



## **International Auditing and Assurance Standards Board (IAASB)**

### ***Exposure Draft: Proposed New and Revised International Standards on Auditing (ISAs)***

---

#### **Introduction**

1. The ABI is the voice of insurance, representing the general insurance, investment and long-term savings industry. It was formed in 1985 and today has over 300 members, accounting for some 90% of premiums in the UK. Our members as institutional investors have some £1,800 billion of funds under management held in a variety of asset classes. These include both equity and fixed interest securities, listed and unlisted, of entities with financial reporting obligations located, denominated or traded in many different countries worldwide. By way of emphasis, the holdings by our members in UK equities are equivalent to almost 20% of the capitalisation of the UK market.
2. We therefore have a strong interest in ensuring that financial reporting addresses the information needs of investors, including shareholders' requirements for the information necessary for them to exercise their governance responsibilities effectively. The provision of additional and better information in the auditor report will assist investors in holding the boards of companies to account. It will also facilitate improved dialogue and engagement.
3. The ABI is pleased to respond to the IAASB's consultation on proposed enhancements to the auditor's report. Overall, we welcome the proposals and believe that they will enhance the usefulness of audit opinions to shareholders. Finally, the incremental costs arising as a result of the package will not be significant as the proposals reflect a recording of views and work that are already reached and undertaken.

#### **General Comments**

##### ***Key Audit Matters***

4. We support the approach of having a principles-based requirement that defines the "filter" applied by auditors to identify the key audit matters. We also agree that entity-specific matters will ultimately be a matter of professional judgement. However, given the nature of the audit process, we believe that the principle of significance is drawn too widely and risks a proliferation of matters that may fail to assist shareholders identifying the key matters.
5. The principles-based approach needs to be underpinned by a more explicit judgement framework. This will aid comparability of judgements across companies

and, in turn, the assessment of audit quality. Accordingly, we suggest amending the proposed objective (para 6) from “significant” to “*significant to shareholders’ understanding* of the financial statements”.

6. Furthermore, paragraph 8(a) should be amended to refer to “*most significant risks*”. This should result in insights related to areas in the financial statements that involve complex financial reporting estimates and significant management judgment. This will require greater engagement with management and those charged with governance around the basis for the selection of these matters and what is said about them in the auditors’ reports. This is welcomed.
7. A focus on why and how the audit addressed key financial statement areas is meaningful and valuable to users. It would also be helpful for the auditor to explain *why* they are of particular importance to the audit and, at a high level, how they were addressed in the audit.
8. We do not share some of the concerns raised that this could have the effect of lowering the threshold for disclosing information to the market. The relationship between what management intend to report and what they end up reporting, subject to the audit, is dynamic. Auditors are a key line of defence for shareholders in ensuring prudent reporting and, via professional scepticism, that a true and fair view has been reached. So if the auditor believes that a matter needs to be addressed at an earlier point or explained further to reach a true and fair view, then we support this. Where such issues do not relate to the true and fair view requirement but are not covered by financial reporting requirements, again, we believe this should be addressed under the usual reporting and audit process.

### **Going Concern**

9. We agree the auditor’s opinion should address going concern and include conclusions on whether:
  - i. management’s use of the going concern basis of accounting in the preparation of financial statements is appropriate, and
  - ii. whether a material uncertainty exists related to events or conditions that, individually or collectively, may cast significant doubt on the company’s ability to continue as a going concern.
10. We also agree that, while material uncertainties will, by their nature, be key audit matters, it is appropriate to present such matters in the going concern section to provide emphasis.
11. However, given the number of active projects currently addressing going concern in both an international, with the International Accounting Standards Board (IASB), and national, context, with the US Financial Accounting Standards Board (FASB) and UK’s Financial Reporting Council, we believe that the IAASB will have to consider

carefully the status and planned actions of the accounting standard setters before finalising its reporting proposals.

12. Overall, so as to ensure the process is advanced in reasonable time, there are merits in the proposed twin-track approach. We would be concerned if publication and implementation was deferred indefinitely until there is international agreement on going concern: it could take a long time for standard setters to reach a common view.

### ***Global Convergence***

13. International convergence on the auditor reporting model is important to institutional investors. We are pleased that there is a consistency with the proposed new auditor reporting models of other national regulators and standard setters. We urge the IAASB to continue to communicate with the European Commission and work closely with the US Public Company Accounting Oversight Board (PCAOB) in finalising their respective reporting requirements.

### ***Materiality***

14. Our members continue to believe it would be useful to have the auditor report on its assessment of materiality. As you will be aware of from recent developments in the UK, the FRC now requires such assessment by auditors, and our members find the information to be very useful in assessing the reliability of financial statements. Its usefulness will also be further enhanced when comparative information is provided over time, providing insight on an important aspect of audit quality.

## Questions for Consultation

---

1. *Do users of the audited financial statements believe that 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?*
15. Yes.
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?*
16. While we fully support the introduction of Key Audit Matters as a concept for improving auditor reporting, we are concerned that the principle of "significance" may be drawn too widely and risks a proliferation of matters that fail to assist shareholders identifying the key matters. As outlined above, we believe that Key Audit Matters should be underpinned by a more explicit judgement framework that focuses on the significance to shareholders and aids comparability and the assessment of audit quality.
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?*
17. While we support the principles-based approach, underpinned by professional scepticism, rather than prescribing items, there could be benefit in adding further guidance to paragraph 8(a-c). Specifically, for 8(a) this should be amended to "most significant" and "involving auditor judgements of material significance to shareholders".
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.*
18. We found the illustrative examples helpful and welcomed the focus on why they were considered significant to the audit.

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?*
19. Yes.
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?*
20. Yes.
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?*
21. Yes.
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?*
22. In practice, it is likely to be very rare that something will be identified as an Emphasis of Matter or Other Matter as opposed to a Key Audit or Going Concern Matter. While such situations will be rare, they are likely to lead to confusion given the number of different sections outlining different Matters. It is therefore helpful to include a requirement to explain how the Matter is separate from the Key Audit Matters.
23. It may be appropriate to combine the Emphasis of Matter and Other Matters into one section for purposes of reporting planning and scoping matters and, for example, dual dating a report, stating that the prior period financial statements were audited by a predecessor auditor.

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 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.*

24. While we support the basic judgement structure proposed, we have reservations regarding the implementation timeline given the number of developments in Going Concern accounting.

*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?*

25. A statement that the going concern basis cannot be guaranteed should be included whether a material uncertainty is identified or not.

*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?*

26. Auditor independence is of critical importance to shareholders and we therefore support including further details on independence and other ethical requirements in the auditor's report. We agree, however, that it is important that this does not result in an exhaustive list of sources and so lose its value to shareholders.

27. Our concern is that the reporting requirement here merely sets out what the auditor is required to do but does not state that the auditor has made the requisite communications with those charged with governance. We should like to see an affirmative statement in this regard, which may also help focus the disclosure. This concern equally applies to the communication of significant audit findings and any significant deficiencies in internal controls.

28. It is important for such disclosures to demonstrate how existing non audit-related commercial relationships are considered in preserving independence.

*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?*

29. In the UK it has been normal practice, for a long time, for the audit partner to be named. This transparency is welcomed and is becoming increasingly relevant as investors engage with auditors. However, such requirements are best addressed under national requirements, which can identify the appropriate vehicles and address legal implications.

*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?*

30. We have no comments to make on this question.

*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?*

31. We believe the IAASB’s decision not to mandate the ordering of sections of the auditor’s report, but rather to use illustrative reports, strikes the right balance in promoting adoption of the report form preferred by the IAASB, while providing flexibility in reporting to national standard setters.

**ABI 27.11.2013**