

IAASB CAG PAPER

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Auditor Reporting—Draft IAASB Consultation Paper

Draft Consultation Paper

Enhancing Auditor Reporting and Evolving the Standard Auditor’s Report

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Preface

Recent discussions, consultations and studies have focused on the value to users of the auditor’s report issued in connection with the audit of financial statements.

In recent years there have been a number of improvements to the standard auditor’s report (SAR),¹ including the addition of wording to clarify the scope of the audit and the respective responsibilities of management and the auditor. Some have suggested, however, that now is the time for a more fundamental review of auditor reporting. This has been in the context of concern that the auditor’s report has not kept pace with the globalized economy and increasingly complex financial reporting requirements, and that auditor reporting and communications are not meeting the needs of financial statement users.

The importance of the financial statement audit and the value of the independent auditor’s opinion on the financial statements generally are not being questioned. Rather, the debate is centered on user needs for additional information about the audited financial statements and about the audit performed, and the role of the auditor and the auditor’s report in providing that information for the users of audited financial statements.

The focus of the recent discussions and debate is not simply on the entity’s financial statements and the independent auditor’s report on those financial statements. The current corporate reporting model in many jurisdictions involves not only compliance with the requirements of the applicable financial reporting framework in financial statements produced for periodic external financial reporting. It also includes narrative disclosures about the entity’s financial condition and operating results, and a wide range of other non-financial information, including that which the entity discloses in its public filings. Nevertheless, financial statement users are also looking for independent “validation”—that is, assurance—regarding the reliability and completeness of this broader range of corporate information disclosures, which they believe would help them make more informed decisions.

Academic research has shown that user perceptions of the quality of auditor reporting seem to be closely linked with their perceptions of the scope and quality of audits. Some would argue that this further supports the development of an expanded auditor reporting model that would include additional commentary in the auditor’s report on the financial statements, along with increased auditor involvement with, or assurance on, the entity’s non-financial information disclosures. Those holding this view contend that a more holistic auditor reporting model would not only better meet the information needs of financial statement users, but also would have a salutary effect on audit quality.

In the near term, the evolution of auditor reporting has become a priority to demonstrate to users the continued relevance of the financial statement audit and the important role of the independent auditor.

Many hold the view that those charged with the governance of an entity can also play an important role in meeting users’ information needs. Under such a model, those charged with

¹ International Standard on Auditing (ISA) 700, *Forming an Opinion and Reporting on Financial Statements*, was issued as a revised standard by the IAASB in December 2004.

governance, likely through an audit committee, would provide a report to users regarding its responsibilities for overseeing the financial reporting process and the audit. Auditors could provide assurance regarding the reasonableness and completeness of the information provided, along with a more detailed report to, and dialogue with, those charged with governance about significant audit matters. Although there is merit in the further development of corporate governance reporting to help bridge the so-called “information gap” experienced by financial statement users, substantial challenges may exist in implementing such a model in many jurisdictions.

Whatever the extent of changes that are viewed as necessary, and may have the potential to deliver a worthwhile result taking into account the interests of not only auditors and users, but also those of other stakeholders likely to be affected, those changes would need to be carefully considered in light of relevant cost-benefit considerations, and an evaluation of other implications and foreseeable consequences. This should include consideration of legal, regulatory or practical challenges associated with proposed changes, as well as safe harbors for management, those charged with governance, or independent auditors where needed to facilitate envisaged changes.

This Consultation Paper is designed to obtain feedback about how auditor reporting might be enhanced for users. It addresses a number of possible areas of change in the auditor reporting model, including possible changes to the structure and content of the SAR. The key premise underlying these nearer-term possible options is that the current scope of the audit performed in accordance with established auditing standards (for example, International Standards on Auditing (ISAs)) will not change, nor would the role of the auditor in the audit of financial statements.

The IAASB believes it is imperative to consult widely across the broad range of stakeholders, including users of audited financial statements, so as to better understand how the value and relevance of the auditor’s report might be enhanced, and what form such enhancement(s) should take. Feedback is solicited from different groups of users of audited financial statements, and also from preparers and auditors, in a number of key areas where the IAASB would like to obtain a better understanding of the relevant issues and about how best to address them. Responses to this consultation will help to inform the IAASB’s views about possible future standard-setting activities on the topic of auditor reporting.

The IAASB encourages all stakeholders to respond to this consultation. Specific questions have been drafted to assist respondents in providing feedback on key aspects of the IAASB’s preliminary thinking. In addition to, or as part of, their response to the IAASB on the specific questions, respondents may choose to provide information from other policy initiatives or research that they believe is relevant to the issues raised in the Consultation Paper.

I. Introduction

Purpose

1. The IAASB is undertaking this public consultation to explore views of a wide range of constituents interested in auditor reporting, about possible approaches to:
 - (a) Enhance the quality, relevance and value of audit reporting; and
 - (b) Improve the standard auditor’s report (SAR) for the financial statement audit.
2. The consultation is being done with full acknowledgement of the range of prior discussions, public consultations and research studies on the topic of auditor reporting.² These have provided a significant body of contemporary information about:
 - (a) User and preparer views on auditor reporting, including perceptions of its relevance and usefulness; and
 - (b) How auditor reporting might be better positioned to effectively deliver value as part of an enhanced corporate reporting and auditing model to meet the reasonable needs of external stakeholders in the current financial reporting environment.

A list of sources consulted in the course of the IAASB’s current initiative is given in Appendix 2.

3. This Consultation Paper builds on the preceding discussions and consultations on the subject, and aims to advance the debate on auditor reporting in the areas identified in paragraph 1.
4. It is intended that the results of this consultation will provide information relevant to the IAASB’s consideration of any future standard-setting initiatives to further develop the ISAs addressing auditor reporting in the direction of desired change, for the widest benefit and on an international basis.

Context

5. Auditor reporting is a topic of international relevance for which the perspectives of the international community are needed to develop possible approaches to further evolve auditor reporting in ways that are able to be applied on an international basis.

Today’s Challenges in Auditor Reporting

6. Against the backdrop of significant new challenges in the business and reporting environment, and consistent with various recent discussions and consultations on auditor

² In 2009, the IAASB commenced an initiative in the area of auditor reporting to give broad consideration to questions about how auditor’s reports on financial statements might be enhanced. Its various efforts to date have included: a broad review of environmental factors pertinent to auditor reporting; examination of contemporary research on user perceptions of the SAR under ISAs; and preliminary consultation with key stakeholders with a view to obtaining an understanding of their concerns and needs regarding auditor reporting. Further information about the IAASB’s current initiative relating to auditor reporting is available at: www.ifac.org/IAASB/ProjectHistory.php?ProjID=0095.

reporting and perspectives contributed by research studies on the subject, the IAASB is of the general view that auditor reporting will need to evolve further to retain its relevance for users of audited financial statements.

7. It is important to appreciate at the outset the wide diversity of users of corporate financial reports and a similar diversity in the ways that auditors’ reports are read and used. As a result, the current views about the usefulness of the SAR tend to be different among the different user groups. An important aim of this consultation is to elicit views of a broad cross-section of different types of users of auditor’s reports.
8. Issues addressed in the Consultation Paper do not exhaustively address experiences and views of all types of users of audited financial statements. Some types of users have been forthcoming in their views on auditor reporting (large investors and financial analysts in particular). Other types of users may conceivably have concerns in other areas not covered in this paper, or indeed may not have any significant concerns to raise on auditor reporting.
9. Nevertheless, a sufficient amount of concern is evident, including through the views provided by some capital market participants—investors and financial analysts, among others—that auditor reporting is perceived to be falling short in meeting users’ needs.

IAASB’s Role and Scope of Consultation

10. As an active participant in the international policy debate, the IAASB is able to make an important contribution in this area in the context of its mandate and strategic objective to develop high-quality auditing standards to promote both audit quality and international convergence in auditing.
11. It is a matter of priority for the IAASB to develop perspectives and obtain views in areas that will influence the development of the ISAs as they relate to auditor reporting. Advancing the evolution of auditor reporting in the desired direction of change will require a coordination of effort at an international level.
12. There are many players undertaking various activities, including standard setting and public consultation with a view toward developing law or regulation at the national level, as is well-illustrated through the recent efforts of a number of national regulators and national auditing standard setters (NSS).
13. This is a positive sign, as there are a number of important issues that relate to individual regulatory systems or corporate governance frameworks, and therefore go beyond the realm of what can be achieved through the ISAs alone. It is clear from the debate that there is opportunity for auditor reporting to evolve further, not only in the context of the international standards on auditing but also in the context of the broad regulatory infrastructure for corporate reporting and information disclosure and systems of corporate governance of which the independent audit is inherently a part.

Public Sector Auditing Perspectives

14. Evolution of auditor reporting in the context of public sector audits has followed developments in public sector auditing over time in different national settings. The public sector auditor’s responsibilities typically derive from the audit mandate, or by obligations on public sector entities arising from law, regulation or other authority (such as ministerial directives, government policy requirements, or resolutions of the legislature), which may encompass a broader scope than the audit of financial statements for entities in the private sector.
15. Auditor reporting requirements germane to public sector audits are addressed in the pronouncements of the International Organization of Supreme Audit Institutions (INTOSAI)³ or the relevant NSS in respect of public sector audits, or in guidance developed by government agencies.
16. Not all of the issues addressed in this Consultation Paper also affect reporting in public sector audits. To the extent that they do, the IAASB expects to work with INTOSAI and NSS for public sector audits, where applicable, to obtain their views as relevant to this consultation.

Perspectives for Audits of Smaller Entities

17. Some are of the view that auditor reporting for audits of smaller entities may be relatively less affected by some of the issues addressed in this paper, regarding the information needs of financial statement users. The financial reporting environment may be less complex for smaller entities, and such entities typically have a narrower range of users that may be able to obtain additional information about the entity through ongoing interactions with management.
18. Others hold the view, however, that it is important to retain consistency in auditor reporting for all entities, regardless of their size and especially as it generally proves difficult to draw clear and consistent boundaries between entities on the basis of size. This would also vary between different countries or jurisdictions.
19. The IAASB will similarly seek views of key constituents in small- and medium-sized entities (SME) audit markets on the issues raised in this paper, through interaction with representative groups that are able to convey the views of users, preparers and auditors from this segment of the audit market.

Overview of this Consultation Paper

20. Section II of this paper outlines areas of concern in relation to the information gap that is perceived by users. It explores channels for the communication of information about the entity to the entity’s shareholders and other financial statement users, including through

³ The INTOSAI Financial Audit Subcommittee (FAS) has developed INTOSAI guidelines based on the clarified ISAs, referred to as the International Standards of Supreme Audit Institutions (ISSAIs) for financial audit. An INTOSAI guideline consists of a Practice Note and the ISA it refers to, or of a newly written INTOSAI guideline and general guidance on public sector issues.

auditor reporting and other external reporting undertaken as part of an entity’s corporate governance arrangements.

21. Section III—the central focus of the consultation—explores possible areas of change to enhance auditor reporting, premised upon the assumption of no changes to the current scope of the financial statement audit. However, wider perspectives relating to auditor reporting are also discussed.
22. The IAASB sees clear opportunity for meaningful evolution of auditor reporting, on an international basis. These possible areas of change are those that the IAASB views, on a preliminary basis, as holding the best near-term prospects of bridging the information gap through the channel of auditor reporting.
23. While additional changes in auditor reporting could be explored in the context of expanding the scope of the financial statement audit, such discussion is beyond the scope of this consultation. Change of that nature would necessarily involve consideration of a range of other related factors including, for example, the institutional arrangements for the external audit function as reflected in relevant law and regulation. These are beyond the scope of the IAASB’s mandate.
24. A further overarching aim of this consultation is to emphasize the fundamental importance of taking a holistic view of auditor reporting set within the context of the applicable regulatory and corporate governance environment and related reporting requirements. While the Consultation Paper does not extend to a detailed examination of these wider perspectives, their importance to the future evolution of auditor reporting in the longer term is acknowledged. Some participants in the debate about auditor reporting have reasonably argued that only change at that level can more fully and effectively address the information gap.
25. In this regard, there is room to also further leverage the anticipated beneficial effects of change that would seem possible to advance through further development of auditing standards, by encouraging the concurrent evolution of corporate governance and regulatory systems, specifically regarding their interaction with auditor reporting. For example, an important evolving perspective being advanced in the United Kingdom (UK) is the need to encourage development of mechanisms or approaches to facilitate flow of relevant information from the entity’s management and the external auditor to the entity’s governing body or audit committee and, as appropriate, to financial statement users (discussed further in paragraphs 108-109).
26. Further, there is growing call for development of corporate information disclosure models that will encompass reporting of a broader range of information relevant for users’ decision-making—specifically, investors and other types of capital market participants.⁴

⁴ An example of such a developing disclosure framework is that being progressed through the initiatives of the International Integrated Reporting Committee (IIRC), which is working towards developing a new, integrated reporting framework that will encompass reporting of both financial and non-financial information about an entity under an integrated reporting model. It would be designed to include appropriate assurance reporting on such reporting. The attractiveness of this initiative is the more holistic approach it would bring to corporate information

27. Section IV briefly outlines areas of change referred to by commentators in recent policy debates that are at this more holistic level, to complete the IAASB’s perspectives on the subject of enhancing auditor reporting more widely—that is, beyond the auditor’s report itself.
28. Section V aims to draw out views about potential effects, implications or consequences, for users, preparers, auditors and other stakeholders, of the possible areas of change identified in Section III, and about possible implications of moving to embrace the more developed forms of corporate governance reporting explained in Section IV. A key consideration is the impact on audit effectiveness and on audit quality (either real or perceived).

II. The Information Gap, and Exploring Channels for Communication with an Entity’s External Stakeholders

Evidence of an Information Gap

29. Users of corporate financial information face the significant challenge of understanding how various corporate financial information disclosures, including those reflected in the audited financial statements, reflect the overall picture of the entity’s financial health and the sustainability of its business in the prevailing economic environment.
30. Many acknowledge that high levels of complexity inherent to the business and reporting environment mean audited financial statements alone are unlikely to provide users with all the information they need for their financial analysis and decision-making.
31. Users, particularly investors, point to the existence of an information gap between what they need, and believe is available, including information provided by the auditor through the report on the financial statement audit, and information presented in the audited financial statements. Investors and analysts find this significantly affecting their ability to accurately price securities, and their related decision-making.
32. This gap potentially presents more general concerns relating to the efficiency of capital and investment markets. If full and proper disclosure of relevant financial and non-financial information does not occur, so that investors or financial analysts in their role as intermediaries are unable to undertake proper financial analysis of an entity to assess the value of its publicly traded securities, there is risk that markets will systematically misprice securities with concomitant adverse effects for market efficiency. This is viewed as an area of significant potential weakness.
33. Not unreasonably, investors view the solution as taking necessary steps to expand the range of relevant information provided to the investment markets through corporate reporting systems established under relevant law or regulation. This leads to consideration of what the available, and most appropriate, channels are for reporting or providing additional information to users about (a) the audited financial statements, and (b) the audit performed.

disclosure. Entity reporting under this model would cover a wider set of information disclosure about the entity than is currently achieved under existing models, including existing financial reporting frameworks. See www.integratedreporting.org.

Bridging the Information Gap—Exploring Channels for Enhanced Communication with Financial Statement Users

34. Auditors are seen as part of the solution to this issue. It has been suggested that auditors should undertake additional reporting or disclosure on a range of matters concerning the entity, some of which are unrelated to the auditor’s responsibility for determining whether the entity’s financial statements are prepared in accordance with the applicable financial reporting framework (and, where applicable, are fairly presented or give a true and fair view, as applicable).
35. Investors view an auditor’s insights into the entity and its business obtained through the audit of the entity’s financial statements as being especially relevant information for their needs—including insights on matters outside the scope of the financial statement audit, such as:
 - The quality of the entity’s governance and its management.
 - The relative degree of conservatism or aggressiveness in the accounting practices it adopts.
 - The financial health of the entity.
36. It is suggested that such reporting could take the form of “auditor commentary,” either as part of the auditor’s report or in a separate report provided by the auditor (for example, an “auditor discussion and analysis”) that could accompany the auditor’s report on the audited financial statements.
37. Some users express indifference, however, about how the information they need is provided or who provides it. Their sole interest is to obtain, or be able to access, the information that is needed and, to them, the question of whether it should be provided by the auditor, or by those charged with governance of the entity or the audit committee (for convenience, hereafter in this paper only the term “audit committee” is used when these terms are referred to in the alternative) has no particular importance.
38. Through the auditor’s two-way communications with those charged with governance (or the audit committee, in the case of larger, or public-interest entities), which is a mandatory feature of the financial statement audit in respect of any significant matters arising in the course of the audit or pertaining to the audit, the audit committee is kept abreast of all significant issues surrounding the audited financial statements, and pertaining to the audit as performed by the external auditor.
39. Despite the apparent indifference of some users, the question of what the appropriate channel for communication with external stakeholders is, on matters of interest to them (assuming it is able to be provided), including on matters unrelated to the audited financial statements, would seem quite relevant. This is addressed further in Section IV in the context of the possibility of developing an enhanced external reporting role for audit committees.
40. Finally, the information gap that users perceive may not be able to be fully bridged through enhanced reporting by either auditors or audit committees. However, there seems to be sufficient clarity in discussions of user information needs to be able to explore how auditor reporting might be able to be enhanced to respond in some of these areas. The suggestion that

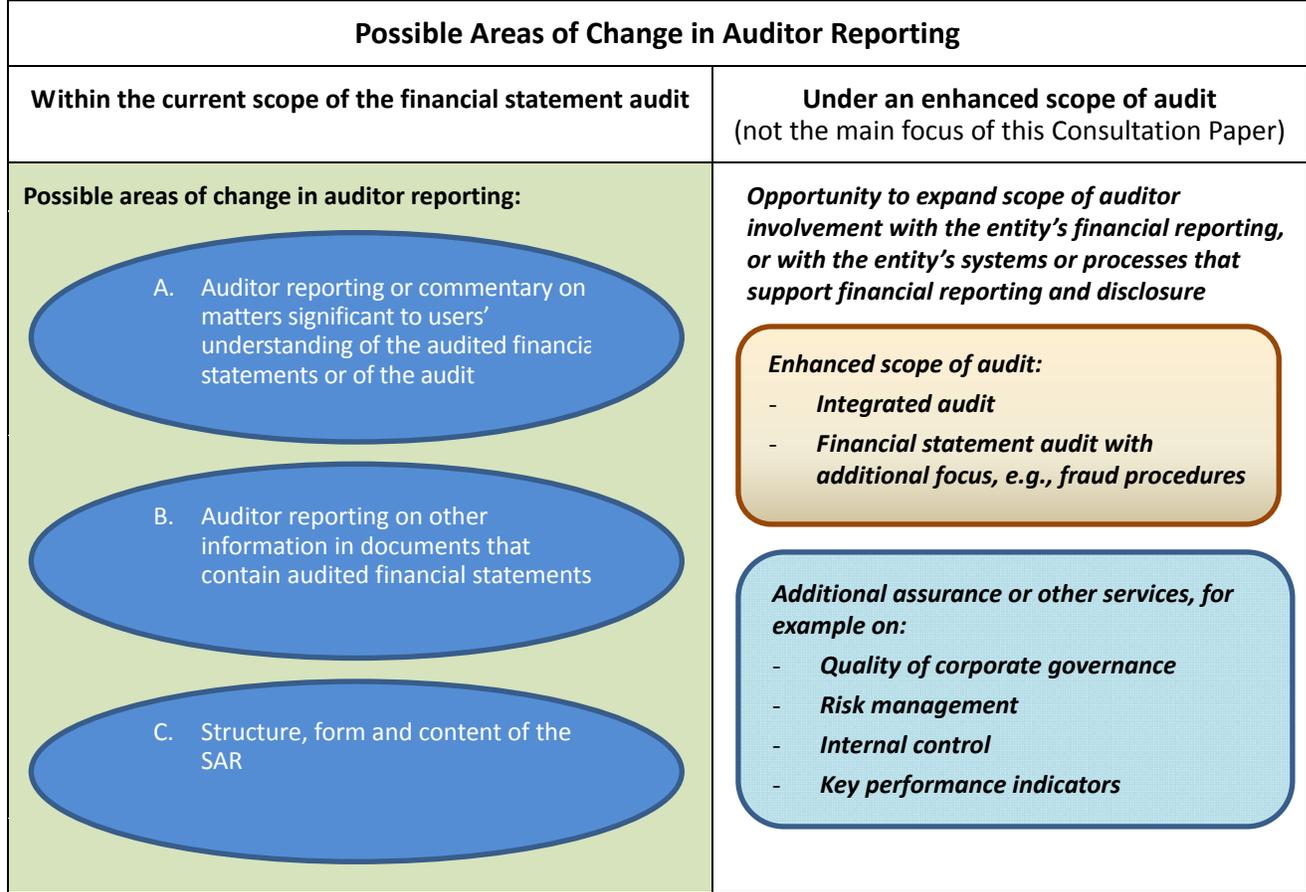
auditors have a role to play, for example through providing additional commentary about matters of interest to users in the auditor’s report, is discussed further in Section III.

<p>Question</p> <p>1. Do respondents believe the discussion of the perceived information gap in Section II is a fair reflection of the issues?</p>

III. Enhancing Auditor Reporting—Possible Areas to Explore

- 41. On the basis that the focus of this Consultation Paper is on auditor reporting under the current model for the audit of financial statements, the IAASB wishes to explore areas where auditor reporting is more likely to be able to be enhanced on an expedited basis, and where auditor reporting on an international basis may be improved.
- 42. On a preliminary basis the areas examined in this section, which build on the current scope of the audit, would seem to offer a basis for enhancing auditor reporting with a view to achieving the widest possible benefit.
- 43. The following model offers a broad conceptual basis for exploring possible approaches to enhance auditor reporting.

Diagram 1: Possible Areas of Change in Auditor Reporting



44. The left-hand side of Diagram 1 deals with changes that are possible to explore that are within the current scope of the financial statement audit. The discussion in sub-sections A–C below focuses on these three areas.
45. More extensive changes that involve changes to the scope of the financial statement audit, or the role of the auditor in providing assurance, such as those indicated on the right-hand side of Diagram 1, would necessitate more fundamental changes to the existing financial reporting regimes, and are therefore beyond the scope of this paper.
46. For example, auditors of certain listed entities in the United States (US), Japan and some other countries are required to perform an integrated audit of the financial statements and internal control over financial reporting. Another example that is sometimes cited for a possible expanded-scope audit is the inclusion of additional forensic procedures to support the auditor’s assessment and response to the risk of material misstatement due to fraud.
47. Furthermore, there is scope for expanded auditor involvement with either an entity’s financial reporting or its systems and processes that support the entity’s financial reporting, through separate engagements to report on other financial or non-financial information of the entity, for example an assurance engagement regarding the entity’s sustainability reports.
48. Under the current audit scope, the areas of possible change to the SAR that are the focus of this consultation, and that would seem reasonably likely to enhance the relevance and usefulness of auditor reporting and improve the communicative value of the SAR, are the following:
 - (a) Auditor commentary on matters significant to users’ understanding of the audited financial statements, or of the audit. (Sub-section A below)
 - (b) Auditor reporting on other information in documents containing audited financial statements. (Sub-section B below)
 - (c) Possible changes to the structure, format, and content of the SAR. (Sub-section C below)

Appendix 1 contains illustrations that show the possible areas of change discussed in sub-sections A–C below with reference to the current SAR.

Question

2. Do respondents support the approach and rationale applied in setting the focus of this consultation on addressing the areas mentioned in paragraph 48, as possible areas to explore to enhance auditor reporting?

A. Auditor Commentary on Matters Significant to Users’ Understanding of the Audited Financial Statements, or of the Audit

49. Broadly speaking, users have expressed a desire for greater transparency into the audit process. Users perceive great value in the auditor’s insights about the risks facing an entity based on the auditor’s knowledge and experience with the entity and its industry. To some, having access to more of this type of information from auditors would not only

help to address the information gap, but would also serve as a means to assess certain aspects of the quality of the audit.

50. The belief is that, if auditors were able to disclose additional relevant information about the audit performed, presented in an understandable manner, this would enhance the relevance and usefulness of the auditor’s report, and therefore its value to users.
51. The nature of additional information called for ranges widely. At one end of the spectrum, it is suggested that auditors can play a role in helping users navigate the financial statements by drawing attention to information within the financial statements, such as important disclosures, that the auditor believes is significant to users’ understanding of the audited financial statements. A perceived concomitant benefit would be enhanced attention to such matters by not only the auditor but by management as well.
52. At the other end of the spectrum are calls for auditors to provide views on qualitative aspects of the entity or its financial statements—to share the auditor’s insights and perceptions about the entity or the quality of its financial reporting based on the work done for the financial statement audit, for example auditor views on:
 - The quality of the entity’s internal controls and financial reporting processes.
 - Qualitative aspects of the entity’s accounting policies, including the relative conservatism or aggressiveness reflected in management’s selected policies.
 - The quality and effectiveness of the entity’s governance structure and risk management, and the quality and effectiveness of its management.
53. Regarding the audit itself, it has been suggested that useful additional reporting by the auditor might include information about the following types of matters:
 - Key areas of audit risk identified by the auditor that influenced the conduct of the audit.
 - Areas of significant auditor judgment, for example judgments about material uncertainties that may cast doubt about an entity’s ability to continue as a going concern, or judgments pertaining to the recognition, de-recognition, measurement or disclosure of relevant items within the financial statements.
 - The auditor’s assessment of management’s critical accounting judgments and estimates, including where each critical judgment or estimate falls within a range of possible results.
 - The level of materiality applied by the auditor to perform the audit.
 - The auditor’s assessment of the entity’s internal controls, including significant internal control deficiencies identified by the auditor during the audit.
 - Areas of significant difficulty encountered during the audit and their resolution.
54. While acknowledging users’ desire for the type of information described in paragraphs 52 and 53, some participants in the debate caution that providing such information could be problematic and may have the unintended effects of either:

- (a) Hindering users’ ability to make decisions based on the audited financial information, for example where information would be more likely to confuse the users than serve as useful clarification; or
 - (b) Undermining perceived audit quality, for example by creating doubt in the minds of a user as to whether the additional information provided is an implicit qualification of the auditor’s opinion or perceived as providing assurance on certain elements of the financial statements or disclosures.
55. Notwithstanding the caution expressed above, as the debate has advanced, it has become more apparent that users place particular emphasis on having additional information about the matters described in the first three bullet points in paragraph 53. These are largely all concerned with matters already disclosed in the financial statements.
56. The current auditor reporting model established in France, which was introduced a few years ago and developed in the context of law applicable to corporate reporting and auditing in France, requires auditors to explain their key judgments and assessments made during the financial statement audit. This model goes beyond the current requirements of the ISAs in some respects, mainly because the reporting of this additional information is required for all audits of all type of entities. It would seem to be worth exploring whether this model, or a similar model that would provide greater insight into the audit performed, can be applied to further develop the SAR under the ISAs.
57. A recent survey carried out in France to obtain views about the usefulness of the additional disclosure by the auditor from groups representative of a wide range of users revealed broad consensus that the required disclosure of the auditor’s ”justification of assessments” is beneficial.
58. The value ascribed to the additional disclosure by the auditor varied considerably among the survey respondents. On balance certain key user groups—including regulators and oversight bodies—believe these additional disclosures provide useful information. The following are among the perceived benefits of such disclosures:
- They complement the current binary form of the auditor’s opinion and enhance the communicative value of the auditor’s report even when the auditor’s report is unqualified;
 - They serve as a useful filter for reading the financial statements, which in many cases are viewed as having become “unreadable;”
 - They meet the needs of users for more information, for example by serving as an alert to readers by highlighting specific areas of the financial statements, and focusing readers’ attention on more subjective areas of the financial statements that, are of interest, even if they do not give rise to a modification of the auditor’s opinion; and
 - They enable the auditor to better explain what the audit involved, and what areas were of concern.
59. The survey also pointed to some areas of difficulty and challenge in using these disclosures, for example:

- They may not be readily understandable to less-knowledgeable users of audited financial statements because they typically use technical language that is only able to be fully appreciated by persons with appropriate background in financial reporting and auditing; and they sometimes are complex to read;
 - They may become standardized (or boilerplate) over time in relation to an entity; and the way they are presented in the report may detract from the readability of the auditor’s report;
 - Auditors tend to view them as increasing their exposure to liability; and
 - Auditors need to be careful not to provide information about the entity that has not been disclosed by the entity itself—and averting that situation typically requires more extensive dialogue with the entity’s management and audit committee about the disclosures the auditor intends to make in the auditor’s report.
60. In summary, from feedback available the French auditor reporting model would seem worthy of consideration as an existing model of reporting that can be used as a reference to further develop the ISAs on auditor reporting.

Use of “Emphasis of Matter” and “Other Matter” Paragraphs in the SAR

61. ISA 706,⁵ revised in 2007, already provides for auditors to draw matters to users’ attention through additional communications in the auditor’s report. The auditor may draw users’ attention, when in the auditor’s judgment it is necessary to do so, to:
- (a) A matter, although appropriately presented or disclosed in the financial statements, that is of such importance that it is fundamental to users’ understanding of the financial statements; or
 - (b) As appropriate, any other matter that is relevant to the users’ understanding of the audit, the auditor’s responsibilities or the audit report.
62. In developing ISA 706, there was much deliberation about encouraging such additional commentary while balancing the risk that too much “other” reporting would either (a) lose impact or (b) become boilerplate over time. Equally important was to ensure that the additional information or commentary would in no way undermine the effectiveness of the auditor’s communication of the opinion on the financial statements. There is a risk that excessive “other reporting” might cause the report to be ambiguous, or confuse readers as to what the auditor’s opinion is on the financial statements.
63. Furthermore there is some research evidence pointing to the fact that the use of Emphasis of Matter and Other Matter paragraphs by auditors to report additional information of significance is widely misunderstood. The evidence is that such disclosures are typically viewed by readers as being “negative,” and therefore equated with qualification of the audit opinion.

⁵ ISA 706, *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor’s Report*

Some Areas of Challenge Regarding the Provision of Auditor Commentary

64. It is generally recognized, as a matter of principle, that the auditor is not responsible, and should not take responsibility, for disclosure of information about the entity to the entity’s external stakeholders. Of necessity, that must remain the responsibility of management and those charged with governance, not only to preserve the effectiveness of the independent audit function but also in the interest of preserving clarity about the responsibilities and boundaries associated with these roles, respectively. There is considerable risk to undermining the effectiveness of both the corporate reporting function and the independent audit function if users were to be faced with the challenge of dealing with competing sources of information about the entity (characterized as a situation where users are faced with “dueling sets of information”).
65. Accordingly, reporting by the auditor (in the form of additional commentary, or otherwise) on matters that are not reported on by the entity itself, especially on matters unrelated to auditor’s opinion on the financial statements, may give rise to a number of impediments or challenges, including the following:
 - Development of suitable criteria to enable reporting on an objective and transparent basis;
 - Practical challenges, e.g., due to the scope for conflict with provisions of national law and regulation concerning privacy, confidentiality, or market disclosure rules, and due to additional liability exposure; and
 - Ultimately, addressing the risk of undermining the audit function itself, for example in respect of the independence of the auditor, or in respect of the effectiveness of the audit process (e.g., if performance of the audit is affected by loss of ability to communicate openly with management and with the audit committee).

Questions

3. Do respondents believe that addressing the possible areas of change described above will assist in bridging the perceived information gap? If not, please explain why not, and what alternative avenues you recommend the IAASB should consider.
4. If respondents believe the SAR should be expanded to include additional commentary by the auditor, what criteria should serve as the basis for auditors to provide such commentary? Should there be limits for the auditor’s role in providing commentary and, if so, what should the limits be?
5. Regarding additional information about the audit, as outlined in paragraph 53:
 - (a) Which of these matters are of highest importance to users?
 - (b) What challenges or obstacles exist for providing this information to users?

B. Auditor Reporting on Other Information in Documents Containing Audited Financial Statements

66. Investors have pointed to the need to have various types of additional information about the entity to enable better decision making. Some examples are information about the entity’s:
- Governance arrangements;
 - Business model, including the sustainability thereof;
 - Risk management; and
 - Internal controls and financial reporting processes.

The entity’s financial report may cover some of these areas in the narrative section of the report.

67. There have been calls for the auditor of the entity’s financial statements to also report on the narrative section of the entity’s financial report, which the auditor’s opinion currently does not cover. Users have said this would enhance the usefulness of the narrative information.
68. Under extant ISAs, the auditor is required to read other information in documents that contain the audited financial statements, and to react in the event the auditor considers there are significant inconsistencies between the other information and the financial information reflected in the financial statements, or if there are any material misstatements of fact in the other information.⁶ The auditor’s reactions may extend to providing additional commentary in an Other Matter paragraph included in the report that will describe the inconsistency for the benefit of users of the financial statements, if the inconsistency is not appropriately addressed by management.
69. In some countries auditors are required to go a step further and include, as part of the report on the audited financial statements, a statement as to whether the auditor has anything to report regarding the consistency of the other information with the audited financial statements. This statement is made pursuant to the auditor’s responsibilities to audit the financial statements and accordingly does not involve additional work effort by the auditor—the auditor’s statement as to the other information is thus a derivative report, rather than a separate report of the auditor. Currently, it does not extend to expression of any opinion or conclusion on the other information.
70. There has also been a suggestion by users that the other information should be the subject of assurance reporting by the auditor (that is, where the auditor would express either an opinion or a conclusion on that information). Although there is appealing to users, it

⁶ ISA 720, *The Auditor’s Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements*, is currently under revision by the IAASB. This standard addresses the auditor’s work effort applied to the examination of other information included in documents that contain audited financial statements, pursuant to the financial statement audit. The project is exploring also whether a revised standard should apply also to other information that accompanies audited financial statements—which, in the context of this consultation, would widen the scope of auditor reporting in this area.

would present some challenges in practice. The narrative section of financial reports often includes information of a type not always susceptible to verification in the same sense as financial information contained in financial statements. Nevertheless, the possibility of auditors providing assurance on some or all of this information can be further explored.

71. In summary, the IAASB believes there is an opportunity to explore:
 - (a) As part of the auditor’s report on the audited financial statements, including a form of mandatory statement by the auditor about other information disclosed in documents that contain audited financial statements; and
 - (b) As a form of separate assurance reporting, appropriate forms of assurance reporting on narrative information disclosures (either in documents that contain audited financial statements, or in documents that accompany the audited financial statements).
72. The IAASB is already pursuing a number of initiatives to develop assurance reporting on non-financial statement subject matter as part of its current standard-setting work program. If assurance reporting were to be done for the narrative section of financial reports, that would require acceptable disclosure models to be applied in preparing that section of the report, which could be used by the auditor to evaluate it.
73. If responses to this consultation provide a strong indication that development of a model of assurance to address narrative information disclosures is a high priority, that may be considered as a further strategic initiative of the IAASB. The IAASB is currently undertaking a public consultation to develop its future strategy for 2012–2014,⁷ and feedback about the need to further develop assurance reporting in this area would be helpful if respondents believe that is the case.

Questions

6. Do respondents believe that addressing the possible areas of change described above will assist in bridging the perceived information gap? If not, please explain why not, and what alternative avenues you recommend the IAASB should consider.
7. If respondents believe the SAR should require a form of mandatory statement by the auditor concerning other information in documents that contain audited financial statements, what should the form of such a statement be?
8. Do respondents believe there is need for assurance reporting on narrative information disclosures in documents that contain audited financial statements, or in documents that accompany audited financial statements?

⁷ The IAASB is currently undertaking an extensive public consultation on its future strategy and work program through the IAASB Consultation Paper [*Proposed Strategy and Work Program for 2012–2014*](#), released in January 2011. The Consultation Paper suggests priority activities for the IAASB during 2012–2014, including among other things with regard to supporting development of new and emerging assurance services. The consultation is until April 4, 2011.

C. Possible Changes to the Structure, Format and Content of the SAR

74. Not least in scope of the possible ways to change the auditor’s report for the better are various options that it is thought would improve the readability and understandability of the report for readers.
75. The types of things that seem to warrant attention here are:
 - (a) Better presentation, or better positioning of the generically-worded content of the report that appear as standardized paragraphs in every auditor’s report;
 - (b) Addressing the lack of common meaning of various technical terms that are used in the auditor’s report; and
 - (c) Clarity of communication of the auditor’s opinion on the financial statements.
76. These areas of possible change are discussed below, and the illustrations provided in Appendix 1 show how these changes might affect the structure and presentation of the SAR if they were to be taken further.

Generic Description of Management and Auditor Responsibilities

77. Currently the auditor’s opinion is presented towards the end of the SAR. The opinion is preceded by an introductory paragraph that identifies, *inter alia*, the financial statements that have been audited, and by paragraphs describing management’s and the auditor’s responsibilities. These paragraphs are intended to provide readers with contextual information important to the readers’ proper understanding of the auditor’s opinion.
78. Research on user perceptions of the auditor’s report points to a widely-held view that the generically worded explanatory information that is standard to all audit reports is not particularly useful. The information cited is that which describes the respective responsibilities of management and the auditor, and the nature and scope of the audit. Many readers view these elements of the report as “boilerplate,” and having no information content for readers.
79. Options suggested are that these paragraphs could be either: (i) removed entirely or, alternatively, replaced by a reference to where such information could be accessed; or (ii) reduced as far as possible; or (iii) retained, but expanded to make them more informative.
80. The idea of an “opinion only” auditor’s report has also been suggested, reflecting research evidence that readers do not perceive any information value in any content of the report other than the opinion expressed. It also implies that the other information contained in the auditor’s report does little if anything to bridge the expectation gaps that surround the financial statement audit.
81. Removing the explanatory material entirely from the report would logically require the acceptance that readers are already sufficiently well-informed about the matters addressed. Evidence suggests this is generally not the case, even in respect of sophisticated users.
82. An alternative would be to relocate the explanatory material to another separate document that can be used communicate about the financial statement audit with users. Such a document, devoted solely to communication of such matters, could be made available

electronically in a publicly accessible online location. Such a model is already being used by the Auditing Practices Board (APB) in the UK.⁸

83. There are compelling reasons, however, for retaining explanatory paragraphs in the report from an international perspective. Among others things, it enables the audit report to be stand-alone, the importance of which may vary depending on the national liability regime. Importantly, it promotes use of internationally consistent communications about the audit.
84. In seeking a balanced response, a possible solution may be to retain the material but position it at the end of the report, or as appendix thereto, while ensuring that it should be understood to be an integral part of the report. This may assist in enhancing the readability of the report while retaining what many view as essential contextual information. It also may facilitate expansion or other modifications of the material (discussed below with regard to the need for explanations of technical language used in the report), while not disrupting the overall balanced readability of the report.

Use of Technical Language in the Auditor’s Report

85. There have been also calls for the wording used in auditor’s reporting to be less technical, and more understandable to lay readers. The root problem would appear to be that technical words appear to lack a common meaning for users who read the report. This problem seems to be especially present in the explanations of the respective responsibilities of management and the auditor, and the nature and scope of the audit.
86. Terms noted as lacking a common meaning for readers include:
 - “fair presentation” or “true and fair view.”
 - “materiality” and “material misstatement.”
 - “reasonable assurance.”

These terms are germane to the auditing function, yet equally important to user understanding.

87. Related, some have pointed to aspects of the audit where a continuing expectation gap exists, and where the current style of report does not provide readers adequate information to enable them to understand fully the context of the auditor’s opinion, in particular:
 - (a) The auditor’s responsibility with respect to fraud in the financial statement audit;
 - (b) The auditor’s compliance with ethical requirements or matters that bear on the auditor’s independence; and
 - (c) The responsibilities of management and those charged with governance of the entity regarding the financial statements, including disclosure of information sufficient to

⁸ In the UK, auditors have the option, in consultation with audited entities if applicable, to remove the paragraphs containing generic explanations about the audit from the auditor’s report. If this option is used the auditor’s report is to instead contain a reference to where this information can be read on the APB’s website—see www.frc.org.uk/apb/scope/private.cfm.

enable a proper understanding of the context of the financial information presented in the entity’s audited financial statements.

88. There may be merit in exploring whether brief but useful further explanations of technical terms and elaboration of aspects of an audit, provided as part of the explanatory paragraphs of the audit report, could be made to assist readers’ understanding of the report. A critical consideration in exploring the above, however, will be the extent to which further explanation assists or hinders understandability, and also legal implications that may be associated with use of additional wording.
89. There is also likely to be merit in investing effort in the development of appropriate educational material that can be made available to users in some easily accessible way.

Communication of the Auditor’s Opinion

90. Some commentators have expressed a preference for the auditor’s opinion to be given greater prominence in the SAR. In many cases, the opinion is what readers first seek to ascertain when they read the report.
91. One option that has been suggested is for the opinion to be presented first in the report. Others argue for the opinion to be positioned so that it will be read with appropriate context. However, the need to do so may be alleviated by the possible changes contemplated regarding the placement of explanatory material in the auditor’s report.

Questions

9. Do respondents believe that addressing the possible areas of change described above will assist in bridging the perceived information gap? If not, please explain why not, and what alternative avenues you recommend the IAASB should consider.
10. Do respondents believe the generically-worded standard explanatory paragraphs contained in the SAR should be either (a) moved to an accessible place outside the auditor’s report, or (b) be retained in the report, but moved to the end of the report (as shown in Appendix 1, Illustration 2)?
11. If respondents believe it is important to explain technical language used in the auditor’s report, would that best be achieved by providing explanations of those terms as part of an explanation of the audit, per the suggestion in paragraph 88?
12. Do respondents have a view about whether the auditor’s opinion should be presented first in the report, before the other content (but after the identification of the financial statements that have been audited)?

IV. An Enhanced Role for the Audit Committee regarding Financial Reporting and the External Audit

92. Resolving the information gap more comprehensively than might be done under the suggestions discussed in Section III would likely require changes that go beyond changes to auditor reporting.

93. As noted earlier in the paper, the general principle followed in law and regulation on corporate financial reporting and other types of corporate disclosures is that information about the entity that is to be reported to the entity’s external stakeholders should be originated by management, or those charged with governance as appropriate. There are important reasons why the auditor should not usually be the originator of information about the entity—among those being that it is fundamental to the effectiveness of the independent audit function.
94. Reporting by the auditor is generally limited to reporting on information about the entity as disclosed by management or those charged with governance for the benefit of the entity’s shareholders and other external stakeholders. Direct reporting of new information by the auditor only occurs in certain prescribed circumstances, for example when specifying details of a necessary adjustment to the financial statements as part of an audit report qualification.
95. As noted in Section III, under extant auditing standards the auditor is required to provide information to external stakeholders in certain clearly defined situations. These are firstly when modifying the auditor’s report, for example when providing a qualified opinion on the financial statements. Secondly, the auditor may decide that certain matters require additional emphasis in the auditor’s report—even when those matters are correctly presented and disclosed in the audited financial statements, if the auditor considers those matters fundamental to users’ understanding of the audited financial statements. As explained in Section III, the possibility may exist to further develop the auditor’s reporting role in the latter situation.
96. Many users have drawn attention to the situation where management or those charged with governance of the entity may not have adequately discharged their reporting role, in the sense that there is information about the entity that has not been sufficiently or properly disclosed for users to be able to properly understand the financial information provided by management or those charged with governance—albeit that the entity has apparently complied with the applicable financial reporting framework in its financial statements. This aspect of the information gap would seem to warrant attention.
97. An important area where further development should be encouraged lies within the corporate reporting model itself. If this line of thinking is followed, the degree of development of the entity’s corporate governance reporting function becomes relevant.
98. Specifically the question of the audit committee’s role in reporting to external stakeholders of the entity deserves more emphasis, because the audit committee plays an important oversight role in respect of the entity’s financial reporting and external audit.
99. In this respect the audit committee is a key part of the entity’s interaction with the entity’s shareholders and other external stakeholders. In some countries the audit committee’s role is clearly specified as being one of stewardship regarding the interests of the entity’s shareholders—which establishes a clear line of responsibility for proper communication with that class of stakeholder.
100. It has to be acknowledged, however, that the role of audit committees or their equivalent as described under different national law and regulation, or governance codes, will vary and possibly quite significantly, in different national settings. Audit committee functions have tended to develop differently in different countries. In some countries, for example the UK

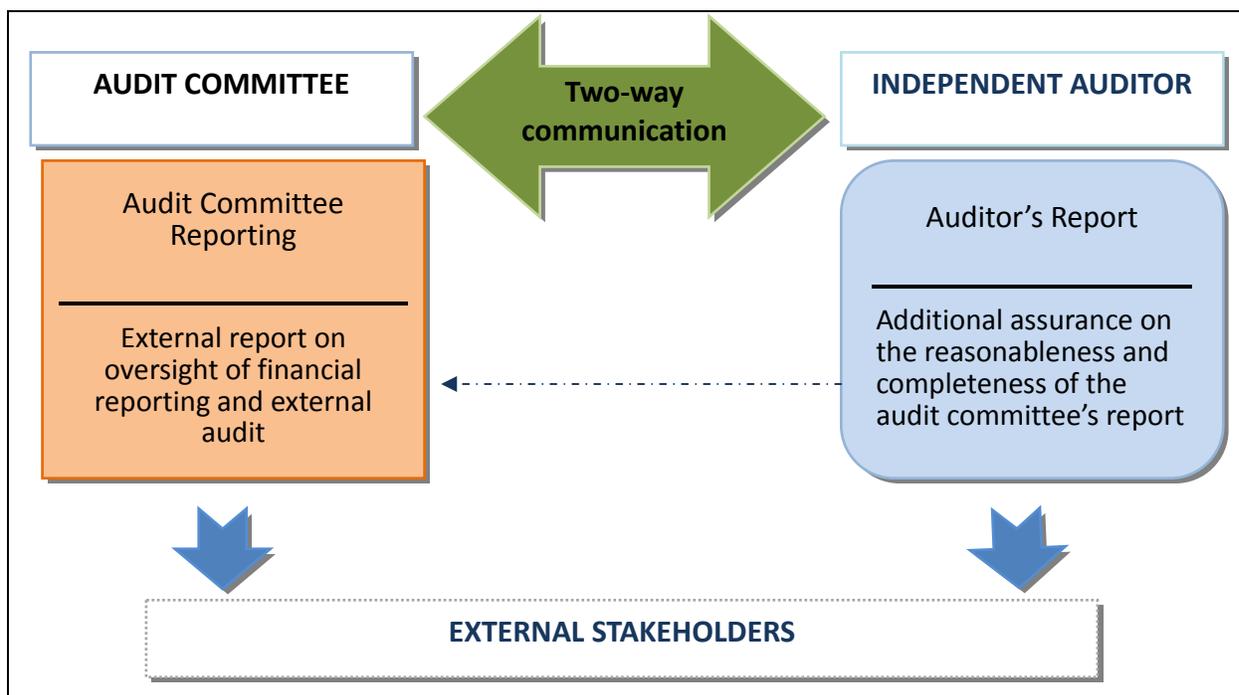
and the US, corporate governance oversight of the entity’s financial reporting to external stakeholders, and of the external audit, is undertaken under the audit committee’s formal mandate. However, in many other countries, the audit committee function, and its external reporting capacities or responsibilities, may be relatively underdeveloped.

101. Furthermore, there seems to be no globally accepted standards or guidance that would serve as benchmarks for the design of the audit committee role in corporate governance functions.⁹ Many commentators in recent debates have recognized this as a further problem area that needs addressing.
102. The existing interaction that occurs between the auditor and the audit committee of an entity offers a platform for further development of audit committee’s external reporting capacity. Diagram 2 below illustrates communication flows that occur between:
 - (a) The audit committee and the auditor (required under auditing standards, on a two-way basis);
 - (b) The audit committee and the entity’s shareholders and other external stakeholders; and
 - (c) The independent auditor and the entity’s shareholders and other external stakeholders.
103. In the context of the wider debate about resolving the information gap, there would seem to be a need for priority attention to be given to strengthening corporate governance reporting mechanisms to ensure, in respect of the entity’s external information disclosure processes and practices, the information gap can be addressed also through the channel of the audit committee.
104. This is a logical course of action if the intention is for the responsibilities of the auditor and those of management and those charged with governance, respectively, to remain as currently specified in most countries, with the entity’s audit committee carrying out the key oversight role.
105. In the UK, the Financial Reporting Council (FRC) has proposed a new model for reporting by the audit committee of an entity that would include an expanded form of auditor reporting. The proposal is for the entity’s audit committee to publicly report to external stakeholders on the approach it has taken to discharge its responsibility regarding the integrity of the entity’s annual report and oversight of the external audit process. This reporting is intended to extend to disclosure of such information about the entity and about the audit performed as is necessary, in the audit committee’s view, for users to be able to understand the entity’s financial report, including the audited financial statements, and the result obtained from the audit of those statements. The second part of the proposal is for an expanded auditor’s report that would include a new section where the auditor reports on the completeness and reasonableness of the audit committee’s report.

⁹ As an example of one initiative, the International Corporate Governance Network has endorsed enhanced disclosure guidelines for board and others developed by the Global Auditor Investor Dialogue—available at www.enhanceddisclosure.org.

106. This reporting model may be shown in visual terms, as follows:

Diagram 2: Audit Committee Reporting Model



107. The required communications between the auditor and those charged with governance or the audit committee, ordinarily include reporting by the auditor to the audit committee, about the audit performed on the financial statements, including information about the audit risks identified, the audit effort applied and the results thereof, and key audit findings. This may also be a legal requirement in some countries but, where it is not, such reporting by the auditor is increasingly done on a formal basis to provide information relevant to the audit committee’s oversight role for financial reporting and the external audit.

108. The approach of placing a priority on strengthening the model of communication and reporting to external stakeholders through the entity’s audit committee is important for the following reasons:

- (a) It reinforces the entity’s responsibility for full and proper information disclosure to external stakeholders, as a matter of good governance; and
- (b) It recognizes the importance of preserving the auditor’s role, being to provide independence assurance on the entity’s financial statements to enhance its credibility for third parties.

If the auditor’s role were to become blurred with that of management or those charged with governance, then the unique value of the audit in providing an independent opinion about the entity’s information would be undermined.

109. Accordingly, an enhanced role for the entity’s audit committee in corporate information disclosure and communications with external stakeholders should be viewed as an important pillar in efforts to address perceived information gaps. This model is able to be used with the current auditor reporting model, and with an enhanced auditor reporting model as discussed in Section III.
110. Following the FRC’s proposal in its recent public consultation, the model should include auditor reporting on the audit committee’s reports to external stakeholders. Whether or not such reporting would be feasible in the auditor’s report on the entity’s financial statements would require further reflection based on a number of factors, including the timing of such reporting *vis-à-vis* the timing of the completion of the financial statement audit.

Questions

13. Do respondents believe that corporate governance reporting (for example, through an entity’s audit committee) should be further developed as part of a more holistic approach to addressing the perceived information gap? If not, please explain why not.
14. Do respondents consider that anticipated beneficial effects of enhanced auditor reporting as described in Section III can be further leveraged if an audit committee reporting model is used, in addition?

V. Consideration of the Potential Impact Associated with Possible Areas of Change

111. This section aims to draw out respondents’ views about the potential effects and implications or challenges associated with:
 - (a) The possible avenues of change for enhancing auditor reporting identified in Section III; and
 - (b) The development of an enhanced model of corporate governance reporting explained in Section IV.
112. It is useful, as part of this consultation, to consider these options for change in light of their anticipated effects, implications or challenges for preparers and auditors, and also for users. It is expected that views on these matters will differ widely among these different groups.
113. An assessment of possible future courses of action relating to standard setting by the IAASB should be informed, on a preliminary basis, by respondents’ views about these issues. In analyzing responses obtained from this consultation, the IAASB will seek to evaluate whether the possible areas of change for auditor reporting outlined in Section III above seem viable, and are generally supported as avenues worthy of further consideration with reference, in particular, to respondents’ views about their likely effects and implications and also associated challenges.
114. A key consideration for evaluating the viability of possible areas of change is the impact on audit effectiveness and on audit quality (either real or perceived). A significant body of respondents to the recent European Commission’s Green Paper on Audit Policy

emphatically made the point that change proposals should clear the figurative hurdle of being in line with the goal of enhancing the quality of audits.

115. Accordingly, it will be important to understand what the likely impact of these potential changes would have on the effectiveness of the financial statement audit. This is a threshold question. If there contrary effects or implications are likely, so that the audit itself would be undermined, either in fact or in perception, there would be no point in further considering any areas where that consequence seems likely or where adverse effects are unable to be effectively mitigated.
116. The IAASB sees an element of potentially strong complementarity between the suggested areas of change described in Sections III and IV. It seems intuitively obvious, however, that the areas of change described in Section III may be able to be advanced in an earlier timeframe. The IAASB considers that the suggested areas of change in relation to auditor reporting, if pursued, would have enduring benefit and retain usefulness even if one or more models of enhanced corporate governance reporting or disclosure were to take form in a manner that would achieve general recognition as an internationally accepted benchmark for such reporting.
117. Nevertheless the IAASB considers it important to obtain an initial understanding about respondents’ views on the extent of any likely difficulties or areas of challenge there may be in moving towards an enhanced corporate governance/audit committee reporting model. It would be most efficient if any future standard-setting activities in relation to auditor reporting were able to be designed to accommodate that model if were to appear likely that it would be advanced as a broader initiative across a number of countries or jurisdictions.

Respondents are requested to:

- (a) **Provide views and feedback about potential effects, implications or challenges associated with:**
 - (i) **Possible areas of change for enhancing auditor reporting described in Section III; and**
 - (ii) **Development of an enhanced model of corporate governance reporting/audit committee reporting described in Section IV.**
- (b) **Rank each of the possible areas of change described in Section III (sub-sections A–C) and Section IV in the order (highest to lowest) that respondents believe would be most likely to enhance the relevance and usefulness of auditor reporting to users, keeping in mind the potential effects, implications or challenges in each case.**

Appendix 1

Illustrations of Possible Areas of Changes to the Standard Auditor’s Report

(Refer to Section III of this Consultation Paper)

Illustration 1: Current Standard Auditor’s Report

INDEPENDENT AUDITOR’S REPORT
 [Appropriate Addressee]
Report on the Financial Statements
 We have audited the accompanying financial statements of ABC Company, which comprise the balance sheet as at December 31, 20X1, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management’s Responsibility for the Financial Statements
 Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor’s Responsibility
 Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity’s preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
 In our opinion, the financial statements present fairly, in all material respects, (or *give a true and fair view of*) the financial position of ABC Company as at December 31, 20X1, and (of) its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Emphasis of Matter
 We draw attention to Note X to the financial statements which describes the uncertainty related to [describe matter(s)]. Our opinion is not qualified in respect of this matter.

Report on Other Legal and Regulatory Requirements
 [Form and content of this section of the auditor’s report will vary depending on the nature of the auditor’s other reporting responsibilities.]
 [Auditor’s signature]
 [Date of the auditor’s report]
 [Auditor’s address]

Possible Areas of Change

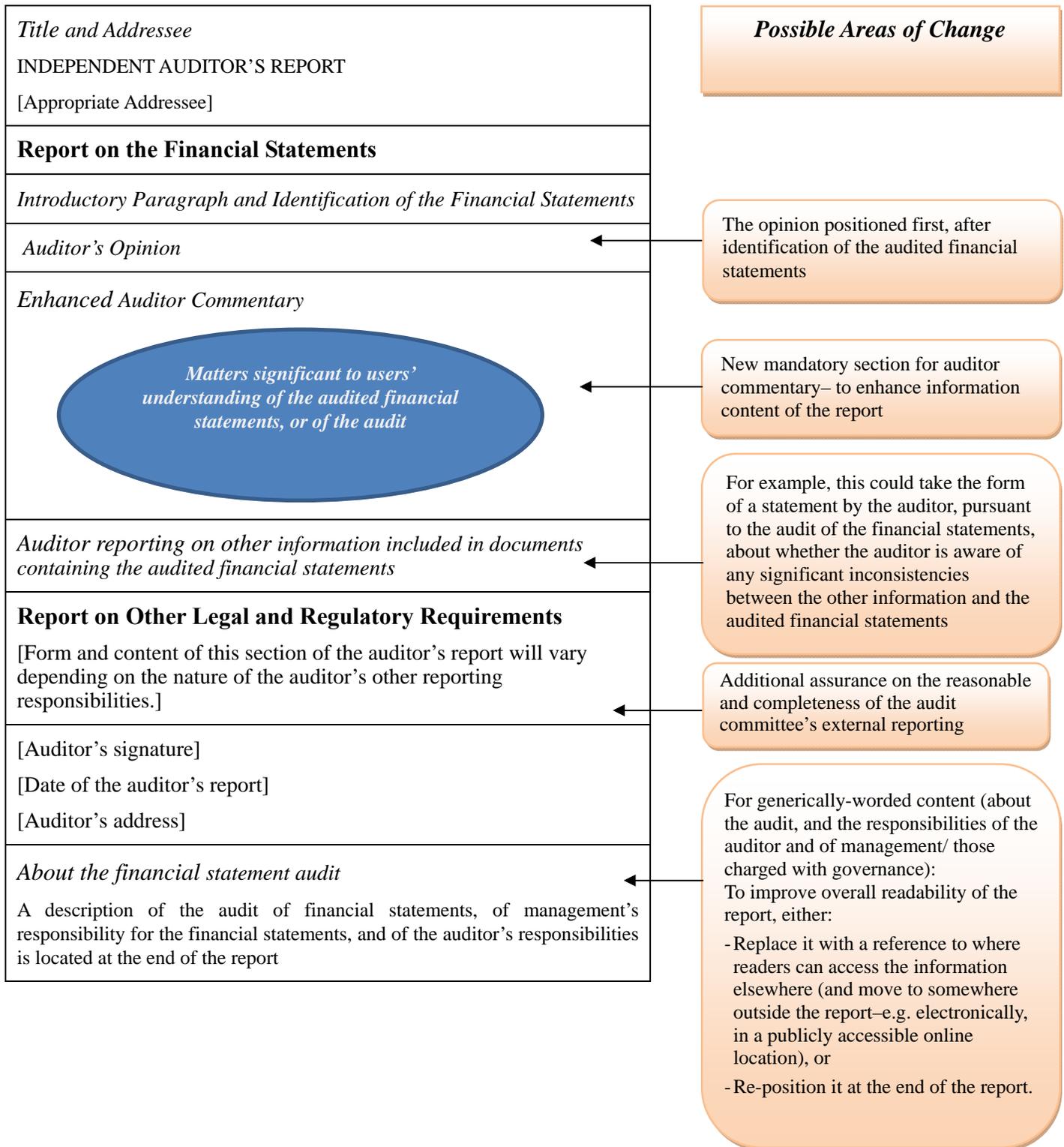
- i) Remove generically worded content of the standard auditor’s report, or
- ii) Move it to another location, either within the report (e.g., at the very end), or somewhere else where it will be easily accessible to readers (e.g. in electronic form)
 See paragraphs 77-84

Additional commentary by the auditor the emphasize matters that the auditor considers are significant to users’ understanding of the audited financial statements, or of the audit, the audit process or the auditor’s responsibilities.
 See paragraphs 49-65

Present the auditor’s opinion first in the report, after identification of the financial statements. This would make it more prominent—clearer communication of the opinion.
 See paragraphs 90-91

Additional reporting by the auditor on other information contained in documents that contain the audited financial statements.
 See paragraphs 66-73

Illustration 2: A Possible Enhanced Structure for the Standard Auditor’s Report



Appendix 2

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¹⁶ www.iosco.org/library/pubdocs/pdf/IOSCOPD337.pdf

¹⁷ www.parliament.uk/business/committees/committees-a-z/lords-select/economic-affairs-committee/publications/

¹⁸ pcaobus.org/News/Events/Documents/02162005_SAGMeeting/Auditors%20Reporting%20Model.pdf

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¹⁹ pcaobus.org/News/Events/Documents/04072010_SAGMeeting/Auditor%27s_Reporting_Model.pdf

²⁰ pcaobus.org/News/Events/Documents/10132010_SAGMeeting/ACAP_Briefing_Paper.pdf

²¹ Available from the Australian Auditing Standards Board: www.auasb.gov.au/Home.aspx

²² www.treas.gov/offices/domestic-finance/acap/index.shtml, www.ustreas.gov/offices/domestic-finance/acap/docs/final-report.pdf.

Appendix 3

List of Questions in this Consultation Paper

The Information Gap, and Exploring Channels for Communication with an Entity’s External Stakeholders

1. Do respondents believe the discussion of the perceived information gap in Section II is a fair reflection of the issues?

Enhancing Auditor Reporting—Possible Areas to Explore

2. Do respondents support the approach and rationale applied in setting the focus of this consultation on addressing the areas mentioned in paragraph 48, as possible areas to explore to enhance auditor reporting?

Auditor Commentary on Matters Significant to Users’ Understanding of the Audited Financial Statements, or of the Audit

3. Do respondents believe that addressing the possible areas of change described above will assist in bridging the perceived information gap? If not, please explain why not, and what alternative avenues you recommend the IAASB should consider.
4. If respondents believe the SAR should be expanded to include additional commentary by the auditor, what criteria should serve as the basis for auditors to provide such commentary? Should there be limits for the auditor’s role in providing commentary and, if so, what should the limits be?
5. Regarding additional information about the audit, as outlined in paragraph 53:
 - (a) Which of these matters are of highest importance to users?
 - (b) What challenges or obstacles exist for providing this information to users?

Auditor Reporting on Other Information in Documents Containing Audited Financial Statements

6. Do respondents believe that addressing the possible areas of change described above will assist in bridging the perceived information gap? If not, please explain why not, and what alternative avenues you recommend the IAASB should consider.
7. If respondents believe the SAR should require a form of mandatory statement by the auditor concerning other information in documents that contain audited financial statements, what should the form of such a statement be?
8. Do respondents believe there is need for assurance reporting on narrative information disclosures in documents that contain audited financial statements, or in documents that accompany audited financial statements?

Possible Changes to the Structure, Format and Content of the SAR

9. Do respondents believe that addressing the possible areas of change described above will assist in bridging the perceived information gap? If not, please explain why not, and what alternative avenues you recommend the IAASB should consider.
10. Do respondents believe the generically-worded standard explanatory paragraphs contained in the SAR should be either (a) moved to an accessible place outside the auditor’s report, or (b) be retained in the report, but moved to the end of the report (as shown in Appendix 1, Illustration 2)?
11. If respondents believe it is important to explain technical language used in the auditor’s report, would that best be achieved by providing explanations of those terms as part of an explanation of the audit, per the suggestion in paragraph 88?
12. Do respondents have a view about whether the auditor’s opinion should be presented first in the report, before the other content (but after the identification of the financial statements that have been audited)?

An Enhanced Role for the Audit Committee Regarding Financial Reporting and the External Audit

13. Do respondents believe that corporate governance reporting (for example, through an entity’s audit committee) should be further developed as part of a more holistic approach to addressing the perceived information gap? If not, please explain why not.
14. Do respondents consider that anticipated beneficial effects of enhanced auditor reporting as described in Section III can be further leveraged if an audit committee reporting model is used, in addition?

Consideration of the Potential Impact Associated with Possible Areas of Change

Respondents are requested to:

- (a) Provide views and feedback about potential effects, implications or challenges associated with:
 - (i) Possible areas of change for enhancing auditor reporting described in Section III; and
 - (ii) Development of an enhanced model of corporate governance reporting/audit committee reporting described in Section IV.
- (b) Rank each of the possible areas of change described in Section III (sub-sections A–C) and Section IV in the order (highest to lowest) that respondents believe would be most likely to enhance the relevance and usefulness of auditor reporting to users, keeping in mind the potential effects, implications or challenges in each case.