

AUDITOR REPORTING STANDARDS AND RELATED CONFORMING AMENDMENTS

THE AUDIT QUALITY ASSURANCE WORKSHOP 7TH-8TH March 2017.

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Benefits of the New Auditor's Report

- ❖ Enhanced communicative value to users
- ❖ More robust interactions and communication among users, auditors and those charged with governance (TCWG)
- ❖ Increased attention by management and TCWG to the disclosures referred to in the KAM section of the auditor's report
- ❖ Increased professional skepticism in areas where KAM are identified
- ❖ Increased audit quality of user's perception of audit quality

Changes to ISAs and how they affect reporting

New and Revised Auditor Reporting Standards:

- ❖ Overarching standards for Auditor Reporting- ISA 700 (Revised)
- ❖ New Key Audit Matters section- ISA 701 (New)
- ❖ Modifications to auditor's opinions- ISA 705 (Revised)
- ❖ Enhanced auditor reporting related to going concern- ISA 570 (Revised)
- ❖ New other information section- ISA 720 (Revised)
- ❖ Revisions to ISA 260 and 706 as a result of ISA 701, and related conforming amendments to ISA 210, ISA 220, ISA 230, ISA 510, ISA 540, ISA 600, ISA 710

What is included in description on KAM

What is KAM?

- ❖ KAM are defined as those matters that, in the **auditor's professional judgement**, were of **most significance** in the audit of the financial statements of the current period.
- ❖ KAM are selected from matters communicated with TCWG.

Which Auditor's report will include KAM Section

- ❖ KAM is required to be communicated in the auditor's report for audits of financial statements of listed entities in accordance with new ISA 701.
- ✓ Law or regulation may require KAM for audits of entities other than listed entities (e.g. public interest entities or public sector entities)
- ✓ Auditors may voluntarily or at the request of management or TCWG, communicate KAM in the auditor's report for entities other than listed entities.

Are KAM Always Communicated in the Auditor's Report

- ❖ Auditor is required to include each KAM unless;
 - ✓ Law or regulation precludes disclosure
 - ✓ In extremely rare circumstances, the auditor determines that the matter should not be communicated.
 - Adverse consequences of communicating the KAM would reasonably be expected to outweigh the public interest benefits of such communication
- ❖ KAM is prohibited for a disclaimer of opinion, but required for a qualified or adverse opinion
- ❖ In certain limited circumstances, there may be no KAM to be communicated

The Decision Making Framework for KAM

KAM Steps:

1. Matters that were communicated with TCWG
2. Matters that required significant auditor attention
3. Matters of most significance in audit

Initial Steps in Determining KAM

- ❖ The Auditor will always consider:
 - ✓ Areas of higher assessed risks of material misstatements or significant risks (i.e. risk requiring special audit consideration)
 - ✓ Significant auditor judgement relating to areas of significant management judgement (e.g. complex accounting estimates)
 - ✓ Effect on the audit of significant events or transactions

Determination of Matters of Most Significance in the Audit-KAM

Matters that required significant auditor attention = Matters of most significance in the Audit

KAM is determined by the Auditor's consideration of the:

- ❖ Nature and extent of communication with TCWG
- ❖ Importance of intended users' understanding of f/s
- ❖ Nature and extent of audit effort needed to address
- ❖ Nature of the underlying accounting policy, its complexity or subjectivity
- ❖ Nature and materiality, quantitatively or qualitatively, of corrected and accumulated uncorrected misstatements due to fraud or error, if any.
- ❖ Severity of any control deficiencies identified relevant to the matter, if any
- ❖ Nature and severity of difficulties in applying audit procedures, evaluating the results of those procedures, and obtaining relevant and reliable evidence.

KAM- What is included in the Description

The description always includes:

- ❖ Why the matter was considered to be KAM
- ❖ How the matter was addressed in the audit
- ❖ Reference to the related disclosure(s) if any

The description of how the matter was addressed in the audit may include:

- ❖ Aspects of the auditor's response or approach
- ❖ Brief overview of procedures performed
- ❖ Indication of the outcome of the auditor's procedures
- ❖ Key observations with respect to the matter

Considerations in Describing KAM

- ❖ KAM should be entity-specific and avoid standardized or overly technical language
- ❖ Description of a KAM should not;
 - ✓ Imply that the matter has not been appropriately resolved by the auditor in forming the opinion on the f/s
 - ✓ Contain or imply discrete opinion on separate elements of the f/s (a peace meal opinion)

KAM- Relationship to Emphasis of Matter (EOM) and Other Matter (OM) Paragraphs and Modified Opinion

- ❖ Concept of EOM and OM paragraphs are retained
- ❖ EOM and OM paragraphs cannot be used as a substitute for communicating a matter determined to be a KAM
- ❖ New requirement to use the term “Emphasis of Matter” in the heading in the auditor’s report when an EOM paragraph is included
- ❖ Matters that give rise to a modified opinion are by their nature KAM

KAM- What are the Documentation Requirement

- ❖ In accordance with ISA 230, ISA 701 requires the auditor to document the professional judgements made about;
 - ✓ Why a matter that required significant auditor attention is or is not a KAM
 - ✓ If there are no KAM, the rationale why
 - ✓ Why a matter determined to be a KAM is not communicated
- ❖ No requirement to document the rationale for why matters communicated to TCWG were not matters that required significant auditor attention.

Enhanced Auditor Reporting on Going Concern

- ❖ Changes in ISAs and the auditor's report to focus more on going concern;
- ✓ Explicit description of the respective responsibilities of management and auditor in all auditors reports
- ✓ Separate GC section required when material uncertainty exists, with a heading "Material Uncertainty Related to Going Concern".
- ✓ New requirement to challenge adequacy of disclosures for GC "close calls"

Interaction Between KAM and GC

- ❖ Matters relating to G.C. including “close calls” may be determined to be KAM and communicated in the auditor’s report in accordance with new ISA 701
- ❖ When a material uncertainty relating to G.C. exists, it is by nature a KAM, but is reported separately in the “Material Uncertainty Related to Going Concern” section of the auditor report.

Other Changes to the Auditor's Report

- ❖ Auditors' opinion required to be present first
- ❖ Required basis for opinion section for unmodified opinion
- ❖ Statement about independence and other ethical responsibilities
- ❖ Naming of the engagement partner, listed entities only
- ❖ Enhanced description of auditor's responsibilities and key features of the audit
- ❖ Required identification section when TCWG are separate from the management

Auditor Reporting and Law or Regulation

- ❖ New and Revised Auditor reporting standard continue to allow for;
 - ✓ Reference to ISA pronouncements in the auditor's report when law or regulation in a jurisdiction specify the layout or wording of the auditor's report, provided that certain requirements are met
 - ✓ Any other reporting responsibilities (ORR) presented by law or regulation in addition to those required by the ISA pronouncements, reported either:
 - In a separate section in the auditor's report
 - If addressing the same topic required by ISA pronouncements in the same section provided the auditor's report clearly differentiates the ORR from the reporting required by the ISA pronouncements