



November 22, 2013

Mr. James Gunn
Technical Director
International Auditing and Assurance Standards Board
International Federation of Accountants
529 Fifth Avenue – 6th Floor [confirm address]
New York, NY 10017
U.S.A.

Dear Mr. Gunn,

Re: Exposure Draft Reporting on Audited Financial Statements

The Canadian Auditing and Assurance Standards Board (AASB) is pleased to provide its comments on the Exposure Draft (ED) *Reporting on Audited Financial Statements*. In developing our response, we considered comments provided to us by our stakeholders who showed a strong interest in this topic. We held many face-to-face and conference call meetings with various user groups, including investors, analysts, management, audit committees, directors, regulators, auditors and others, as set out in Appendix 2 to this letter.

General Comments

While our stakeholders have broadly expressed significant concerns about a number of aspects in the proposals, the AASB and many stakeholder support the objective of enhancing the value and relevance of auditor reporting including, as appropriate, enhancing the auditor's report on the financial statements. We also support the development of an auditor reporting model including consistent use of auditor's reports that users around the world can understand, that national standard setters would adopt and that auditors would apply.

In responding to the IAASB's Invitation to Comment *Improving the Auditor's Report*, (ITC) the AASB raised a number of significant concerns based on the input received from Canadian stakeholders. We recognize that in developing the ED the IAASB made improvements compared to the ITC. Accordingly, when consulting with Canadian stakeholders about the ED, the AASB informed Canadian stakeholders about the improvements, auditor reporting developments in other jurisdictions and the potential consequences of adopting or not adopting the proposed

new and revised ISAs in Canada. While Canadian stakeholders are strongly supportive of the AASB continuing to adopt ISAs as Canadian Auditing Standards (CASs), they raised a number of broadly shared significant concerns about the proposals in the ED. The AASB is extremely troubled about adopting proposals that are still causing concerns to key elements of our stakeholder community solely to maintain our commitment to adopting ISAs as CASs. Therefore, we strongly encourage the IAASB to consider the recommendations noted below, and in our response to the questions in the ED set out in Appendix 1 to this letter, as they will, in our view, provide a basis to allow the final auditor reporting standards to be operational in the Canadian environment.

The following are significant points we would like to bring to your attention:

1. The applicability of the proposed Key Audit Matters (KAM) requirements
2. Achieving consistency in reporting of KAM
3. The approach to reporting on going concern
4. The need for consistency of reporting requirements of the IAASB and the United States Public Company Accounting Oversight Board (PCAOB)
5. The effective date of the final standards

1. The applicability of the proposed KAM requirements

The applicability of the proposed KAM requirements is a key concern for Canadian stakeholders. Comments focused on the proposed split between listed/other than listed entities and the appropriateness of this split in a Canadian context. Of concern to many Canadian stakeholders is the proposal that KAM be required for “listed entities”. Stakeholders support limiting the scope of the KAM requirements (as discussed in paragraph 54 of the Explanatory Memorandum). Reporting KAM is a new concept in most jurisdictions and allowing a period of experience will be important before considering whether it is necessary to expand the requirements to other entities or to address areas for improvement of the standards. However, stakeholders believe that the prescription that KAM be required for audits of financial statements of “listed entities” is problematic in a Canadian context.

1. On the one hand, we believe that requiring auditor’s reports on the financial statements of all listed entities to include KAM is too broad a requirement because of the nature of the Canadian listed entity marketplace. The Canadian market is segmented into the TSX (approximately 1,500 issuers of which nearly 10% have a market capitalization of less than \$10 million), and the TSXV (approximately 2,000 issuers of which nearly 75% have a market capitalization of under \$10 million, are in the resource sector and in start-up mode). Stakeholders highlight that there are a limited number of companies in Canada of a sufficient size that institutional investors and analysts are actively following them; and it is institutional investors and analysts who are expected to benefit most from the reporting of KAM.

There are significant differences between the needs of users of financial statements in the different market segments in Canada. Participants in the TSXV market indicated that given the nature of many of these entities and their often limited financial resources, requiring KAM may add cost with limited benefits for investors. In addition, investors and other users of the financial statements of many early stage resource and other companies listed on the TSXV place greater emphasis on reserve reports from experts and other reporting on future prospects of the commercial success of the company in making investment decisions. Accordingly, some questioned whether such a requirement would be in the public interest given what they see as the potential adverse consequences for economic development of imposing an additional burden on the auditors, preparers and audit committees of such entities.

2. On the other hand, we believe the requirement for auditors to include KAM in their reports on the financial statements of listed entities would exclude certain Canadian entities that would otherwise be treated similarly to listed entities in terms of regulatory and accounting requirements, such as financial institutions that are not listed entities.

There are a number of other terms in general usage in Canada, whether in securities and other legislation or regulation and accounting standards, such as “reporting issuer”, “publicly accountable enterprise”, and “market participant”. There is no one term that we could recommend that appropriately addresses our concerns.

On the assumption that other jurisdictions may also have similar concerns to those identified in Canada, we believe the application of KAM to all listed entities needs to be reconsidered.

We recommend the IAASB change the scope of application of the KAM requirements to require KAM for audits of the financial statements of listed entities but also provide national standard setters with the flexibility to add to or subtract from the audits covered by the requirement. This might be accomplished by revising paragraph 30 of proposed ISA 700 as follows:

Key Audit Matters

30. For audits of complete sets of general purpose financial statements of a listed entity, other than those listed entities specifically excluded by the national standards setter in a jurisdiction, the auditor shall communicate key audit matters in the auditor’s report in accordance with proposed ISA 701....

Application material to support this requirement could be provided along the following lines:

In some jurisdictions, the term “listed entity” may result in the inclusion of entities for which the disclosure of key audit matters is of limited value to stakeholders. Alternately, there may also be entities that are not listed but for whom disclosure of key audit matters is of significant interest to stakeholders. In order to accommodate these jurisdictional differences, national standard setters are permitted to make specific inclusions or exclusions to the entities for which auditors are required to communicate key audit matters

in the auditor's report on their general purpose financial statements without affecting the ability of auditors to state that the audit was conducted in accordance with International Standards on Auditing.

A conforming amendment to paragraph 4 of proposed ISA 701 would also be required.

We believe that this approach will allow national standard setters to define the entities where there will be benefit to having KAM requirements and therefore more consistent KAM reporting.

In the event that the IAASB does not agree with this approach, the AASB believes that another approach should be implemented – develop principles to explain the nature, type and size of entities that the IAASB believes should be included in the reporting requirements rather than using the term “listed entities”. The AASB acknowledges that this approach is less desirable given the challenges the IAASB has already faced in developing a global definition of public interest entities.

2. Achieving consistency in reporting KAM

In discussing the illustrative examples of KAM included in the ED, comments and concerns from users included the following:

- The illustrative examples demonstrate different approaches that might be taken by the auditor in describing a KAM; users questioned what the implications are, if any, when an auditor uses a different approach for some matters than for others, for example including certain audit procedures and a conclusion in some cases but not in others.
- The level of detail provided in an auditor's report will depend on the judgment of each auditor so there is the prospect that two audit reports on two identical companies may look significantly different based on individual auditor perspectives. Users were of the view that lack of consistency could inappropriately affect conclusions they might reach from reading the report.
- There was concern that auditors will likely tend to report the same matters year after year, for example because (a) the auditing standards define the matter as a significant risk (such as revenue recognition), (b) other auditors in the same industry include the matters, or (c) out of fear of their judgments being questioned in the future.
- Some users were of the view that given the expected cost of the proposals and, in their view, the limited value of the information provided in the examples, perhaps a more effective approach would be for KAM to consist of a list of the matters the auditor considered to be of most significance with a reference to the related disclosures (rather than providing further information about audit procedures or conclusions from the auditor's procedures).

We conclude from this that more guidance is needed to help auditors report on a more consistent, meaningful basis. In acknowledging the views of users, we also note that auditors identified complementary concerns in terms of determining what matters to include as KAM

and how to describe such matters in the auditor's report. The AASB also acknowledges the challenges that IAASB faces in addressing these concerns and, in particular, the difficulty in addressing such concerns in advance of practice evolving. We believe, however, that it is desirable to address potential issues in advance of issuing the final standards rather than wait until poor practices emerge and then trying to change behaviour. For this reason, we recommend that the IAASB consider developing new illustrative examples of KAM using the results of the field testing that took place during the exposure period with a view to assisting auditors better apply the proposed standards.

We believe that the results of field testing will assist the IAASB in considering whether the requirements and application material dealing with determining and communicating KAM need to be refined.

In addition, we believe that the IAASB should make changes to the application material in proposed ISA 701 to:

- emphasize that the number of matters to be disclosed is intended to be the matters of most significance in the audit that are ultimately useful to the users of the financial statements so as to limit the number of KAM that are included in the auditor's report;
- prohibit the auditor from providing conclusions or opinions on individual matters as users may take inappropriate assurance on the matters; and
- explain more clearly why one approach to describing a matter may be more relevant than another.

3. The approach to reporting on going concern

Although the IAASB has made improvements to the proposed wording of the going concern statements as compared with the ITC, Canadian stakeholders reiterated concerns they identified when responding to the ITC, namely:

- The statements are confusing and open to misinterpretation by less-informed users, particularly with respect to material uncertainties.
- Management is not currently required under IFRSs to make an explicit statement that it has prepared the financial statements on a going concern basis. Some auditors are concerned that this might confuse users as to the respective roles of management and the auditor with respect to going concern.
- Some auditors believe that the requirements will result in additional cost because making explicit statements in the auditor's report will necessitate greater involvement of senior audit staff and quality control reviewers. It is not clear that such additional work will increase audit quality.
- Public sector auditors are concerned that the proposed going concern wording may not be appropriate in a public sector context (for example, the references to "liquidation" or "ceasing trading", which generally do not apply in a public sector context).
- Users and others also questioned whether the proposals would address the underlying objective of the proposals – to address concerns coming out of the financial crisis.

- Most users and auditors commenting on the going concern proposals believe that the current exception reporting model is more effective in highlighting going concern issues for users than the proposed statements on going concern.

Based on the comments received from our stakeholders, we believe that the proposed statements on going concern will be of limited value to users and could also increase the expectation gap rather than reduce it. We also believe that the IAASB should continue to work with accounting standard setters as part of a holistic approach to reporting on going concern.

We recommend that, as outlined in paragraph 84 of the Explanatory Memorandum, the IAASB defer finalization of reporting on going concern as part of that holistic approach. We understand that such an approach would be consistent with the direction being taken by the PCAOB on this type of reporting.

4. The need for consistency of reporting requirements of the IAASB and the PCAOB

We believe it is important that auditor's reports on the financial statements of companies that operate in a global environment are consistent so that readers are not confused. In particular, because of the significant number of Canadian companies that are listed in the United States, we are supportive of the IAASB working with the PCAOB to reach solutions that will result in similar auditor's reports. For example, if the PCAOB "critical audit matters" requirements are significantly different from the IAASB KAM requirements it could result in auditors of two similar companies that operate in different markets having significantly different auditor's reports. For this reason, we support the IAASB continuing to work together with other bodies that are taking an interest in auditor reporting in their jurisdictions, such as the European Commission and the PCAOB.

5. The effective date of the final standards

We believe that it is preferable to have an effective date that creates a clear delineation between when auditors use the old and new form of report. Given the significance of the proposed changes in the auditor's report, we believe that having different forms of report during the same time period will be extremely confusing to users and serve to create questions about the relative quality of the respective audits which are not justified. An "early adoption is permitted" approach could exacerbate this concern for the same reasons.

We recommend an effective date of periods ending on or after December 14, 2016, with early adoption not permitted, for the following reasons:

- Using a "periods beginning" effective date is problematic because it would result in auditor's reports on financial statement periods shorter than one year (say, January 1,- March 31, 2016) containing auditor's reports under the new standards whereas auditor's reports on financial statements for years ending on the same date (say, the year ending March 31, 2016) would be under the extant ISAs. Using a "periods ending" approach does not affect the fact that auditor's reports for calendar 2016 would be under the new

standards (as would be the case if the effective date were for periods beginning on or after December 15, 2015).

- We believe that audit firms will need time to develop their education and internal guidance, and national standard setters will likely need time to develop implementation guidance materials and increase awareness among the preparer and audit committee communities, in advance of the new reports being used. There would likely not be enough time with an earlier effective date.
- Making the new reporting standards effective for 2016 calendar year end audits would also be closely aligned with the timing of the proposed PCAOB reporting standards.

We hope that these comments will be useful to the IAASB in developing its proposed changes to auditor reporting standards. If you have any questions or require additional information, please contact Greg Shields, Director, Auditing and Assurance Standards at (416) 204-3287.

Yours very truly



Mark Davies, FCPA, FCA, CIA
Chair, Auditing and Assurance Standards Board (Canada)

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Bruce Winter, FCPA, FCA
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Appendix 1: Responses to Questions in the Exposure Draft

Key Audit Matters

1. **Do users of audited financial statements believe the introduction of a new section in the auditor's report describing the matters the auditor determined to be of most significance in the audit will enhance the usefulness of the auditor's report? If not, why?**

There were mixed views from users on this question. Most users of audited financial statements indicated that expanding the auditor's report to introduce a new section dealing with Key Audit Matters has the potential to be an improvement over the existing pass/fail model. However, users expressed different views as to how useful this information would likely be given the costs expected to be involved. Some users were concerned that the matters included in the report may be of a boilerplate nature and repetitive from year to year with little in the way of constructive insights that would aid their decision-making. Some users also were concerned that including such matters may be misunderstood, for example, if matters raised in the auditor's report are (a) perceived to constitute a warning to users even when the auditor may be satisfied that the financial statements are not misstated, or (b) perceived as providing additional assurance about the matter when none is intended.

Many Canadian users, preparers and auditors are satisfied with the current auditor's report. They are not convinced that readers will take the time to read the longer reports, or read all of the report. There is therefore a risk that significant matters the auditor wishes to bring to users' attention will be lost sight of. Under the current reporting model, users are able to quickly detect if the auditor has added paragraphs to the auditor's report that contain additional information of which, in the auditor's judgment, the users need to be aware.

2. **Do respondents believe the proposed requirements and related application material in proposed ISA 701 provide an appropriate framework to guide the auditor's judgment in determining the key audit matters? If not, why? Do respondents believe the application of proposed ISA 701 will result in reasonably consistent auditor judgments about what matters are determined to be the key audit matters? If not, why?**

Canadian stakeholders are concerned that the requirements and application material in proposed ISA 701 do not provide an appropriate framework to guide the determination of key audit matters on a consistent basis for the following reasons:

- The matters that the auditor discusses with the audit committee and that the audit committee would consider to be significant to the audit are not necessarily the same as those that are relevant to users of the financial statements because of the audit committee's greater understanding of the entity and what is important in respect of its oversight responsibilities.
- The matters auditors are required to take into account, as set out in paragraph 8 of ISA 701, are generally matters requiring significant auditor judgment. To the extent that there is variability in auditor judgments about such matters, there is likely to be variability of inclusion of such matters in the auditor's report. Different auditors may

have different thresholds in terms of determining whether a matter is a key audit matter.

- Circumstances that require significant modification of the auditor's approach often result from something that management has done or not done as expected in the audit plan, such as a significant deficiency in internal control. Describing in the auditor's report such a deficiency may constitute disclosing original information about the entity, which some stakeholders believe is not the auditor's role. Paragraph 8(c) of proposed ISA 701 may create an expectation that if the auditor does not include a significant deficiency in internal control as a KAM then there are no significant deficiencies in internal control when, in fact, there is a significant deficiency but it is not considered important enough to be a KAM.
- Paragraph A24 of proposed ISA 701 provides a list of other considerations in determining whether a matter is a key audit matter but is not helpful in explaining how these considerations affect this determination. For example, it is not clear whether the fact that a matter is common to all companies in an industry, increases or decreases the likelihood that it should be reported as a key audit matter. Similarly, it is not clear how the fact that the auditor has obtained a written representation from management about its plans and intentions would be a key audit matter.
- Paragraph 8 and the related application material do not address how the auditor is expected to deal with uncorrected misstatements accumulated during the audit (including the effect of uncorrected misstatements of prior periods on the financial statements). Such matters are, however, required to be communicated with those charged with governance and may require significant auditor attention.

For the above reasons, the AASB believes that there will not be reasonably consistent judgments about what matters are key audit matters. Because of this, we believe there will be a tendency for auditors to include a longer list of matters to address their concern that their judgments may be questioned in the future. Matters will be included in the auditor's report subject to the variable judgments of auditors. Accordingly, for two identical entities with two different auditors, the auditor's report may contain a significantly different list of key audit matters depending on the professional judgment of each auditor. This, in our view, detracts from the information value that could be provided by reporting on key audit matters, will inhibit users from appropriately assessing audit quality and prevent reasonable comparability of reporting.

We recognize that providing a numerical limit for KAM, or some kind of range, suffers from being arbitrary. However, we believe that the guidance in paragraph A7 of proposed ISA 701 should be enhanced to encourage more strongly that the number of matters reported as KAM should be small, for example by emphasizing that the number of matters to be disclosed is intended to be the matters of most significance in the audit that are ultimately useful to the users of the financial statements. We believe that if the number of KAM can be limited it may help to address to a certain extent our concerns about potential boilerplate disclosures and lack of comparability of auditor's reports.

We recommend that the IAASB evaluate the results of field testing that has taken place during the exposure period as they may shed light on the extent to which our concerns are borne out in practice and whether there is a need to specify a limit on the number of KAM in the auditor's report in the final standard.

3. **Do respondents believe the proposed requirements and related application material in proposed ISA 701 provide sufficient direction to enable the auditor to appropriately consider what should be included in the descriptions of individual key audit matters to be communicated in the auditor's report? If not, why?**

No. From a user perspective, users who read the IAASB's illustrative report in the ED were struck by the diversity in the manner by which key audit matters might be reported. This led them to question (a) what the different approaches for describing key audit matters imply about the auditor's overall assessment of a key audit matter, (b) if two auditors describe the same key audit matter in different ways, whether this implies the auditors have applied a different work effort to the matter and (c) whether the different descriptions imply different levels of audit quality. They were therefore concerned that the underlying requirements and application material permit different possible approaches that will potentially result in inappropriately inconsistent descriptions of key audit matters.

From the auditor perspective, auditors also expressed concern about how they are expected to describe key audit matters. They recognize that there is significant flexibility provided on how this should be done which allows for innovation and professional judgment. However, many auditors feared that their judgments will be questioned in the future on why they described a matter in a particular way and why this description differed from the description used by the same auditor or other auditors in similar circumstances. This may drive practice towards less insightful, standardized wording.

The application material in paragraph A41 of proposed ISA 701 indicates that an auditor might provide a conclusion in relation to a matter. It also suggests that there is a need for the auditor to avoid giving the impression that the discussion about KAM in the auditor's report is intended to convey an opinion on individual matters. In our view, the auditor cannot control what assurance a user takes from a conclusion on a matter. In particular, we believe that the illustrative matters in the ED that include wording such as "we concluded the use of such a model was appropriate" and "based on the audit procedures performed, we did not find evidence of" could be misinterpreted as providing an opinion on the respective matters. Therefore, we believe that the IAASB should make it clear that the description of KAM should not include a conclusion on the matter as readers may take assurance from such conclusion that is not warranted.

Paragraph A37 of proposed ISA 701 provides guidance to the auditor with respect to providing original information about the entity. We recognize that there may be circumstances when the auditor may need to include such information in order to appropriately describe a KAM. Accordingly, we do not support a prohibition on the

auditor providing original information about the entity if it is critical to the auditor's description of a KAM. However, paragraph A37 makes reference to the possibility that in some circumstances the disclosing of original information about the entity may be inappropriate. We note that paragraph A35 of proposed ISA 701 also refers to circumstances that may restrict the ability of the auditor to communicate KAM. It was not clear whether the circumstances in paragraph A35 are the ones considered in paragraph A37 where it would be inappropriate for the auditor to disclose original information about the entity or whether the IAASB is contemplating other circumstances not addressed in paragraph A35. We believe that this needs to be clarified.

4. **Which of the illustrative examples of key audit matters, or features of them, did respondents find most useful or informative, and why? Which examples, or features of them, were seen as less useful or lacking in informational value, and why? Respondents are invited to provide any additional feedback on the usefulness of the individual examples of key audit matters, including areas for improvement.**

Users did not find any of the illustrative examples particularly useful. They were viewed as being superficial and lacking in true insights. Many users questioned the value of including matters that, at the end of the day, did not appear to result in the identification of concerns or a misstatement of the financial statements. They believed that some matters may be misinterpreted as being a warning about potential problems when in fact that is not the case. The descriptions of audit procedures were generic in nature and likely not going to be understood by average users, whether in terms of their adequacy in addressing the related risk or the implications for quality of the audit. Users were confused as to why certain examples provide more detail (including conclusions on the matter) than others.

Specific comments from users included:

- Goodwill. This example provides factual information which is likely duplicative of disclosures in the financial statements but contains, in the view of users, no specific insights. It was considered to have limited informational value.
- Valuation of financial instruments. The discussion about valuation models is not in sufficient detail for sophisticated users who would want more information about how the model addressed specific accounting challenges of valuation of financial instruments. Preparers indicated that wording such as "We challenged management's rationale" casts negative aspersions about management which could be problematic.
- Revenue recognition. Users presume that because the fraud standard requires the auditor to assume that there is a significant risk relating to revenue recognition that revenue recognition will appear in most auditor's reports. They were not convinced that this would be useful. The example provides no indication of whether there was a problem. The fact that fraud is specifically mentioned in the matter even when none appears to have been detected may be misinterpreted as providing a warning to users in this respect.

- It was not clear whether, and to what extent, the illustrative examples included original information about the entity. It would have been helpful to know this when assessing the value of the information that the auditor is providing on a matter.

In our view, the IAASB should work to improve the illustrative examples by explaining more clearly why one approach to describing the matter may be more relevant than another. One approach to improving the examples may be by selecting from specific reports developed during the field testing phase by audit firms.

5. **Do respondents agree with the approach the IAASB has taken in relation to key audit matters for entities for which the auditor is not required to provide such communication – that is, key audit matters may be communicated on a voluntary basis but, if so, proposed ISA 701 must be followed and the auditor must signal this intent in the audit engagement letter? If not, why? Are there other practical considerations that may affect the auditor’s ability to decide to communicate key audit matters when not otherwise required to do so that should be acknowledged by the IAASB in the proposed standards?**

The applicability of the proposed KAM requirements is a key concern for Canadian stakeholders. Comments focused on the proposed split between listed/other than listed entities and the appropriateness of this split in a Canadian context. Of concern to many Canadian stakeholders is the proposal that KAM be required for “listed entities”. Stakeholders support limiting the scope of the KAM requirements (as discussed in paragraph 54 of the Explanatory Memorandum). Reporting KAM is a new concept in most jurisdictions and allowing a period of experience will be important before considering whether it is necessary to expand the requirements to other entities or to address areas for improvement of the standards. However, stakeholders believe that the prescription that KAM be required for audits of financial statements of “listed entities” is problematic in a Canadian context.

- (a) On the one hand, we believe that requiring all auditors’ reports on the financial statements of listed entities to include KAM is too broad a requirement because of the nature of the Canadian marketplace. The Canadian market is segmented into the TSX (approximately 1,500 issuers of which nearly 10% have a market capitalization of less than \$10 million), and the TSXV (approximately 2,000 issuers of which nearly 75% have a market capitalization of under \$10 million, are in the resource sector and in start-up mode).

Stakeholders highlight that there are a limited number of companies in Canada of a sufficient size that institutional investors and analysts are actively following them; and it is institutional investors and analysts who are expected to benefit most from the reporting of KAM.

There are significant differences between the needs of users of financial statements in the different market segments in Canada. Participants in the TSXV market indicated

that given the nature of many of these entities and their often limited financial resources, requiring KAM may add cost with limited benefits for investors. In addition, investors and other users of the financial statements of many early stage resource and other companies listed on the TSXV place greater emphasis on reserve reports from experts and other reporting on future prospects of the commercial success of the company in making investment decisions. Accordingly, some questioned whether such a requirement would be in the public interest given what they see as the potential adverse consequences for economic development of imposing an additional burden on the auditors, preparers and audit committees of such entities.

- (b) On the other hand, we believe the requirement for auditors to include KAM in their reports on the financial statements of listed entities would exclude certain Canadian entities that would otherwise be treated similarly to listed entities in terms of regulatory and accounting requirements, such as financial institutions that are not listed entities.

There are a number of other terms in general usage in Canada, whether in securities and other legislation or regulation and accounting standards, such as “reporting issuer”, “publicly accountable enterprise”, and “market participant”. There is no one term that we could recommend that appropriately addresses our concerns.

On the assumption that other jurisdictions may also have similar concerns to those identified in Canada, we believe the application of KAM to all listed entities needs to be reconsidered.

We recommend the IAASB change the scope of application of the KAM requirements to require KAM for audits of the financial statements of listed entities but also include criteria under which national standard setters have the flexibility to add to or subtract from the entities covered by the requirement. This might be accomplished by revising paragraph 30 of proposed ISA 700 as follows:

Key Audit Matters

31. For audits of complete sets of general purpose financial statements of a listed entity, other than those listed entities specifically excluded by the national standards setter in a jurisdiction, the auditor shall communicate key audit matters in the auditor’s report in accordance with proposed ISA 701....

Application material to support this requirement could be provided along the following lines:

In some jurisdictions, the term “listed entity” may result in the inclusion of entities for which the disclosure of key audit matters is of limited value to stakeholders. Alternately, there may also be entities that are not listed but for whom disclosure of key audit matters is of significant interest to stakeholders. In order to accommodate these jurisdictional

differences, national standard setters are permitted to make specific inclusions or exclusions to the entities for which auditors are required to communicate key audit matters in the auditor's report on their general purpose financial statements without affecting the ability of auditors to state that the audit was conducted in accordance with International Standards on Auditing.

A conforming amendment to paragraph 4 of proposed ISA 701 would also be required.

We believe that this approach will allow national standard setters to define the entities where there will be benefit to having KAM requirements and therefore more consistent KAM reporting. Further, if the definition of listed entities included in the final standard is more narrowly defined, for example by limiting the requirements only to larger listed entities, however defined, this would more likely result in national standard setters adding to the list of entities to which KAM requirements apply, rather than subtracting from this list.

In the event that the IAASB does not agree with this approach, the AASB believes that another approach should be implemented – develop principles to explain the nature, type and size of entities that the IAASB believes should be included in the reporting requirements rather than using any specific term such as “listed entities” The AASB acknowledges that this approach is less desirable given the challenges the IAASB has already faced in developing a global definition of public interest entities.

Further, some Canadian stakeholders expressed concern with the recognition in paragraph 30 of proposed ISA 700 (Revised) that law or regulation may impose requirements for auditors to communicate key audit matters. They acknowledge that law or regulation may impose requirements on auditors. However, stakeholders expressed the view that the incidences when this will be necessary will be greater if the IAASB does not clearly articulate when it is appropriate for KAM to be included in the auditor's report.

The AASB agrees that when an auditor decides to communicate key audit matters on a voluntary basis the auditor should follow proposed ISA 701 and indicate this intent in the engagement letter. We believe it is reasonable that management and those charged with governance are made aware when the auditor plans to report in accordance with proposed ISA 701. We are not aware of any practical considerations that need to be acknowledged in the proposed standards.

6. **Do respondents believe it is appropriate for proposed ISA 701 to allow for the possibility that the auditor may determine that there are no key audit matters to communicate?**
 - (a) **If so, do respondents agree with the proposed requirements addressing such circumstances?**
 - (b) **If not, do respondents believe that auditors would be required to always communicate at least one key audit matter, or are there other actions that could be taken to ensure users of the financial statements are aware of the auditor's responsibilities under proposed ISA 701 and the determination, in the auditor's professional judgment, that there are no key audit matters to communicate?**

Yes. The AASB agrees that it is appropriate for proposed ISA 701 to allow for the possibility that the auditor may determine that there are no key audit matters to communicate. However, there is a disconnect between this principle and the objective of the auditor to report matters of most significance. The proposed wording of the auditor's report in this circumstance ("this section of the auditor's report is intended to describe the matters...of most significance...and the auditor has determined that there are no matters to report") does not make sense.

We suggest the wording be changed to refer to "key audit matters" rather than matters of most significance. This would avoid the potential disconnect.

We do not believe that the requirements in paragraph 13(a) and (b) proposed ISA 701 are necessary. Paragraph 20(b) of ISA 220 already requires the engagement quality control reviewer to review the financial statements and the auditor's report. Further, a key discussion at the end of the audit with the audit committee is the form and content of the auditor's report. Adding these requirements in paragraph 13 is therefore duplicative and seems to imply that the auditor's initial discussion and communication would not be effective.

Paragraph A47 of proposed ISA 701 indicates that it will be "rare" that the auditor of a listed entity would not determine at least one KAM. Given the significant number of listed entities in the Canadian TSXV that are in the early stages of development, we do not believe that this will necessarily be a rare circumstance. We believe that reference to "rare" should be removed from this paragraph. Further, we believe it would also be helpful to expand the application material to provide more guidance as to other circumstances when no key audit matters may be identified.

We do not agree that auditors should be required to always communicate at least one key audit matter as this would result in perfunctory compliance in those situations where no key audit matters in fact exist.

7. **Do respondents agree that, when comparative financial information is presented, the auditor's communication of key audit matters should be limited to the audit of the most recent financial period in light of the practical challenges explained in paragraph 65? If not, how do respondents suggest these issues could be effectively addressed?**

Yes. We agree that the auditor's communication of key audit matters should be limited to the audit of the financial statements of the current period. However, for clarity, we believe that the application material in paragraph A8 of proposed ISA 701 should make it clear that a key audit matter in the audit of the financial statements of the current period may relate to the comparative information, for example determining whether the retroactive application of a change in accounting policy in the current period is appropriate.

8. **Do respondents agree with the IAASB's decision to retain the concepts of Emphasis of Matter paragraphs and Other Matter paragraphs, even when the auditor is required to communicate key audit matters, and how such concepts have been differentiated in the Proposed ISAs? If not, why?**

Yes. We agree with the IAASB's decision to retain the concepts of Emphasis of Matter paragraphs and Other Matter paragraphs, even when the auditor is required to communicate key audit matters. We also agree with how such concepts have been differentiated in the proposed ISAs except that we believe that when a key audit matters section is presented in the auditor's report the heading for any Emphasis of Matter paragraphs should be required to include further context to clearly differentiate it from key audit matters.

We recommend that the second bullet in paragraph A15 of proposed ISA 706 (Revised) be added as a requirement in paragraph 9 of that ISA.

Going Concern

9. **Do respondents agree with the statements included in the illustrative auditor's reports relating to:**

(a) The appropriateness of management's use of the going concern basis of accounting in the preparation of the entity's financial statements?

(b) Whether the auditor has identified a material uncertainty that may cast significant doubt on the entity's ability to continue as a going concern, including when such an uncertainty has been identified (see the Appendix of proposed ISA 570 (Revised))?

In this regard, the IAASB is particularly interested in views as to whether such reporting, and the potential implications thereof, will be misunderstood or misinterpreted by users of the financial statements.

No. The AASB does not agree with the statements included in the illustrative auditor's reports relating to going concern.

Although the IAASB has made improvements to the proposed wording of the going concern statements as compared with the ITC, Canadian stakeholders reiterated concerns they identified when responding to the ITC, namely:

- The statements are confusing and open to misinterpretation by less-informed users, particularly with respect to material uncertainties.
- Management is not currently required under IFRSs to make an explicit statement that it has prepared the financial statements on a going concern basis. Some auditors are concerned that this might confuse users as to the respective roles of management and the auditor with respect to going concern.
- Some auditors believe that the requirements will result in additional cost because making explicit statements in the auditor's report will necessitate the involvement of senior audit staff and quality control reviewers. It is not clear that such additional work will increase audit quality.
- Public sector auditors are concerned that the proposed going concern wording may not be appropriate in a public sector context (for example, the references to "liquidation" or "ceasing trading", which do not generally arise in a public sector context).

- Users and others also questioned whether the proposals would address the underlying objective of the proposals – to address concerns coming out of the financial crisis.
- Most users and auditors commenting on the going concern proposals believe that the current exception reporting model is more effective in highlighting going concern issues for users than the proposed statements on going concern.

Based on the comments received from our stakeholders, we believe that the proposed statements on going concern will be of limited value to users and could also increase the expectation gap rather than reduce it. We also believe that the IAASB should continue to work with accounting standard setters as part of a holistic approach to reporting on going concern.

We recommend that, as outlined in paragraph 84 of the Explanatory Memorandum, the IAASB defer finalization of reporting on going concern as part of that holistic approach. We understand that such an approach would be consistent with the direction being taken by the PCAOB on this type of reporting.

10. What are respondents' views as to whether an explicit statement that neither management nor the auditor can guarantee the entity's ability to continue as a going concern should be required in the auditor's report whether or not a material uncertainty has been identified?

We do not support the inclusion in the auditor's report of explicit statements about going concern. In the event that such statements are included in the auditor's report, we believe that when a material uncertainty has been identified the addition of the statement that neither management nor the auditor can guarantee the entity's ability to continue as a going concern is redundant and duplicative.

Compliance with Independence and Other Relevant Ethical Requirements

11. What are respondents' views as to the benefits and practical implications of the proposed requirement to disclose the source(s) of independence and other relevant ethical requirements in the auditor's report?

Users were of the view that this disclosure was marginally beneficial although most are satisfied with the extant requirement for the auditor's report to explain that the auditor is required to comply with relevant ethical requirements.

Auditors identified some practical implementation concerns. In Canada, for example, there are some differences in ethical requirements depending on the province in which the auditor is licensed. For Canadian audits of entities that involve auditors from different provinces, explaining the source of the ethical requirements maybe somewhat complex. Auditors also noted that this concern would be even greater for international audits. Nevertheless, we believe that these practical implementation concerns can be overcome.

Disclosure of the Name of the Engagement Partner

12. What are respondents' views as to the proposal to require disclosure of the name of the engagement partner for audits of financial statements of listed entities and include a "harm's way exemption"? What difficulties, if any, may arise at the national level as a result of this requirement?

We are not convinced that disclosing the engagement partner name would have positive behavioral implications for auditors. We are concerned that users might reach inappropriate conclusions with respect to the performance and capabilities of engagement partners on larger audits.

Auditors of Canadian entities that are registered with the US Securities and Exchange Commission indicated that disclosure of the name of the engagement partner may increase the personal liability of Canadian engagement partners in the US when they are named in documents filed with the SEC. Because there may be different legal consequences in different jurisdictions, the AASB believes that national standard setters should be provided the flexibility to decide whether the requirement to disclose the name of the engagement partner should apply in its jurisdiction.

We support there being a harm's way exemption when disclosure is reasonably expected to lead to a significant security threat to the individual.

We do not see the need for application paragraph A45 of proposed ISA 700 (Revised), which indicates that law or regulation may require that the name of the engagement partner responsible for audits of financial statements other than listed entities be included in the auditor's report. While it is a true statement, we do not believe it adds any value.

In Canada and possibly in other jurisdictions, reference in the auditor's report to the engagement partner's licence number and the location of a public register identifying the engagement partner, is sufficient to enable those who wish to do so identify the name of the engagement partner.

We recommend that proposed paragraph 46(k) be deleted. In the event that this paragraph is retained in the final standard we suggest the following:

- (a) the requirement be amended to require that the engagement partner be able to be identified in the auditor's report (rather than specifying that the engagement partner's name be included in the auditor's report);
- (b) national standard setters be given the flexibility to decide whether this requirement should apply in its jurisdiction; and
- (c) paragraph A45 be deleted.

Other Improvements to Proposed ISA 700 (Revised)

13. What are respondents' views as to the appropriateness of the changes to ISA 700 described in paragraph 102 and how the proposed requirements have been articulated?

We support the improved description of the responsibilities of the auditor and key features of the audit in paragraphs 35-38 of proposed ISA 700 (Revised).

We agree with the requirement in paragraph 39 of proposed ISA 700 (Revised) that the description of the auditor's responsibilities shall be included within the body of the auditor's report or in an Appendix to the report. We do not agree with paragraph 40 which would permit location of such description outside the report because the description is, in our view, a key element of the auditor's report and users are less likely to read material that is located outside the auditor's report rather than within the report itself.

We recommend that paragraph 40 be deleted. In the event that paragraph 40 is retained, we believe that paragraph 39 needs to be revised. This is because paragraph 39 specifically requires the description of the auditor's responsibilities to be included in the auditor's report. As currently worded, if law or regulation permitted the auditor to refer to a website under paragraph 40, the auditor would still have to comply with paragraph 39. Accordingly, paragraph 39 needs to contain the caveat "Except in the circumstances described in paragraph 40..."

We support the requirement to describe the responsibilities of those responsible for overseeing the financial reporting process in paragraph 33 and the related application material in proposed ISA 700 (Revised).

We support the proposals dealing with other reporting responsibilities.

14. **What are respondents' views on the proposal not to mandate the ordering of sections of the auditor's report in any way, even when law, regulation or national auditing standards do not require a specific order? Do respondents believe the level of prescription within proposed ISA 700 (Revised) (both within the requirements in paragraphs 20–45 and the circumstances addressed in paragraphs 46–48 of the proposed ISA) reflects an appropriate balance between consistency in auditor reporting globally when reference is made to the ISAs in the auditor's report, and the need for flexibility to accommodate national reporting circumstances?**

The AASB does not support the proposal not to mandate the ordering of sections of the auditor's report in any way, for the following reasons:

- We do not find the IAASB's reasons for not mandating the ordering of the auditor's report to be compelling:
 - Paragraph 104 of the Explanatory Memorandum refers to "cultural reasons". We do not believe that cultural reasons justify avoidance of presenting the auditor's report in a manner that enhances audit quality. In our view, this justification for not mandating the ordering of the report would set a dangerous precedent for future standard setting activities.
 - Paragraph 105 of the Explanatory Memorandum notes that the proposal to not mandate ordering of the report is largely consistent with extant ISAs 700, 705 and 706. This may well be the case, however under the extant ISAs the auditor's report is generally six paragraphs whereas under the proposed ISAs the auditor's report could be several pages in length. We believe that these significantly different circumstances justify serious consideration of the need to mandate ordering.

- We believe there are potentially negative consequences of not mandating the ordering of the report, which may include:
 - It will be more difficult for users to compare and contrast different auditor’s reports;
 - It creates the potential for disagreements between management and the auditor about the placement in the report of important matters which may not be in the best interest of users of the report;
 - It may create confusion among users about the relative significance of matters that are presented in different locations in the report; and
 - It inevitably will increase inconsistency in global reporting.

We recommend that the ordering of the report be mandated in the final standard.

We support the level of prescription of the requirements in paragraphs 20-45 of proposed ISA 700 (Revised). We also support the requirements for specific headings in the auditor’s report to ensure the required reporting elements can be recognized in all reports.

With respect to paragraphs 46-48 of proposed ISA 700 (Revised) we have the following comments, which we believe would enhance the consistency and comparability of auditor reporting in the public interest while permitting an appropriate degree of flexibility:

- The paragraphs should reflect the recommendations we have made in our other responses to questions in the ED to the extent that they are relevant. For example, consistent with our views with respect to ordering of sections in the auditor’s report, we believe that ordering should also be mandated in paragraphs 46-48 (unless a specific ordering is required under law or regulation).
- Paragraph 46(a) should be identical to paragraph 21 to clearly indicate that the report is the report of an independent auditor. Permitting the use of other titles could result in titles that users find confusing and/or do not appropriately reflect the auditor’s independence role.
- Paragraph 46(c) should be more specific as to the form of opinion expressed by the auditor by incorporating the requirements in paragraph 24. The auditor’s opinion is probably the key piece of information that users refer to when reading the report. Consistency of the wording of the opinion is critical in clearly articulating to users the auditor’s conclusion from the audit.
- Paragraph 46(f) should be identical to paragraph 29. We find the words “addresses the reporting requirements in” as being open to significant interpretation. We are not supportive of including statements on going concern in the auditor’s report. However, if such statements are included, we believe that permitting different wording to be used would be confusing to users, particularly when the financial statements are prepared in accordance the same international financial reporting frameworks. If paragraph 46(f) is not revised as we suggest, we recommend that the words “and is not inconsistent with” be added after “requirements”.
- Paragraph 46(h) should be identical to paragraph 31. Again, we believe that permitting different wording to be used would be confusing to users. If paragraph 46(h) is not

revised as we suggest, we recommend that the words “and is not inconsistent with” be added after “requirements”.

Appendix 2: Summary of AASB Consultations with Canadian Stakeholders re IAASB Exposure Draft

- Twelve written responses were received including from auditors of large, medium and small firms and public sector auditors, a prudential regulator and a bank.
- Roundtable discussions in various provinces throughout Canada (Nova Scotia, Quebec, Ontario, Manitoba, Alberta and British Columbia). These were organized by the local provincial institutes of chartered professional accountants. The institutes were asked to seek participants not just of auditors but also of preparers, management, directors/audit committees and users. There were over 100 participants.
- Roundtable discussions with various CPA Canada groups. These provided access to directors, preparers and investors, as well as auditors. There were approximately 40 participants in these groups.
- A conference call with the chief accountants committee of Canadian securities regulators.
- Staff also had a discussion with various members of the national professional practices groups of public sector auditor general staff across Canada.
- A webinar was held to inform participants about the ED. There were approximately 1,000 live participants and over 2,000 registrants who could assess the webcast either live or in archive.