

## Proposed Changes to Other ISAs as a Result of ISA 701

### I. Changes to Proposed Conforming Amendments to ISA 210, *Agreeing the Terms of Audit Engagements*, to Address Voluntary Communication of Key Audit Matters (KAM)

#### Agreement on Audit Engagement Terms

10. Subject to paragraph 11, the agreed terms of the audit engagement shall be recorded in an audit engagement letter or other suitable form of written agreement and shall include: (Ref: Para. A22–A25)
- (a) The objective and scope of the audit of the financial statements;
  - (b) The responsibilities of the auditor;
  - (c) The responsibilities of management;
  - (d) Identification of the applicable financial reporting framework for the preparation of the financial statements; and
  - (e) Reference to the expected form and content of any reports to be issued by the auditor, ~~including, if the auditor is not required to communicate key audit matters but intends to do so, a statement that the auditor intends to communicate key audit matters;~~ and (Ref: Para. A23a)
  - (f) A statement that there may be circumstances in which a report may differ from its expected form and content.

\*\*\*

*Audit Engagement Letter or Other Form of Written Agreement* (Ref: Para. 10–11)

#### Form and Content of the Audit Engagement Letter

A23. The form and content of the audit engagement letter may vary for each entity. Information included in the audit engagement letter on the auditor's responsibilities may be based on ISA 200. Paragraphs 6(b) and 12 of this ISA deal with the description of the responsibilities of management. In addition to including the matters required by paragraph 10, an audit engagement letter may make reference to, for example:

- Elaboration of the scope of the audit, including reference to applicable legislation, regulations, ISAs, and ethical and other pronouncements of professional bodies to which the auditor adheres.
- The form of any other communication of results of the audit engagement.
- The requirement for the auditor to communicate key audit matters in the auditor's report in accordance with proposed ISA 701.<sup>1</sup> [*No change proposed from ED*]
- The fact that because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with ISAs.

<sup>1</sup> Proposed ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

- Arrangements regarding the planning and performance of the audit, including the composition of the engagement team.
- The expectation that management will provide written representations (see also paragraph A13).
- The agreement of management to make available to the auditor draft financial statements and any accompanying other information in time to allow the auditor to complete the audit in accordance with the proposed timetable.
- The agreement of management to inform the auditor of facts that may affect the financial statements, of which management may become aware during the period from the date of the auditor's report to the date the financial statements are issued.
- The basis on which fees are computed and any billing arrangements.
- A request for management to acknowledge receipt of the audit engagement letter and to agree to the terms of the engagement outlined therein.

A23a. ~~Referring to the expected form and content of the auditor's report in agreeing the terms of the audit engagement enables management and, where appropriate, those charged with governance to understand how the auditor may communicate about the audit, in particular in relation to key audit matters. When the auditor is not required to communicate key audit matters, Acknowledging that the auditor intends to communicate key audit matters in the auditor's report when not otherwise required to do so makes management and those charged with governance aware of the auditor's intent. However, the form and content of the auditor's report, including the description of key audit matters, is the sole responsibility of the auditor. When the auditor is not required to communicate key audit matters, it may therefore be helpful for the auditor to make reference in the terms of the audit engagement to the possibility of communicating key audit matters in the auditor's report and, in certain jurisdictions, it may be necessary for the auditor to include a reference to such possibility in order to retain the ability to do so~~

[**Note:** An update to the changes proposed in the Exposure Draft relating to the illustrative audit engagement letter included in Appendix 1 of ISA 210 will be considered by DT-700 for the IAASB's consideration at its September 2014 meeting.]

## **II. New Conforming Amendments to ISA 220, *Quality Control for an Audit of Financial Statements*, to Address Voluntary Communication of Key Audit Matters (KAM)**

### **Engagement Performance**

#### *Engagement Quality Control Review*

...

20. The engagement quality control reviewer shall perform an objective evaluation of the significant judgments made by the engagement team, and the conclusions reached in formulating the auditor's report. This evaluation shall involve:
  - (a) Discussion of significant matters with the engagement partner;
  - (b) Review of the financial statements and the proposed auditor's report;

- (c) Review of selected audit documentation relating to the significant judgments the engagement team made and the conclusions it reached; and
  - (d) Evaluation of the conclusions reached in formulating the auditor's report and consideration of whether the proposed auditor's report is appropriate. (Ref: Para. A26–A27, A29–A31)
21. For audits of financial statements of listed entities, the engagement quality control reviewer, on performing an engagement quality control review, shall also consider the following:
- (a) The engagement team's evaluation of the firm's independence in relation to the audit engagement;
  - (b) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations; and
  - (c) Whether audit documentation selected for review reflects the work performed in relation to the significant judgments and supports the conclusions reached. (Ref: Para. A28–A31)

...

#### *Engagement Quality Control Review*

...

#### Nature, Timing and Extent of Engagement Quality Control Review (Ref: Para. 20)

- A26. Remaining alert for changes in circumstances allows the engagement partner to identify situations in which an engagement quality control review is necessary, even though at the start of the engagement, such a review was not required.
- A27. The extent of the engagement quality control review may depend, among other things, on the complexity of the audit engagement, whether the entity is a listed entity, and the risk that the auditor's report might not be appropriate in the circumstances. The performance of an engagement quality control review does not reduce the responsibilities of the engagement partner for the audit engagement and its performance.

A27a. When the auditor is required or otherwise decides to communicate key audit matters in accordance with proposed ISA 701, the engagement quality control reviewer's evaluation required by paragraph 20 includes consideration of:

- Those matters the auditor has determined are the key audit matters to be included in the auditor's report, if any;
- The key audit matters that the auditor has determined will not be communicated in the auditor's report in accordance with paragraph 11 of proposed ISA 701, if any;
- If applicable, depending on the facts and circumstances of the entity and the audit, the auditor's determination that there are no key audit matters to communicate in the auditor's report; and
- The proposed wording to be included in the Key Audit Matters section of the auditor's report.

#### Engagement Quality Control Review of Listed Entities (Ref: Para. 21)

A28. Other matters relevant to evaluating the significant judgments made by the engagement team that may be considered in an engagement quality control review of a listed entity include:

- Significant risks identified during the engagement in accordance with ISA 315 (Revised),<sup>2</sup> and the responses to those risks in accordance with ISA 330,<sup>3</sup> including the engagement team's assessment of, and response to, the risk of fraud in accordance with ISA 240.<sup>4</sup>
- Judgments made, particularly with respect to materiality and significant risks.
- The significance and disposition of corrected and uncorrected misstatements identified during the audit.
- The matters to be communicated to management and those charged with governance and, where applicable, other parties such as regulatory bodies.

These other matters, depending on the circumstances, may also be applicable for engagement quality control reviews for audits of financial statements of other entities.

#### Considerations Specific to Smaller Entities (Ref: Para. 20–21)

A29. In addition to the audits of financial statements of listed entities, an engagement quality control review is required for audit engagements that meet the criteria established by the firm that subjects engagements to an engagement quality control review. In some cases, none of the firm's audit engagements may meet the criteria that would subject them to such a review.

#### Considerations Specific to Public Sector Entities (Ref: Para. 20–21)

A30. In the public sector, a statutorily appointed auditor (for example, an Auditor General, or other suitably qualified person appointed on behalf of the Auditor General), may act in a role equivalent to that of engagement partner with overall responsibility for public sector audits. In such circumstances, where applicable, the selection of the engagement quality control reviewer includes consideration of the need for independence from the audited entity and the ability of the engagement quality control reviewer to provide an objective evaluation.

A31. Listed entities as referred to in paragraphs 21 and A28 are not common in the public sector. However, there may be other public sector entities that are significant due to size, complexity or public interest aspects, and which consequently have a wide range of stakeholders. Examples include state owned corporations and public utilities. Ongoing transformations within the public sector may also give rise to new types of significant entities. There are no fixed objective criteria on which the determination of significance is based. Nonetheless, public sector auditors evaluate which entities may be of sufficient significance to warrant performance of an engagement quality control review.

---

<sup>2</sup> ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

<sup>3</sup> ISA 330, *The Auditor's Responses to Assessed Risks*

<sup>4</sup> ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*