

**ISA 700<sup>1</sup>—Issues and Drafting Team Recommendations****Summary of the IAASB's Discussions at Its June 2014 Meeting***Statement of Independence and Other Relevant Ethical Requirements*

The IAASB reconfirmed its March 2014 decision to require an explicit statement in the auditor's report that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The IAASB also tentatively agreed to require a statement that (i) identifies the jurisdiction of origin of the independence and other relevant ethical requirements or, (ii) when the relevant ethical requirements are those of the International Ethics Standard Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), refers to the IESBA Code.

The Board agreed further revisions to the application material supporting this requirement to provide guidance about what is intended in relation to the jurisdiction of origin of relevant ethical requirements, including in group audit situations, noting the proposed requirement allows for tailoring by law, regulation or national auditing standards to reflect jurisdiction-specific circumstances.

Ms. de Beer noted the Board's decisions appeared consistent with the feedback from the Consultative Advisory Group (CAG) to provide transparency while being mindful of impracticalities of providing extensive detail in the auditor's report. She was of the view that it was a significant improvement from earlier proposals and would provide information that would be valuable to users.

The Board agreed to seek input on its conclusions from the IESBA at the IESBA's July 2014 meeting to finalize the proposed requirement and application material.

*Disclosure of the Engagement Partner's Name*

The IAASB supported the Drafting Team's recommendation in Agenda Item 2-A for a revised requirement addressing disclosure of the name of the engagement partner in the auditor's report for audits of complete sets of general purpose financial statements of listed entities. This revised requirement permits non-disclosure in rare circumstances when disclosure is reasonably expected to lead to a significant personal security threat, with application material explaining that non-disclosure is not intended to include threats of legal liability, or legal, regulatory or professional sanctions. The Board also agreed that, if the auditor intends not to include the name of the engagement partner in the auditor's report, the auditor should discuss this intention with those charged with governance (TCWG) to assess the likelihood or severity of a significant personal security threat. Ms. de Beer suggested the CAG would likely support this requirement as revised.

The Board also agreed revised application material to explain that the auditor may also be required by law, regulation or national auditing standards, or may decide, to include additional information beyond the engagement partner's name in the auditor's report to further identify the engagement partner (e.g., the engagement partner's professional license number that is relevant to the jurisdiction where the auditor practices).

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<sup>1</sup> Proposed ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*

#### *Other Revisions to Proposed ISA 700 (Revised)*

The Board also agreed further refinements to proposed ISA 700 (Revised), as included in Updated Agenda Item 2-B. Except for certain proposed requirements related to going concern and key audit matters, the Board agreed to close off its deliberations on proposed ISA 700 (Revised). It will further consider the illustrative reports included in the Appendices of proposed ISA 700 (Revised) at its September 2014 meeting.

#### *Revisions to ISA 705<sup>2</sup>*

The Board tentatively agreed recommendations of the Drafting Team set out in Agenda Item 2-A and the corresponding revisions to proposed ISA 705 (Revised) in Agenda Item 2-E. However, the Board asked the Drafting Team to further refine the standard to take into account the Board's discussions about whether the requirements to report on key audit matters, going concern and other information should apply when the auditor expresses an adverse opinion or disclaims an opinion on the financial statements. Specifically, the Board asked the Drafting Team to:

- Simplify the structure and geography of those requirements, by placing all requirements relating to modifications of the auditor's opinion in proposed ISA 705 (Revised) rather than in proposed ISA 700 (Revised) or other standards.
- Revisit whether it was appropriate to have requirements that explicitly prohibit reporting certain information in the auditor's report when the auditor expresses an adverse opinion or disclaims an opinion on the financial statements, in particular the auditor's responsibilities with respect to other information. In this regard:
  - The Board confirmed its preference for the approach taken in proposed ISA 720 (Revised)<sup>3</sup> to require auditor reporting on other information when the auditor expresses an adverse opinion, rather than the DT-705 recommendation to prohibit such reporting.
  - It was suggested that having the auditor's report describe a material misstatement of other information could in some circumstances be relevant to users even when the auditor disclaims an opinion on the financial statements and hence a prohibition on doing so would not be appropriate.

#### **Objectives of the IAASB Discussion**

The following are the objectives of the IAASB discussion at its September 2014 meeting:

- Consider input received from the IESBA on the Board's June 2014 revised proposal related to the statement of independence and other relevant ethical requirements.
- Approve the revised drafts of proposed ISA 700 (Revised) and proposed ISA 705 (Revised).
- Consider revisions to proposed ISA 705 (Revised) addressing whether the requirements to report on key audit matters, going concern and other information should apply when the auditor expresses an adverse opinion or disclaims an opinion on the financial statements.

<sup>2</sup> Proposed ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*

<sup>3</sup> Proposed ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information*

- Consider and finalize proposed changes to other ISAs (all conforming amendments) arising from the auditor reporting project (**Agenda Item 2-F**).

## I. Statement of Independence and Other Relevant Ethical Requirements

### A. Feedback from the IESBA

1. At the IESBA's July 9, 2014 meeting, the DT-700 Chair solicited views from IESBA members on the IAASB's revised proposal (i.e., illustrative wording, requirement and application material as agreed at the IAASB June 2014 meeting) related to having a statement about compliance with independence and other relevant ethical requirements in the auditor's report. The IESBA agenda material that facilitated this discussion is available on the IESBA website.<sup>4</sup>
2. The IESBA unanimously supported the IAASB's June 2014 proposal, but suggested that the IAASB consider:
  - Providing guidance within proposed ISA 700 (Revised) to address circumstances when a dual reference to both the IESBA Code and national independence and other relevant ethical requirements might be appropriate.
  - Whether the illustrative wording that refers to the IESBA Code could be more prominently presented in the standard, such that it would be indicated as the preferred approach versus having it presented as a secondary option in a footnote.
  - Minor editorial and drafting suggestions aimed at clarifying the illustrative wording and the application material.

### B. Drafting Team Recommendations

#### *Illustrative Auditor's Reports*

3. DT-700 considered the input from IESBA and recommends that changes be made to the circumstances that are assumed for the illustrative auditor's reports in proposed ISA 700 (Revised) to reflect when:
  - The relevant ethical requirements that apply to the audit comprise the IESBA Code, together with the ethical requirements that are relevant to the audit of the financial statements in the jurisdiction (see Illustration 1 of **Agenda Item 4-B**);
  - The IESBA Code comprises the relevant ethical requirements that apply to the audit (see Illustration 2 of **Agenda Item 4-B**); and
  - The relevant ethical requirement that apply to the audit are those of the jurisdiction (see Illustrations 3–4 of **Agenda Item 4-B**).
4. In the illustrative auditor's reports across all the other auditor reporting standards, for simplicity, the statement about independence and ethical requirements refers to:
  - The IESBA Code in the case of consolidated financial statements; and

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<sup>4</sup> See July 2014 IESBA Meeting Agenda Item 6, *Auditor Reporting—Independence and other Relevant Ethical Requirements* at <http://www.ifac.org/ethics/meetings/july-7-9-2014-new-york-usa>

- The relevant ethical requirement that apply to the audit in the jurisdiction in all other circumstances.
5. Notwithstanding the IESBA's suggestion to illustrate reference to the IESBA Code as the preferred approach, DT-700 is of the view that illustrating different circumstances and illustrative wording in the auditor reports in the standard would provide more guidance to auditors. DT-700 is also of the view that depicting a reference to the IESBA Code within the body of the auditor's report in Illustrations 1 and 2 of **Agenda Item 4-B**, rather than how it was previously presented in a footnote, is an appropriate way to provide a steer towards referring to the IESBA Code in ISA auditor's reports.
  6. Though not explicitly stated in proposed ISA 700 (Revised), it is envisaged that the auditor will only make a reference to the IESBA Code when it is applicable. Thus, in circumstances when the IESBA Code is not relevant to a jurisdiction, a reference to the IESBA Code in an auditor's report would not be appropriate.

*Requirements and Application Material*

7. Paragraphs 28(c), A34 and A38–A39 of **Agenda Item 4-B** reflect clarifications made to the ISA resulting from input from IESBA members, in particular as it relates to the application material relevant to group audits.

**Matter for IAASB Consideration**

1. The IAASB is asked for its views on the revisions to the illustrative wording, requirement and application material in proposed ISA 700 (Revised) relating to the statement of independence and other relevant ethical requirements.

## **II. Revisions to ISA 705**

### **A. Elements to Be Included in the Auditor's Report When the Auditor Expresses an Adverse Opinion or Disclaims an Opinion on the Financial Statements**

*The IAASB's Position in the Exposure Draft (ED)*

8. The IAASB's proposals included in proposed ISA 705 (Revised) in the ED prohibited the auditor from including additional information on going concern, key audit matters, and other information when the auditor disclaims an opinion on the financial statements. Proposed ISA 705 (Revised) also prescribed the use of an abbreviated auditor's responsibilities section when the auditor disclaims an opinion on the financial statements. The IAASB's ED did not include such prohibitions in proposed ISA 705 (Revised) when the auditor expressed an adverse opinion.

*Going Concern*

9. At its June 2014 meeting the Board agreed that there may be merit in allowing for auditor reporting on material uncertainties related to going concern even when the auditor disclaims an opinion on the financial statements, given the importance investors attach to going concern issues and the fact that such disclosure would have been required by extant ISA 570. Accordingly, the requirement in paragraph 29 of proposed ISA 705 (Revised) does not prohibit the auditor from doing so.

#### Key Audit Matters (KAM)

10. Paragraphs 20–22 of Section III of **Agenda Item 2-A** addresses the changes to proposed ISA 700 (Revised) and proposed ISA 705 (Revised) relating to KAM, reflecting the Board’s decision at its June 2014 meeting to require reporting on KAM when the auditor expresses an adverse opinion, but to prohibit the auditor from doing so when the auditor disclaims an opinion on the financial statements as a whole, as well as other clarifications determined to be necessary to align the ISAs.

#### Other Information (OI)

14. As the ISA 720 Task Force (TF) is still considering the implications of auditor reporting on OI more broadly, the DT-700 Chair and ISA 720 TF Chair, together with Staff, are of the view that it is more appropriate for the ISA 720 TF to consider whether auditor reporting on OI should be prohibited when the auditor expresses an adverse opinion or disclaims an opinion on the financial statements. As such, this circumstance is no longer explicitly addressed in paragraph 29 of **Agenda Item 4-C**. Rather, a conforming amendment will be made to ISA 705 (Revised), and if necessary, proposed ISA 700 (Revised), to address those issues once the ISA 720 project is finalized.

#### Matter for IAASB Consideration

2. The IAASB is asked for its views on the revised draft of proposed ISA 705 (Revised) presented as **Agenda Item 4-C**.

### III. Other Revisions to ISAs 700 and 705

#### A. Revisions Resulting from the Work of Other Drafting Teams

11. Paragraphs 29, 34(b)–(c), 39(b)(iv), 50(f)–(g) and A48 of proposed ISA 700 (Revised) include changes resulting from the work of the going concern Drafting Team (DT-570). The rationale for these changes are described in **Agenda Item 3-A**. Similarly, paragraphs 30, 31, 50(h), A40–A43 and A70–A73 of proposed ISA 700 (Revised) include changes resulting from the work of key audit matters Drafting Team (DT-701). The rationale for those changes are described in **Agenda Item 2-A**.

#### B. Other Changes to ISA 700

##### *Illustrative Auditor’s Reports*

12. The illustrative auditor’s reports included in the Appendix to proposed ISA 700 (Revised) were not included in the June 2014 version of the ISA. Instead, Illustration 2 of the Appendix was presented as a separate agenda item. Illustration 2 in proposed ISA 700 (Revised) is shown in marked text to reflect the further refinements arising from the Board’s discussions at its June 2014 deliberations. Illustrations 1, 3, and 4 are shown in clean, but reflect all changes necessary to be in alignment with both Illustration 2 and the revised requirements in proposed ISA 700 (Revised).

##### *Requirements and Application Material*

13. **Agenda Item 4-B** also includes minor changes resulting from editorials and clarifications suggested by Board members since the June 2014 meeting.

## IV. Other Conforming Amendments

14. The IAASB's July 2013 ED included proposed changes to extant ISA 210.<sup>5</sup> The IAASB considered revisions the proposals related to the scope of DT-701's work at its June 2014 meeting. DT-700 is responsible for considering the revisions to the illustrative engagement letter in extant ISA 210, which included the revised descriptions of management and the auditor's responsibilities. Section II.A of **Agenda Item 2-F** includes DT-700's proposed changes to ISA 210 since ED.
15. At the time that the ED was finalized, it was also agreed that conforming changes would be made to all other illustrative auditor's reports included in the ISAs in finalizing the auditor reporting project. Sections II.B-D of **Agenda Item 2-F** include conforming amendments to other ISAs resulting from the auditor reporting project, including conforming amendments to illustrative auditor's reports that are included in ISAs 510,<sup>6</sup> 600<sup>7</sup> and 710,<sup>8</sup> respectively Those changes are intended to align to the revised presentation and incorporate the enhancements that form part of proposed ISA 700 (Revised).

### Matters for IAASB Consideration

3. The IAASB is asked for its views on the other revisions to the proposed ISA 700 (Revised), including the revisions to the illustrative auditor's reports.
4. The IAASB is also asked for its views on the proposed conforming amendments to the other ISAs.

### Significant Matters Identified by DT-700

13. In DT-700's view, the significant matters it has identified as a result of its deliberations since the beginning of this project, and its considerations therein, have all been reflected in the issues papers presented to the IAASB at its meetings. In DT-700's view, there are no significant matters it has discussed in this project that have not been brought to the IAASB's attention.

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<sup>5</sup> ISA 210, *Agreeing the Terms of Audit Engagements*

<sup>6</sup> ISA 510, *Initial Audit Engagements—Opening Balances*

<sup>7</sup> ISA 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*

<sup>8</sup> ISA 710, *Comparative Information—Corresponding Figures and Comparative Financial Statements*