objective.

III. Other Matters for Future Consideration, Including Alternative Approaches

52. The following areas are matters raised by respondents that the TF intends to further consider as it refines proposals relating to AC.
- Respondents who highlighted the need for a more “holistic approach” to address the information gap cited a need for reform in accounting standards to reduce complexity, rather than users relying on auditors to discern important information for them, as well as the need for TCWG to ensure management's disclosures are meaningful and focused on key risks affecting the entity. The TF intends to further consider how the TF and the IAASB may best engage with the IASB to raise views of respondents about the need for a reduction in complexity of financial reporting and a focus on critical disclosures. In this regard, the TF has acknowledged links to the IAASB's Disclosures Project.
 - In addition, the UKFRC effective company stewardship model is frequently mentioned as a preferred option to provide investors with information about both management's judgments and the audit that was performed. How can the IAASB raise the need for enhancements in corporate governance with parties who may be able to enact change in this area (e.g., IOSCO and national securities regulators, ICGN, the Financial Stability Board (FSB), others?) It was suggested that, rather than including subjective entity-specific information in the audit reports of individual entities, there may be greater benefit in audit firms providing more

transparency on pervasive matters noted in particular industries, by publishing reports or engaging directly with regulators and investors.

- The TF may need to further consider how work currently being undertaken in other relevant IAASB projects (e.g. disclosures, audit quality, the revision of ISA 720) may affect the content and timing of the exposure draft (ED) of proposed revised ISA 700.

Appendix 1

Overall Views Whether AC Is an Appropriate Response to User Demands (Question 3 of the ITC)

Note: The following table is intended to depict the level of support for the concept of AC, both on an overall basis and from a geographic perspective. Green indicates support for the concept, yellow indicates mixed views (including balancing support and lack of support from individual respondents within the category), and red indicates an overall lack of support for the concept. Blank boxes indicate no respondents fell into that particular category. The overall category is intended to be a summary of all regions. Appendix 2 provides further detail, in particular identifying caveats or where respondents believed the concept of AC should be further refined moving forward.

It is intended to provide a directional steer on key issues and has been focused on those stakeholders that are primary participants in the financial reporting supply chain. The views of other respondents, (academics, public sector organizations, member bodies and other professional organizations, and individuals and others) are included in the main paper.

	Investors and Analysts	Regulators and Oversight Authorities	National Standard Setters	Accounting Firms – Forum of Firms ⁸⁶	Accounting Firms – Regional and Smaller Firms	TCWG	Preparers
Overall	Green	Green	Yellow	Green	Yellow	Yellow	Red
Organizations with a Global Mandate	Green	Green	White	Green	White	Green	White
Asia Pacific	Green	Green	Yellow	White	Red	Yellow	White
Europe	Green	Green	Green	Yellow	Yellow	White	White
Middle East and Africa	White	Green	White	White	Green	Yellow	White
North America	Green	Yellow	Red	White	Red	White	White
South America	White	White	White	White	White	Green	White

⁸⁶ The Forum of Firms is an association of international networks of accounting firms that perform transnational audits. Members of the Forum have committed to adhere to and promote the consistent application of high-quality audit practices worldwide, and use the ISAs as the basis for their audit methodologies. They are indicated with a * on the list of respondents.

Appendix 2

The Objective and Focus of AC

	Investors and Analysts	Regulators and Oversight Authorities	National Standard Setters	Accounting Firms – Forum of Firms	Accounting Firms – Regional and Smaller Firms	TCWG	Preparers
Support for Concept of AC (Appendix 1)	Green	Green	Yellow	Green	Yellow	Yellow	Red
Focus on financial statements using an Expanded EOM/Roadmap Approach	Yellow	Yellow	Yellow	Green	Yellow	Yellow	Red
Focus on Key Area of Audit and Significant Auditor Judgments	Green	Green	Yellow	Red	Red	Yellow	Yellow
Mandate a Detailed Description of the Auditor’s Procedures	Red	Red	Red	Red	Red	Red	Red
Support AC Based on Professional Judgment with Appropriate Guidance	Green	Green	Yellow	Green	Green	Yellow	Yellow
Need for More Holistic Approach/Improvements to Financial Reporting	Yellow	Green	Green	Green	Yellow	White	Green