

ENHANCED AUDITOR REPORTING

LIVE CHAT: QUESTIONS AND ANSWERS

INTRODUCTION

Following on from the International Auditing and Assurance Standards Board's (IAASB) new requirements for auditors' reports issued in early 2015, the Auditing and Assurance Standards Board (AUASB) have now released equivalent requirements in Australia.

These new requirements are intended to enhance the transparency and information value of auditors' reports, representing a significant move away from the so called "boiler plate" wording in existing auditors' reports.

From reporting periods ending on or after 15 December 2016, auditors of listed companies will need to report Key Audit Matters for the first time and auditors of all companies will need to make significant changes to their auditors report.

This live chat saw expert panellists from the AUASB address questions about the impact on auditors of the new enhanced auditor reporting requirements.

The experts who addressed members' questions were:

- Richard Mifsud, Executive Director, AUASB
- Howard Pratt, Senior Technical Manager, AUASB
- Claire Grayston, Policy Adviser – Audit & Assurance, CPA Australia

PODCAST

The Chairman and Deputy Chairman of the IAASB and Chairman of the AUASB jointly recorded a [podcast](#) with CPA Australia in November 2015 to explain the impact of these changes. The AUASB is responsible for issuing the new requirements in Australia.

RESOURCES

Further background material is available in the IAASB's Auditor Reporting Toolkit.

- [Auditor Reporting Fact Sheet](#)
- [Slide Presentation in support of the IAASB's New and Revised Auditor Reporting Standards](#)
- [At a Glance](#)
- [Basis for Conclusions](#)
- [Auditor Reporting Project History](#)
- [Auditor Reporting – Key Audit Matters](#)
- [Auditor Reporting – Illustrative Key Audit Matters](#)
- [Auditor Reporting on Going Concern](#)

DISCLAIMER

The answers given by the AUASB staff to questions asked during the CPA Live Web on 26 February 2016 are not the views of the AUASB. Answers are given as a general guide only and are the personal views of the presenters.

Care is taken in providing answers to participants' questions during the Live Web; however, due to the format of the conference, it is not possible to provide a complete suite of answers that address all possible circumstances that may exist in practice. Accordingly, participants must refer to, and comply with, the Auditing Standards when applying the standards and do not rely on the answers provided during the session.

QUESTIONS AND ANSWERS

Which Auditing Standards changed as a result of the new auditor reporting initiative?

- Revisions that result in replacement of pre-existing standards – ASAs 260, 540, 700, 705 and 706.
- Introduction of a new standard – ASA 701
- Conforming amendments to pre-existing standards – Compiled ASAs 200, 210, 220, 240, 300, 315, 320, 330, 450, 500, 510, 540, 560, 580, 600, 710 and 800.

What are the main changes to auditor reporting?

1. The format of the auditor's report:
 - a. The auditor's opinion is located first
 - b. A new basis for opinion paragraph must follow the opinion and:
 - i. Must state the audit conducted in accordance with the Australian Auditing Standards
 - ii. Refer to the auditor's responsibilities
 - iii. Include an independence statement
 - iv. State that sufficient appropriate audit evidence has been obtained.
 - c. Enhanced description of management's responsibilities, including:
 - i. Assessing going concern
 - ii. Disclosing going concern matters, when applicable
 - iii. Determining that the use of the going concern basis of accounting is appropriate.
 - d. Enhanced description of the auditor's responsibilities, including:
 - i. Concluding on management's use of the going concern basis of accounting.

- ii. Communicating with management regarding, among other matters, the planned scope and timing of work, significant audit findings and any significant deficiencies in internal control.
 - iii. When applicable, communicating key audit matters.
2. When applicable, a new format for reporting a going concern issue – replaces the pre-existing approach that requires an emphasis of matter paragraph
 3. When applicable, a new section on key audit matters (KAM)

Do the latest auditor reporting requirements apply to the audit of all entities?

Yes, with the exception of ASA 701, this is conditional. ASA 701 applies to:

- The audit of a general purpose financial report of a listed entity.
- When required by law or regulation.

The standard also applies when the auditor otherwise decides to communicate key audit matters.

What is the operational date for the changes?

ASIC has indicated that it will expect registered company auditors to comply with the new and revised auditor reporting standards once they become operative or periods ending on or after 31 December 2016. Regulators in other countries will need to work in with their national standard setting bodies.

What are the key impacts if clients are mainly preparing special purposes financial reports?

For special purpose financial reports the format of the auditor's report will need to include all of the changes in the enhanced auditor reporting, except for key audit matters (unless the auditor chooses to include key audit matters) and naming of the engagement partner. The main changes are:

- opinion section first followed by the basis for opinion
- if applicable, enhanced reporting on going concern and "other information"
- statement about auditors independence and ethical responsibilities
- enhanced description of the auditor's responsibilities and key features of the audit

Could the changes lead to friction between the client and the auditor? The client may not like some (or all) of the comments. How can auditors be protected against this reaction? I don't mean just companies regulated by ASIC.

The underlying purpose of communicating key audit matters where they are reported in audit reports of listed entities is that they should be, in the auditor's professional judgement those matters which were of most significance in the audit of the financial report. The auditor reporting changes have also resulted in changes to ASA 260 so as to ensure that there is appropriate communication between the auditor and those charged with governance (board and audit committee) prior of any such matters being reported in the auditor's report. Therefore there should be no surprises and hopefully little if any "friction", and no more healthy discussions with those charged with governance than has been the case in the past.

Were any other changes made to the Auditing Standards in addition to the main enhanced auditor reporting changes?

Yes.

ASA 720 *The Auditor's Responsibilities Relating to Other Information* was revised and replaced.

The revision of ASA 720 was not conducted as part of the auditor reporting initiative, per se, however, new reporting requirements have been introduced under that standard which also apply to periods ending on or after 15 December 2016.

[Aus] Appendix 2 in ASA 720 provides a helpful decision tree diagram with references back into the standard itself.

In addition, there have also been consequential changes arising from the IAASB's auditing disclosures enhancements, which have essentially been confined to changes in application materials in some of the standards.

Has the AUASB provided illustrative examples of the new-style auditor's report?

Yes. ASA 700 includes example reports in the appendices – unmodified opinions.

Other ASAs also include example reports – for example, ASAs 570, 705, 706.

Has the AUASB issued any further guidance?

The AUASB is developing a series of bulletins designed to provide helpful information to auditors. The bulletins will build up to a bank of useful information on practical issues. The first bulletin is expected to deal with certain aspects of the new auditor reporting requirements and is expected to be published on the AUASB website in the coming months.

Are the auditor's responsibilities located on the AUASB website?

They will be very soon. The AUASB has approved implementation of the relevant illustrations of the auditor's responsibilities for different audit engagements – loading on the AUASB website is in progress and expected to be operational sometime in the coming months.

The intention is that auditors will be able to include a hyperlink in their auditor's reports that takes the reader directly to the relevant description of the auditor's responsibilities on the AUASB website.

The Explanatory Guide will provide information on how auditors link to the description of auditor's responsibilities on the AUASB website.

What will the AUASB be doing to assess auditor's implementation of the revised auditor reporting standards?

The AUASB will conduct a post implementation review once the new and revised standards have been implemented over several reporting periods. We will also be liaising with the auditing profession and regulators in relation to any feedback which may be provided regarding the implementation of the new standards, particularly after the first year of mandatory implementation.

Our auditors provide numerous audit findings letters, but most of the findings from the final audit don't get conveyed in a letter to TCWG until after the financial statements have been signed off by all parties. So it would seem with their current approach that the communication to TCWG is too late for a matter to be a KAMs in the audit report; as they didn't convey in writing significant audit matters before issuing their opinion. Are they permitted to send an email and this constitutes communicating to the TCWG?

Audit finding letters are not necessarily key audit matters. The key audit matters relate only to the most significant matters considered by the auditor over the course of the audit and must be selected from matters communicated with TCWG. Communications may include emails however if the matter is so significant then you would expect a fulsome discussion with TCWG. Matters should not be raised at the end of the audit and the new requirements encourage timely discussion as matters arise.

In determining KAM for listed entities, what matters might be considered as requiring significant auditor attention?

Areas of:

- Higher risk of material misstatement
- Significant auditor judgement due to significant management judgement
- Significant events or transactions.

See ASA 701 paragraphs 9, 13, 14, A13, A14, A18, A27, A29, A54 and A55.

What must the auditor disclose when communicating key audit matters (KAM) in an auditor's report?

- Why the matter was determined to be a KAM and
- How was the matter addressed in the audit.

Are Emphasis of Matter and Other Matter paragraphs still permitted?

Yes.

- EOM – fundamental to users' understanding of the financial report
- OM – matter relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report

No EOM or OM paragraphs are permitted if the matter has been reported as a KAM. See ASA 706 8(b) and 10(b).

Are there likely to be many EOM or OM paragraphs in the future or do you think they are a thing of the past?

A decrease in the number of such paragraphs will occur but only where the matter has been determined to be of significance in the audit and is therefore reported as a KAM.

The prime example of this is in relation to a material uncertainty regarding going concern. Previously an EOM, now a separate section in the auditor's report.

On the other hand, an EOM paragraph would still be used to direct the reader to a contingent liability note regarding legal action where the auditor has not communicated the matter as a KAM.

Another example is that an EOM paragraph is required for audits of Special Purpose Financial Reports and where the auditor wishes to restrict distribution of the auditor's report.

OM paragraphs have not been common in the past and their numbers are unlikely to change significantly in the future. The purpose and nature of OM paragraphs differ from the purpose and nature of KAM and therefore an overlap is unlikely.

Has the "relevant period" been retained in the revised ASA 570 Going Concern?

Yes.

For purposes of the auditor's evaluation of management's assessment of the entity's ability to continue as a going concern, the relevant period remains from the date of the existing auditor's report to the expected date of the subsequent auditor's report.

What should the auditor do if a KAM is not included, or required to be included, in the financial report and Those Charged with Governance (TCWG) refuse to communicate the matter in another form (e.g. Director's Report)?

ASA 701, paragraph 13 makes clear that not all KAM are able to be referenced to a disclosure.

ASA 701, paragraphs A18 and A35 – A37 refer to the question.

The adequacy of the description of a KAM is a matter of professional judgement. The nature and extent of information provided by the auditor should be concise and understandable, while not inappropriately providing original information about the entity. (para. A34)

The description of KAM is not usually of itself original information about the entity, as it describes the matter in the context of the audit. However, the auditor may consider it necessary to include additional information to explain why the matter was considered to be one of most significance in the audit and therefore determined to be a key audit matter. The auditor may encourage management to disclose additional information. (para. A36)

An example of a KAM that is not required to be disclosed in the financial report is the implementation of a new IT system which may have a significant effect on the auditor's overall strategy or is related to a significant risk (e.g. changes to a system affecting revenue recognition).

Broadly, a KAM of this nature would not breach the original information rule as it refers to the audit focus of a common commercial activity and does not imply that there is a "problem".

Ultimately, the auditor uses professional judgement in complying with ASA 701. Clear and fulsome communication with Those Charged with Governance is essential and where appropriate, encouragement to disclose within, or outside of, the financial report may overcome any perceived problems. The auditor increases focus on the way in which the KAM is worded.

Discussions with TCWG or management may well be open and wide-ranging (even fractious) but the key issue currently is whether the audit opinion will be qualified or not. Now auditors are expected to comment on issues that management/TCWG might not want raised. If they don't like the comments, they will find a way to change auditors. I don't say that all will react in this manner but a significant number can be expected to think (and maybe act) along the lines of changing auditors.

It may well be that in certain circumstances management do not agree with the KAM identified by the auditor, but if the auditor considers the KAM are appropriate, and they not matters which should not be communicated because they may cause adverse consequences (see ASA 701 para.14), then the auditor should communicate the KAM.

What early planning by auditors in advance of applying the new audit requirements would be helpful?

1. Provide appropriate training for partners and staff. Be sure to include "audit documentation" relating to the new auditor reporting requirements, as one of the topics.
2. Agreeing the terms of engagement
 - a. When agreeing the terms of engagement under ASA 210, inform those charged with governance (TCWG), that the format of the auditor's report will differ from the previous year.
 - b. Where applicable, TCWG should be advised that key audit matters (KAM) will be communicated in the auditor's report. Provide TCWG with appropriate explanations of the new requirements.
 - c. When possible, indicate to TCWG what matters are likely to be KAM. The prior year audit file may be helpful.
 - d. Explain to TCWG the increased information required in the "Responsibilities for the Financial Report" section of the auditor's report. Inform TCWG that there has been no change in their responsibilities, merely an enhancement in the description thereof, particularly in respect of assessing going concern.
 - e. Provide TCWG with an example of the form and content of the new-format auditor's report that is likely for the specific entity.
3. Drafting auditor's report templates for firm use.

4. **** IMPORTANT **** When the auditor chooses to refer to the description of the auditor’s responsibilities on the AUASB website, auditors must include in their auditor’s report only the hyperlink that refers to the specific applicable description for example:
- a. Single company – Corporations Act 2001.
 - b. Group Entity – Corporations Act 2001.
 - c. Single Entity – Not listed.
 - d. Single Entity – Compliance Framework.

The individual hyperlinks are expected to be available on the AUASB website sometime in coming months.

FURTHER INFORMATION

- <http://www.iaasb.org/new-auditors-report>
- <http://www.cpaaustralia.com.au/audit>
- <http://www.auasb.gov.au>

For help or to suggest other topics for live online chats please email livechats@cpaustralia.com.au

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