

## Auditor Reporting

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IAASB Meeting

Brussels, Belgium

February 12–14, 2013

# Agenda

- Revised Structure of Auditor Reporting Task Force
- Timing of Discussions and Outcomes Needed
- Auditor Commentary (AC)
- Remaining Suggested Improvements Included in the Invitation to Comment (ITC)
- Proposed Revisions to ISA 700
- Update on Accounting Standard Setters' Activities Relating to Going Concern (GC)
- Next Steps

# Timing of Discussions and Outcomes Needed

*Tuesday a.m.*

Auditor Commentary (AC), including revised objective and proposed criteria (requirements and guidance)

IAASB feedback

*Wednesday a.m.*

Remaining Suggested Improvements in ITC

IAASB agreement on proposed way forward

Proposed Revisions to ISA 700

IAASB agreement and feedback, including areas for potential new application material

*Thursday a.m.*

IAASB agreement of revised objective and suggestions for proposed requirements and guidance for AC

*Thursday p.m.*

Update on Going Concern

Discussion of Next Steps

# Auditor Commentary

## Agenda Item 2-A

## Drafting Team Recommendations

- Revised title and objective for Auditor Commentary (AC)
- Emphasis of Matter (EOM) and Other Matter (OM) paragraphs
  - Should be retained for non-listed entities and further consideration given to retaining for listed entities in light of the revised objective of AC
  - Detailed review of ISA 706 and other ISAs planned
  - Will be affected by IAASB decision on way forward for reporting on GC
- New ISA 707 to include objective, definitions, requirements and guidance for AC
- New requirement in proposed ISA 700 (Revised) for auditors of listed entities to include AC
  - Possible guidance explaining potential application by non-listed entities

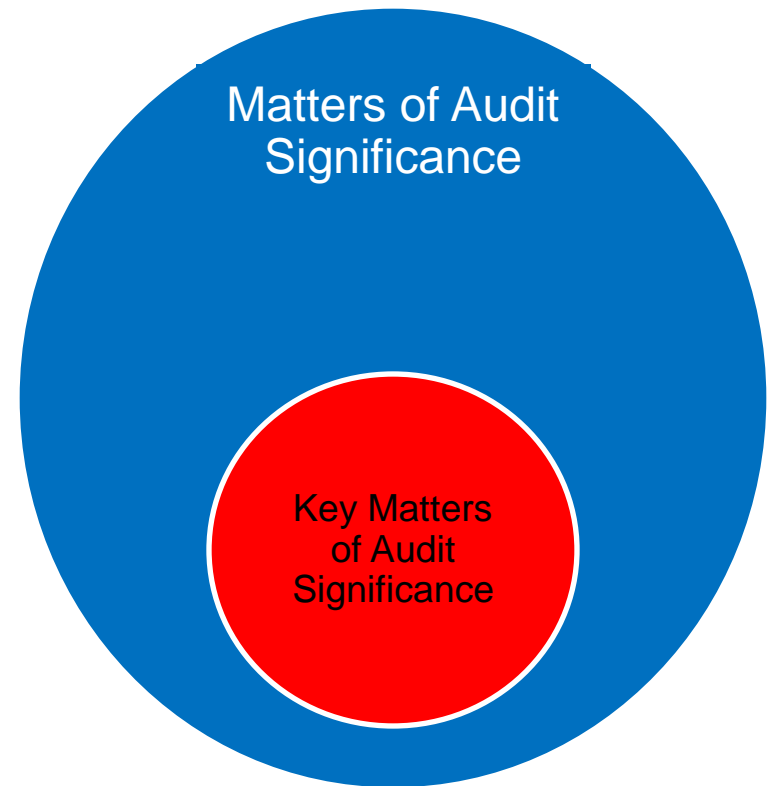
## Proposed Revised Objective for AC

The objective of the auditor,  
*having formed an opinion on the financial statements,*  
is to  
**identify and communicate in the auditor's report**  
**key matters of audit significance**  
to enhance users' understanding about the audit that  
was performed.

**Note:** Does not signal a shift *away* from significant matters in the financial statements, but rather intended to articulate a focus in the auditor's thought process of selecting matters to report based on the audit performed, with reference to the disclosures in the financial statements as appropriate.

# What Are Matters of Audit Significance?

- Matters that relate to significant auditor judgments
  - Includes matters discussed with TCWG or the EQCR
  - Any other matters that involved significant auditor judgment
- Builds on the auditor's work effort in an ISA audit
- An intentionally broad starting point to considering what should be reported externally



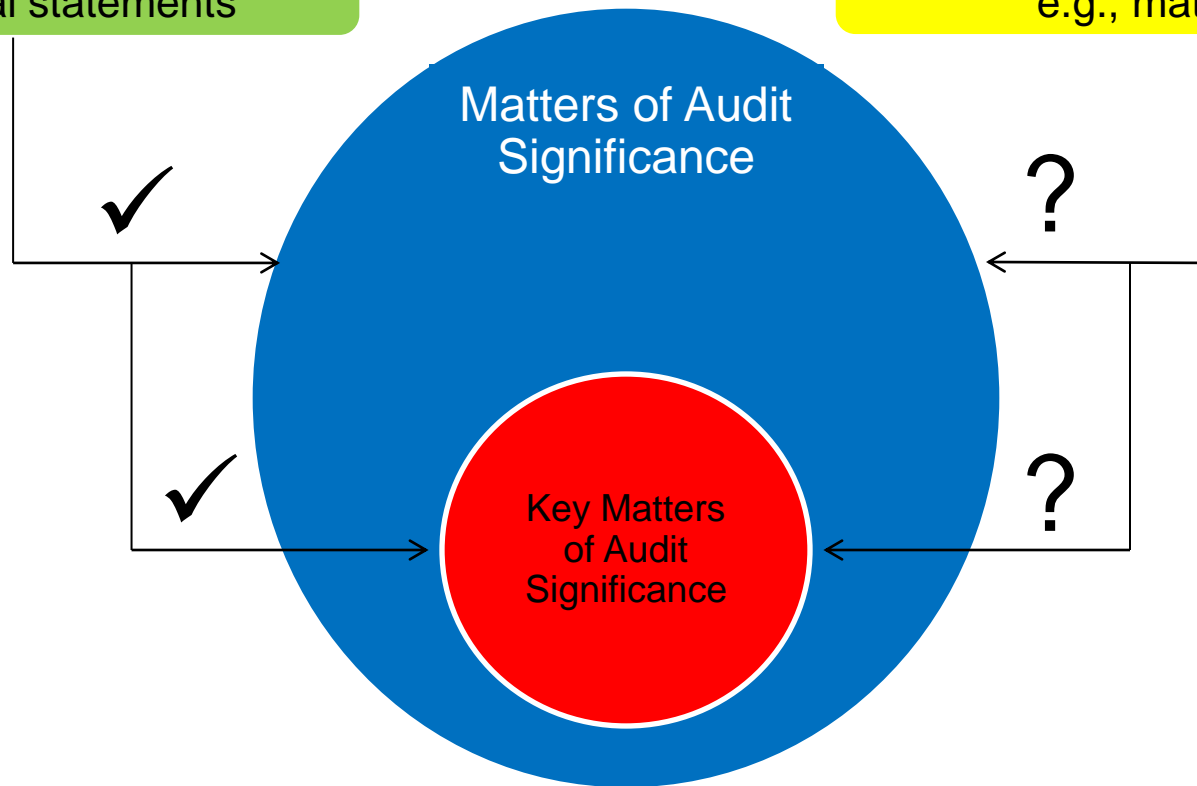
# How Do Matters of Audit Scope and Strategy Relate to Matters of Audit Significance?

## Outputs

Auditor judgments related to matters presented or disclosed in the financial statements

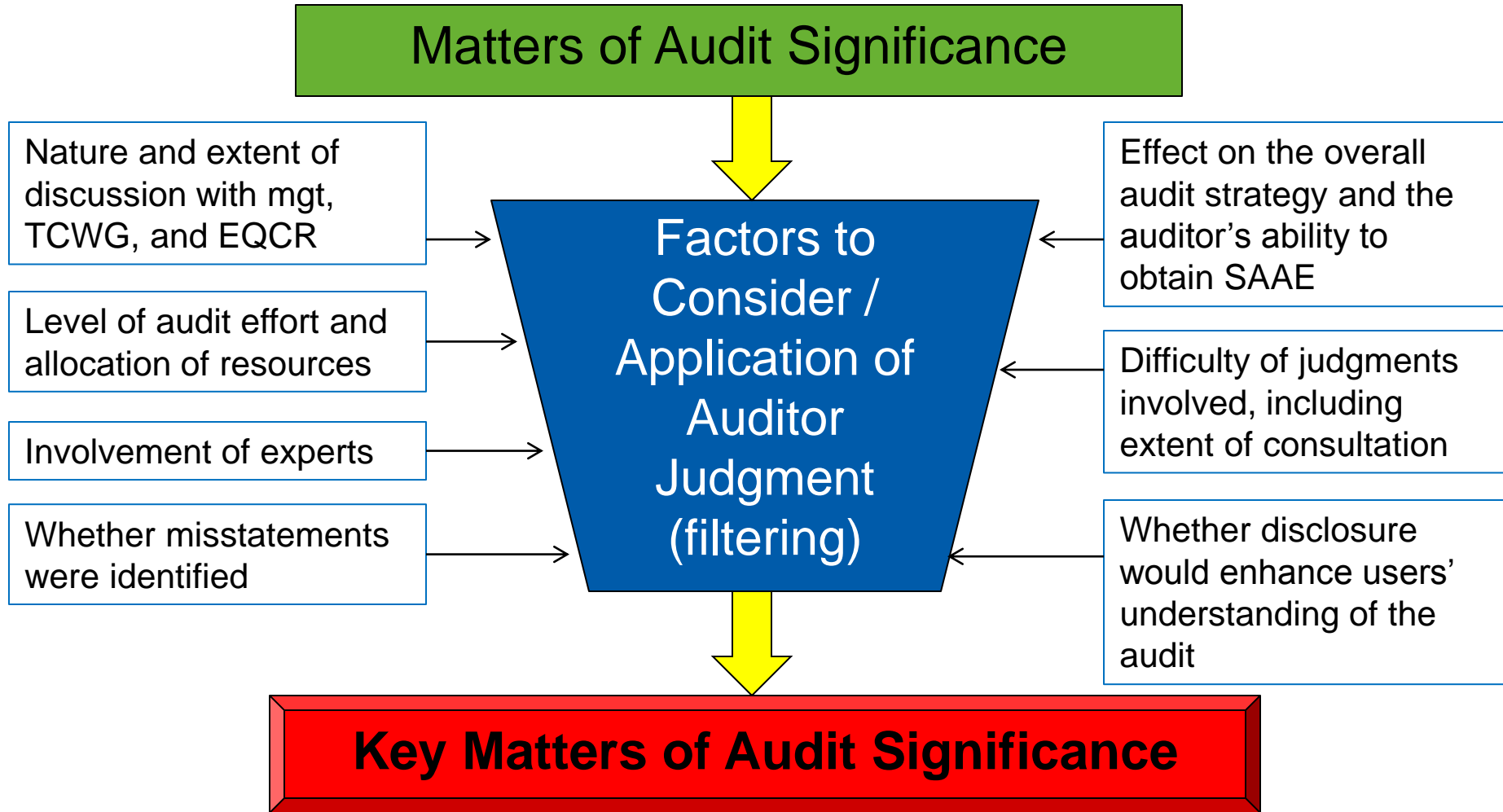
## Inputs

Auditor judgments related to planning and scoping the audit, e.g., materiality





# How are **Key** Matters of Audit Significance Identified?



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Invitation to Comment  
Agenda Item 2-B

## Involvement of Other Auditors Section II of Agenda Item 2-B

## Overall Views about Disclosing the Involvement of Other Auditors (OA)

- ITC included an example within AC about the involvement of OA
  - Reflected the breakout between affiliated and non-affiliated firms used to illustrate a group audit
  - Suggested percentage of audit hours as an appropriate measure
  - Did not disclose firm names or jurisdictions
  - Complemented by wording in Auditor’s Responsibility section on group audits
- Majority of respondents, in particular accounting firms, did not support disclosure under any circumstance
  - Doing so is contrary to the principle of “sole responsibility” in ISA 600
  - May result in users misinterpreting the role of component auditors and the degree of responsibility assumed given the safeguards in ISA 600

## Further Reasons Why Disclosure of OA Was Not Supported

- May imply that a higher level of network firm involvement leads to higher audit quality
  - Could cause pressure for audits of components to be done within one firm or network, leading to an increase in insourcing, decrease in competition and further concentration within the audit market
- Quantitative data about the use of OA on its own may not allow users to assess the impact of their involvement
- Difficult to find an appropriate, understandable and transparent approach to measuring the involvement of OA
- Important to discuss the involvement of OA with TCWG, but not a matter for disclosure in the auditor's report

## Views in Support of Disclosure of OA

- Provides additional transparency and insight into the audit process
  - Illuminates situations where significant portions of the audit, including joint ventures, are performed by firms other than the firm that signs the group audit opinion
- Could affect investors' and others' assessment of the inherent risks in the audit and could influence their views regarding the quality of the audit
  - In particular if there are different views about the quality of other auditors
  - Audit inspectors have identified issues with both the extent to which component auditors are used and the extent of involvement of the group auditor in the work of the component auditor
  - Calls for disclosure when the OA's firm is not able to be inspected

## DT-707's Consideration of a Possible Way Forward in Relation to Disclosure of the Involvement of OA

- Do not require disclosure in the auditor's report in all cases
- Consider whether disclosures about involvement of OA may be appropriate in certain circumstances
  - As a matter of audit scope or strategy?
  - In relation to matters about the group audit required by ISA 600 to be discussed with TCWG?
- Alternatively, leave the decision to require disclosure to NSS based on what is considered necessary or appropriate in the context of their particular jurisdictions and in light of their audit inspection regimes



## DT-707's Consideration of a Possible Way Forward in Relation to Disclosure of the Involvement of OA

1. In light of responses to the ITC, does the IAASB agree with DT-707's recommendation that disclosure of the involvement of OA may be appropriate in certain circumstances?

## Other Information Section III of Agenda Item 2-B

## Reporting on Other Information (OI)

- ITC signaled that the suggested wording in ITC was subject to change based on responses to the Exposure Draft of proposed revised ISA 720 (ED-ISA 720)
  - Within ED-ISA 720, IAASB developed illustrative wording to replace what was presented in the OI section of the illustrative report in the ITC
- ED-ISA 720 out for comment through March 14, 2013
  - Analysis of responses to ED-ISA 720 will further inform the IAASB's deliberations relating to a statement in the auditor's report about OI
  - Full review of comments received on ED-ISA 720 is planned for June 2013
- Important for DT-700 to liaise with the ISA 720 Task Force (TF) to determine an appropriate way forward in light of responses received to ED-ISA 720

## Overall Views about Reporting on OI

- Majority of respondents supportive of including an explicit statement in the auditor's report in relation to OI
  - Doing so clarifies the auditor's responsibilities for OI and helps avoid misinterpretation
  - Reporting on OI already done in many jurisdictions
- However, a few investors and analysts were of a view that assurance on OI may be more meaningful

## Concerns about Reporting on OI

- Conclusion may be misinterpreted by users as conveying some level of assurance on OI
  - Having a disclaimer may reduce risk of misinterpretation, but could also create further confusion about the auditor's work effort
- Practical challenges due to timing and availability of OI need to be addressed
- May be useful in the first year, but may become boilerplate and of less value over time

## Contrary Views about Including an Explicit Statement on OI

- A few respondents, in particular accounting firms and member bodies and other professional organizations, did not see the value of including a statement about OI because doing so:
  - May widen the expectations gap
  - May lengthen the auditor's report and encourages boilerplate
  - Goes beyond the auditor's existing responsibilities to conclude on the audited financial statements
  - May result in increased audit work effort, audit fees, and additional liability risks

## Suggestions Made for Improving OI Section

- Revisit placement of OI section
  - Either place after the section dealing with the auditor’s responsibilities for the audit, since OI is not audited and the auditor’s responsibilities for it are described separately, or
  - Adjacent to the auditor’s opinion – as a basis for that opinion, rather than implying separate additional responsibilities beyond the audit
- Explicitly identify in the auditor’s report whether the OI was available at the date of the report
- Disclose material misstatements of fact and their implications for the auditor’s opinion
- Clearly describe the nature and extent of the auditor’s work, and include a statement about management’s responsibilities for OI

## Enhanced Descriptions of the Responsibilities of Management, TCWG, and the Auditor Section IV of Agenda Item 2-B



## Overall Views about Enhanced Descriptions of Responsibilities of Management, TCWG and the Auditor

- Strong majority of respondents indicated that the enhanced descriptions included in the ITC were useful to users' understanding of the respective roles and responsibilities of management, TCWG, and the external auditor in the context of an ISA audit
  - Comprehensive description of the auditor's responsibilities complements new reporting elements as a means to avoid unintended consequences of widening the expectations gap
  - The more robust description of responsibilities is a useful starting point to better educate users about the audit process
  - Discussion about fraud, internal control, accounting policies and estimates, overall presentation of the financial statements and disclosures could be of great value to institutional investors

## Suggestions to Improve Usefulness of the Enhanced Description of the Auditor's Responsibilities

- Explore ways to make the wording of the section more concise, but at the same time more informative and easier to understand (e.g., avoid technical terms)
  - Detailed suggestions included in para. 41 of Agenda Item 2-B
- Explore alternate ways of further summarizing, organizing and presenting standardized information so as not to distract attention from the auditor's opinion

## Views about Description of Responsibilities of Management and TCWG

- Reposition discussion of management's responsibility for going concern (GC) to the GC section as context to that section
- Specific to the description of management's and TCWG's responsibilities, requirements should be sufficiently principles-based to accommodate jurisdictional circumstances
- Need for flexibility as to where this information may be included and how it may be described

## Contrary Views about Usefulness of the Enhanced Description of the Auditor's Responsibilities

- Many believed the lengthier description did not add value
  - Negative effect on the balance between entity-specific and standardized information in the auditor's report
  - But some support for allowing such information to be presented elsewhere
- Extant ISA 700 description of responsibilities is appropriate
  - Concept of an audit cannot be fully summarized and described in the auditor's report
- Expectations gap between what an audit does and what some users think an audit is designed to do could increase because the description of the auditor's responsibilities is significantly longer than that of management

## DT-700 Considerations for Possible Way Forward in Relation to Descriptions of Responsibilities

- Continue to explore the concept of including enhanced descriptions of the respective responsibilities of management, TCWG, and the auditor
- Consider in tandem with the possibility of allowing the material to be included in an Appendix to the auditor's report or on a website
- Revised ISA 700 will need
  - Requirements for appropriate headings in the auditor's report
  - An example auditor's report that would illustrate the IAASB's expectations of what matters should be addressed, the level of detail, and how the information should be organized
  - Requirements addressing the description of responsibilities of management, TCWG, and the auditor

## Options for Developing Requirements Regarding Description of the Auditor's Responsibilities

- *Option 1:* Mandate the specific words to be used in the auditor's report to describe the auditor's responsibilities for the audit of the financial statements
  - Preferred DT-700 approach taken in Agenda Item 2-D
- *Option 2:* Draft the requirements to describe the auditor's responsibilities for the audit of the financial statements in a manner that indicates the *concepts or matters* that should be addressed in a manner consistent with the ISAs
  - Without mandating the specific words
  - Example language would be provided in the illustrative report
  - Could result in undesirable level of flexibility, and multiple descriptions of an ISA audit, within and across jurisdictions

## Matters for IAASB Consideration

2. In light of responses to the ITC relating to the enhanced descriptions of the responsibilities of management, TCWG and the auditor, how should DT-700 proceed? For example:
  - (a) In light of the wording presented in para. 39 of Agenda Item 2-D, does the IAASB support DT-700's recommendation that a more prescriptive approach to requirements to describe the auditor's responsibilities should be taken?
  - (b) Recognizing the challenges of doing so, should DT-700 seek to further refine the description of the auditor's responsibility to be included in the illustrative report of the Auditor Reporting ED?

## Relocating the Description of the Auditor's Responsibility Section V of Agenda Item 2-B



## Overall Views about Relocating the Description of Auditor's Responsibility

- Majority of respondents to this question supported the idea of having the IAASB explicitly allow standardized material to be relocated to a website of an appropriate authority or to an appendix to the auditor's report
  - Doing so would be an appropriate way to deal with reducing the length of standardized material in the auditor's report
  - Already being done in the UK via a link to the FRC's website – concept supported by UK investors

# Views about Where the Description of the Auditor's Responsibilities Should Be Located

Support for Website	Support for Appendix
Facilitates having more detailed and useful description of the responsibilities of those involved in the financial reporting process	Users would not take the time to go to a website to read what is considered to be essential information
Should be maintained by an appropriate body (e.g., a professional body, NSS, or audit oversight body) and reflect a balanced view	Practical challenges anticipated with placing standardized information on a website (e.g., accuracy, completeness, version control and accessibility)
In either case, the auditor's report should clearly indicate how users can access standardized information, and auditors should have flexibility to judge what is appropriate in the context of the specific engagement	

## Contrary Views about Relocating the Description of the Auditor's Responsibility

- Many, in particular accounting firms, were of the view that allowing standardized information to be relocated to a website may
  - Diminish the relative importance of the information
  - Have the unintended consequence of widening the expectations gap as this information would likely not be read
- Strong view that it was necessary to read the complete auditor's report, including the description of the auditor's responsibilities, in order to fully comprehend the role of an auditor and the nature of the auditor's work

## DT-700's Considerations for a Possible Way Forward Regarding Relocation of the Description of the Auditor's Responsibilities

- Revised ISA 700 should acknowledge that, in all circumstances, auditors could be permitted to include the description of the auditor's responsibilities in an appendix to the auditor's report
- Also should acknowledge that law, regulation or national auditing standards may permit auditors to refer to the description of the auditor's responsibilities located on a website of an appropriate authority, rather than in the auditor's report

## DT-700's Considerations for a Possible Way Forward Regarding Relocation (cont.)

- If supported, appropriate safeguards must be put in place to respond to concerns about relocating this material
  - Continue to require a heading for the Auditor's Responsibility section
  - Mandate a clear and detailed reference to such information
- Application material could further indicate that
  - Content in both cases needs to address matters included in the illustrative auditor's report
  - When a website is used, it must be maintained by an appropriate body (i.e., not an accounting firm)

## Matters for IAASB Consideration

3. Does the IAASB support DT-700's recommendation that the auditor should be permitted to exclude material describing the auditor's responsibilities from the auditor's report? If so:
  - (a) Does the IAASB agree that relocation to either an appendix or a website is appropriate?
  - (b) Beyond requiring an explicit link to such material, what other safeguards, if any, should the IAASB put in place to ensure that allowing for such material to be excluded from the auditor's report does not result in users having a lesser understanding of the nature of an audit and the auditor's responsibilities?

## Disclosing the Name of the Engagement Partner Section VI of Agenda Item 2-B

## Support for Disclosing the Name of the Engagement Partner (EP)

- Many respondents, in particular investors and analysts, regulators and oversight authorities, and NSS, expressed strong support for disclosure of EP name in the auditor's report among respondents because doing so
  - Improves transparency for users
  - Is believed to provide engagement partner with a greater sense of personal responsibility and accountability, which respondents believe translates to improved audit quality
  - Is already required or customary in many jurisdictions



## Contrary Views about Disclosing the Name of the EP

- Other respondents, in particular accounting firms, challenged the value of the disclosure of the EP's name, noting that
  - Because of differing legal environments, NSS should decide
  - Having EP's name in the auditor's report instead of the firm's name may be perceived as a reduction in the responsibility of the firm
  - Having EP's name in the auditor's report result in actual or perceptions of increased legal liability exposure for the EP
  - Threats of increased liability exposure could result in increased audit fees

## DT-700 Considerations for a Possible Way Forward Relating to Disclosing the Name of the EP

- Strong public interest argument for having the name of the EP available in the public domain and recognition that this is already current practice in many jurisdictions or being explored by others
- But legitimate concerns related to auditor liability, noted particularly in the US
- Recommendation that for listed entities the EP's name should be available to users of the financial statements
  - If otherwise unavailable publicly, the name of the EP would be required to be disclosed in the auditor's report
  - Limiting the requirement to listed entities was thought appropriate as calls for such information largely came from institutional investors
  - For non-listed entities, including SMEs, often the EP's name is already known to users through other means, albeit informal in many circumstances

## Matter for IAASB Consideration

4. In light of the responses to ITC, what are the IAASB's views in relation to DT-700's suggestion relating to public disclosure of the EP's name for listed entities?

# Timing of Discussions and Outcomes Needed

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Auditor Commentary (AC), including revised objective and proposed criteria (requirements and guidance)

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Remaining Suggested Improvements in ITC

IAASB agreement on proposed way forward

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Update on Going Concern

*Thursday p.m.*

Auditor Commentary

Next Steps

# Update on Going Concern

## Going Concern (GC) Update

- In light of the responses to the ITC, at its December 2012 meeting the IAASB agreed to continue to explore auditor reporting on GC, in particular to further consider
  - How the work of accounting standard setters (i.e., IFRIC/IASB and US FASB) in the area of GC may affect the nature of the IAASB's proposals
  - Whether the use of EOM paragraphs to highlight material uncertainties should be retained
  - Whether reporting on GC should be required for all entities or whether an approach based on the importance of GC considerations to the individual entity would be preferable
- Recognition of the importance that certain stakeholders (e.g., EC) attach to having explicit statements in the auditor's report relating to GC

## Update on IASB and IFRIC Activities

- At its January 2013 meeting, IFRIC discussed limited narrow amendments to IAS 1, *Presentation of Financial Statements*
- IAASB DTs met with IASB Staff and an IASB member in advance of the IFRIC meeting and were of the view that these amendments, in particular the new examples, were helpful and were responsive to concerns expressed by respondents to the ITC about reporting on GC
- IFRIC agreed to recommend these amendments to IASB for exposure
  - If agreed by IASB, proposals would be publicly exposed and discussion would continue through late 2013

## Update on US Financial Accounting Standards Board (FASB) Activities

- FASB is proposing a new financial reporting model for management's assessment of GC, and related disclosures
  - Previously no responsibility for management to do so
- However, FASB approach establishes thresholds that are likely to result in more and potentially earlier disclosures about GC than under IAS 1
- At its January 2013 meeting, the FASB agreed to draft a proposed Accounting Standards Update for its members to consider for approval for a 90-day period of public exposure



## Proposed Way Forward for GC

- DT-700's focus will be to further consider the responses to the ITC and recommend an appropriate way forward relating to auditor reporting on GC under extant ISA 570 in April 2013
  - Priority consideration to be given to whether reporting on GC should be for all entities as a separate section in the auditor's report and implications for EOM paragraphs
  - Overarching requirement for auditors to report on GC will be in ISA 700, with specific reporting requirements to be included in proposed ISA 570 (Revised)
- DT-700 will also consider the implications of IASB and FASB proposals relating to GC

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Auditor Commentary

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# Next Steps

## February 2013 to April 2013

- Thanks to the IAASB for providing good direction for the DTs
  - DTs will meet early in March 2013 and have multiple teleconferences planned
- Substantive discussion with the Consultative Advisory Group planned for April 8–9, 2013
- For April 2013 IAASB meeting, DT-701 will prepare
  - First draft of a complete proposed ISA 701
  - Recommendations for conforming changes to ISA 260 and possibly ISA 706, depending on progress of DT-700 in relation to EOM paragraphs for GC
- For April 2013 IAASB meeting, DT-700 will prepare
  - First draft of a complete proposed ISA 700 (Revised)
  - Recommendations for the way forward in relation to GC, conforming changes to ISA 705 and possibly other ISAs

## Other Efforts

- NSS Meeting May 30–31, 2013
  - Plans to involve NSS in engaging with investors and other users at the national level in advance of the meeting
- Ongoing outreach in pursuit of alignment, to the extent practicable, with others currently addressing auditor reporting
  - EC, UKFRC, US PCAOB
- Discussion of auditor reporting continues to factor heavily on the outreach efforts of IAASB leadership
  - IOSCO, Forum of Firms, etc.
  - Considering further opportunities to interact with GAID, CFA Institute, etc.
- DT Chairs and Staff to explore how ED can be presented to continue to engage stakeholders, in particular investors
  - Explanatory Memorandum to be leveraged as a communications tool

IAASB

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