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Mr. Imran Vanker
Director: Standards
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5 October 2022

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Per email: standards@irba.co.za

Exposure Draft: Proposed Rule on Enhanced Auditor Reporting for the Audit of Financial Statements

Dear Mr. Vanker

We welcome the opportunity to comment on the Exposure Draft: Proposed Rule on Enhanced Auditor Reporting for the Audit of Financial Statements. This comment letter deals with responses to the questions posed in the Exposure Draft and are structured in two parts:

Part 1: General comments address a short introduction which provides some comments relevant to all the questions you have asked (for avoidance of repetition)

Part 2: Conforms to your requested format with our detailed answers to your specific questions.

The comments and considerations expressed in this comment letter are based on collated views of Ernst & Young Inc. South Africa and do not represent the collective view of the global EY network of firms.

If you wish to discuss these comments further, please contact Nicki Bester (nicki.bester@za.ey.com), Anzelle Wessels (anzelle.wessels@za.ey.com) or Roger Hillen (roger.hillen@za.ey.com).

Yours sincerely,

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1. General comments

Overall, we are supportive of IRBA's initiative to enhance auditor reporting for the audit of financial statements, which will contribute to enhancing the users of the financial statements understanding of an audit and the assurance being provided.

We do believe that the IRBA will need to develop guidance to support the proposed IRBA Rule, so as to, along with the proposed Rule, provide for a consistent and comparable approach in implementing the proposed IRBA Rule by audit firms. We also believe that it is vital that the guidance is issued and available well in advance of the effective date of the proposed IRBA Rule. Detailed suggestions on where and what guidance is needed is included in our response to your specific questions.

We recommend that the IRBA consider the impact of the proposed IRBA Rule on joint audits. For example, how would the disclosures in the auditor's report, as it relates to joint audits, be affected by part 1(d) of the proposed IRBA Rule. As such, we believe that the IRBA should provide guidance on how joint auditors should comply with the proposed IRBA Rule.

Directive 2 of 2017, *Matters related to the communication of key audit matters in the independent auditor's report*, issued by the South African Reserve Bank (now the Prudential Authority) requires that auditors share with the Prudential Authority any key audit matters to be communicated in the auditor's report prior to the finalisation of the audit opinion. We recommend that the IRBA engage with the Prudential Authority on the proposed IRBA Rule so that the Prudential Authority can determine whether they should expand Directive 2 of 2017 to extend to any of the proposed disclosures in the auditor's report as it relates to the proposed IRBA Rule.

2. Responses to specific questions

Respondent Information

Respondent type	Firm
Organisation Name	Ernst & Young Inc.
Full Name	<ul style="list-style-type: none"> • Anzelle Wessels • Roger Hillen
Job Title	<ul style="list-style-type: none"> • Professional Practice – Assurance Technical Associate Partner • Professional Practice Director
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Question 1:

Do you support the proposed IRBA Rule on Enhanced Auditor Reporting for the Audit of Financial Statements? Yes / No.

If “No”, please indicate the reason(s) for your response.

We are in general supportive of IRBA’s initiative to enhance auditor reporting for the audit of financial statements, through the proposed IRBA Rule.

Our response to this specific question is structured in the same order as the Proposed IRBA Rule on Enhanced Auditor Reporting for the Audit of Financial Statements to provide detail comment on each section of the Proposed IRBA Rule.

Part 1(a) of the proposed IRBA Rule: *For all audits of annual financial statements, the audit firm shall disclose in the independent auditor’s report the materiality applied, and an explanation of significant judgements made by the auditor in determining materiality for the audit.*

We support part 1(a) of the proposed IRBA Rule as we continue to believe disclosing the materiality applied and an explanation of significant judgments made by the auditor in determining materiality for the audit in the auditor’s report may be useful to enhancing the user’s understanding of how the audit was performed.

We do however refer to our comment raised in the Comment Letter to the Consultation Paper: Enhanced Auditor Reporting dated 16 September 2021 where it was noted that we believe that this disclosure rule should be applicable to audits of Public Interest Entities, both listed and non-listed, whose financial statements are widely distributed, where we believe this will be of most use to the users.

Part 1(b) of the proposed IRBA Rule: *For all audits of annual financial statements, the audit firm shall disclose in the independent auditor's report, how the auditor evaluated management's assessment of the entity's ability to continue as a going concern and, where relevant, key observations arising with respect to that evaluation.*

We do not support proposed 1(b) of the proposed IRBA Rule. However, should the Rule be passed we believe such disclosure would be of most value to Public Interest Entities, both listed and non-listed. It is further noted that ISA (UK) 570 (Revised) requires this disclosure for listed entities and for Public Interest Entities only.

As per our response to your consultation paper on enhanced auditor reporting, we still believe that the audit approach and procedures performed to evaluate management's assessment of the entity's ability to continue as a going concern are mostly uniform for all entities. We recognise that the evaluation of the evidence, key assumptions and judgements would be unique for each entity. Although the disclosure of the auditor's evaluation of management's assessment would be of interest to the users, describing this would require setting out all the details from the forecasts and explaining in long form the conclusions reached on all procedures and the thinking in forming the final judgments. The auditor's evaluation may cause confusion to the users of the financial statements as to whether there is an uncertainty related to going concern or not, may attract unnecessary attention, and may detract from the fact that the entity is considered a going concern. In addition, for the disclosure to make most sense, we note that information might be required to be disclosed that is not contained in the financial statements themselves.

Furthermore, we commented that the auditors' assessment of going concern and the way in which the auditor concludes would require the auditor to agree with management on their assessment and for the summary of this assessment to be disclosed by management in the financial statement disclosure. ISA 570 (Revised) and the concept of fair presentation would require management to disclose all the matters giving rise to potential uncertainty along with their plans and other key assumptions and judgments made in concluding on whether or not such matters give rise material uncertainties related to going concern. Where there is a complex assessment of going concern due to the identification of indicators, this level of detail in the financial statement disclosure would always be required and only the conclusion made by management on whether there is material uncertainty would change in the financial statements and in the auditor's report. Therefore, the reader of the financial statements and the auditor's report would always be provided with the summarised details in the financial statements necessary to understand the conclusions. Replicating these same disclosures in the auditor's report would not further enhance the usefulness of the audit report to the users, but rather unnecessarily lengthen the audit report.

We believe the real concern may lie with the application of ISA 570 (Revised) by auditors in ensuring that management's disclosure is sufficiently detailed and provides sufficient clarity in how the going concern basis of preparation (with or without material uncertainty being concluded) was determined when there were indicators of uncertainty identified. Guidance in this area may therefore be a better solution even though it would continue to increase disclosure driven by the auditing standards rather than through the financial reporting framework. Nevertheless, increased disclosure from management on going concern would be best given in their assessment, and the auditor only audits such assessment and is not in fact opining discretely on the going concern position.

The auditor cannot disclose original client information in the auditor's report. The entity is required to disclose original information; however, the challenge is that there is no sufficiently available guidance on the expected level of disclosures by management in the financial statements on going concern. In this regard, we suggest that the IRBA engage with the South African Institute of Chartered Accountants (SAICA) so that they can be tasked with developing this guidance for companies in the South African environment to enhance understanding regarding going concern disclosure.

Part 1(c) of the proposed IRBA Rule: *For all audits of annual financial statements, the audit firm shall disclose in the independent auditor's report, audit procedures specific to the auditor's response to the material uncertainty related to going concern, where relevant.*

We support the Part 1(c) of the proposed IRBA Rule. However, we believe it should only be applicable to Public Interest Entities, both listed and non-listed, whose financial statements are widely distributed.

At a high level, the auditor's procedures to evaluate management's assessment of the entity's ability to continue as a going concern are set out in ISA 570 – Going Concern. These procedures remain largely the same between all entities with the differences being in the nuances of how the results are evaluated and interpreted. We do note that most assessments would comprise obtaining management's assessments along with their profit and cashflow forecasts. The auditor would then obtain evidence for the assumptions, assess the completeness of the forecasts against known conditions, loans, and other events and whether the forecasts incorporate management's plans and the overall reasonability of the forecasts considering these factors. The auditor may then stretch or adjust the forecasts for concerns to determine potential impacts. Based on the results from these steps, the auditor would assess his/her conclusion whether a material uncertainty exists or not. Setting out these procedures in the audit report using a generalised approach to reporting on going concern would likely not further enhance the understanding of the audit. The detailed considerations and analyses however could be useful information to the users which we believe should then be disclosed by management in their financial statements to which the auditors could reference.

Part 1(d) of the proposed IRBA Rule: *For all audits of annual financial statements, the audit firm shall disclose in the independent auditor's report, the following matters, where the disclosure has not been made by the preparer in the annual financial statements or the annual report:*

- i. Fees paid or payable to the firm and network firms for the audit of the financial statements on which the firm expresses an opinion.*
- ii. Fees, other than those disclosed under (d)(i), charged to the client for the provision of services by the firm or a network firm during the period covered by the financial statements on which the firm expresses an opinion. For this purpose, such fees shall only include fees charged to the client and its related entities over which the client has direct or indirect control that are consolidated in the financial statements on which the firm will express an opinion.*
- iii. Any fees, other than those disclosed under (d) (i) and(ii), charged to any other related entities over which the audit client has direct or indirect control for the provision of services by the firm or a network firm when the firm knows, or has reason to believe, that such fees are relevant to the evaluation of the firm's independence.*
- iv. If applicable, the fact that the total fees received by the firm from the audit client represent, or are likely to represent, more than 15% of the total fees received by the firm for two consecutive years, and the year that this situation first arose.*

We support part 1(d) of the proposed IRBA Rule though we believe it should only be applicable to audits of Public Interest Entities, both listed and non-listed.

As per our response to your consultation paper on enhanced auditor reporting, we believe that it is important that sufficient information and context is given about the non-audit fees to enhance transparency to users about the auditor's independence.

As mentioned in our general comments, we believe it will be necessary for the IRBA to consider how joint auditors should comply with part 1(d) of the proposed IRBA Rule.

Part 2(a) of the proposed IRBA Rule: *For the audit of all Public Interest Entities as defined in the IRBA Code, the audit firm, shall disclose in the independent auditor's report additional disclosures in the auditor's report about the scope of the audit in the context of group audits.*

We support part 2(a) of the proposed IRBA Rule. We believe disclosing the scope of the audit in relation to the group audit as done in the UK (number of in-scope locations and coverage of key financial metrics) may enhance

the users' understanding about how the group audit is conducted and may be able to bridge the expectation gap of users, regarding the extent of the audit performed.

We however want to emphasise our previous comment raised in our Comment Letter to the Consultation Paper, that we believe that this disclosure rule should be applicable to audits of listed entities and Public Interest Entities whose financial statements are widely distributed.

Part 2(b) of the proposed IRBA Rule: *For the audit of all Public Interest Entities as defined in the IRBA Code, the audit firm, shall disclose in the independent auditor's report the communication of Key Audit Matters, as defined in International Standard on Auditing 701 Communicating Key Audit Matters in the Independent Auditor's Report (ISA 701).*

We support part 2(b) of the proposed IRBA Rule.

Part 3 of the proposed IRBA Rule: *Where the auditor has communicated Key Audit Matters, as defined in ISA 701, the outcome of audit procedures or key observations with respect to Key Audit Matters shall be disclosed in the independent auditor's report.*

We do not support part 3 of the proposed IRBA Rule.

We do not believe that it is suitable to require the auditor to communicate the outcomes of audit procedures or key observations with respect to key audit matters communicated in the auditor's report.

As per our response to your consultation paper on enhanced auditor reporting, our reasons are as follows:

- It is clear within ISA 701 that key audit matters are not separate opinions on individual matters. The danger with requiring disclosures about the outcome of audit procedures or key observations with respect to key audit matters is that such disclosures could be interpreted by users as discrete opinions on specific elements of the financial statements. This could cause confusion for users around the understanding of the audits of financial statements and the overall reasonable assurance opinion expressed over the financial statements as a whole and has the potential to widen the knowledge gap about audits.
- We note that paragraph A46 of ISA 701 already provides for the auditor to apply professional judgment in communicating how a key audit matter was addressed and allows the auditor to provide an indication of the outcome of audit procedures or key observations with respect to the key audit matter. We do not believe it would be appropriate to mandate such disclosures by the auditor.
- Furthermore, we note that the spirit of ISA 701 is not to provide original information by auditors in the audit report, but that management provides the necessary disclosures of information relevant to users within the financial statements. We have reservations about disclosing key observations with respect to key audit matters which may constitute original information, for instance by noting whether an entity's assumptions are aggressive or conservative in nature to sector benchmarks which is not a disclosure required by IFRS.

Question 2:

Do you believe that there is guidance required in support of the proposed IRBA Rule on Enhanced Auditor Reporting for the Audit of Financial Statements? Yes / No.

If “yes”, please indicate the areas in which guidance is needed.

Yes, we believe guidance is required in support of the proposed IRBA Rule on Enhanced Auditor Reporting for the Audit of Financial Statements. We further believe that it is vital that such guidance be issued and available well in advance of the effective date of the proposed IRBA Rule.

Like Question 1, our response to this specific question is structured in the same order as the proposed IRBA Rule. Our responses therefor will provide detail comment on the guidance required on each section of the proposed IRBA Rule.

Part 1(a) of the proposed IRBA Rule: *For all audits of annual financial statements, the audit firm shall disclose in the independent auditor's report the materiality applied, and an explanation of significant judgements made by the auditor in determining materiality for the audit.*

We believe that guidance is required to support Part1(a) of the proposed IRBA rule to provide clarity on the nature and extent of disclosures required in disclosing an explanation of significant judgements made by the auditor in determining materiality for the audit.

As per our response to your consultation paper on enhanced auditor reporting dated 16 September 2021, we believe that specific guidance should be provided about what to disclose in respect of materiality to result in some consistency and to allow evaluations across the different methodologies adopted by audit firms. We note the following points:

- We believe that if the materiality amount should be disclosed this should be accompanied by disclosure on the benchmark used, the percentage used and the primary reason(s) for using the benchmark. Clear guidance should also be provided on what and the extent to which other significant judgments that were made by the auditor to determine materiality should be disclosed in the auditor's report. For example, whether the auditor merely states that the basis was adjusted or normalised or whether such adjustment or normalisation needs to be further clarified as part of the disclosure in the auditor's report.
- Additional guidance may also be needed on disclosure of the different benchmark base options the auditor considered / was able to consider based on the methodology used.
- There may also be cases where there are no significant judgments made in determining materiality on an engagement. As such, we believe that guidance should be provided on how to implement part 1(a) regarding “explanation of significant judgments” in such cases.
- Guidance should also clarify whether the auditor should disclose any changes in the materiality amount between the planning and execution of the audit and the final materiality amount, or simply disclose the final materiality amount. Although this disclosure may be useful, we also recognised that the concept of materiality is complex, and that disclosing various materiality thresholds at planning and final may create unintended confusion to the users. On balance, we suggest that only the final materiality should be disclosed without any further explanation on the change in the materiality amount from planning to final.
- There may be circumstances where different materiality amounts apply to one engagement. For example, when an auditor is engaged to audit Collective Investments Schemes, a different materiality amount is calculated for each fund, however one auditor's report is issued for the audit engagement of the Collective Investment Scheme. As a result of this circumstance and any other similar circumstances that may arise, guidance should be provided in what manner materiality amount(s) should be disclosed in the auditor's report.

Part 1(b) of the proposed IRBA Rule: *For all audits of annual financial statements, the audit firm shall disclose in the independent auditor's report how the auditor evaluated management's assessment of the entity's ability to continue as a going concern and, where relevant, key observations arising with respect to that evaluation.*

We believe that guidance is required to support Part 1(b) of the proposed IRBA Rule.

Should part 1(b) of the Rule be passed, we believe that guidance is necessary on the nature and extent of what the auditor should disclose in the auditor's report on how the auditor evaluated management's assessment of the entity's ability to continue as a going concern and, where relevant, key observations arising with respect to that evaluation.

The guidance should clarify:

- The extent of detail the auditor is expected to disclose in the auditor's report as it relates to the auditor's evaluation of management's assessment.
- What is meant by "key observations" that the auditor should disclose about the evaluation.
- How key observations should be described to avoid wording that suggests discrete opinions being provided or that might cause confusion to the users.

Part 1(c) of the proposed IRBA Rule: *For all audits of annual financial statements, the audit firm shall disclose in the independent auditor's report audit procedures specific to the auditor's response to the material uncertainty related to going concern, where relevant.*

We believe that guidance is required to support 1(c) of the proposed IRBA Rule.

Should part 1(c) of the Rule be passed, we believe that guidance is necessary on the extent of detail the auditor is expected to disclose in the auditor's report as it relates to audit procedures specific to the auditor's response to the material uncertainty related to going concern.

The guidance should address the balance that should be achieved by ensuring the disclosures are not overly boiler plate nor overly complex which would not enhance the users understanding and thus not be useful. The guidance should also address the matter of not providing original information (much like ISA 701) by auditors in the audit report, but that management provides the necessary disclosures of information relevant to users within the financial statements.

Part 1(d) of the proposed IRBA Rule: *For all audits of annual financial statements, the audit firm shall disclose in the independent auditor's report the following matters, where the disclosure has not been made by the preparer in the annual financial statements or the annual report:*

- Fees paid or payable to the firm and network firms for the audit of the financial statements on which the firm expresses an opinion.*
- Fees, other than those disclosed under (d)(i), charged to the client for the provision of services by the firm or a network firm during the period covered by the financial statements on which the firm expresses an opinion. For this purpose, such fees shall only include fees charged to the client and its related entities over which the client has direct or indirect control that are consolidated in the financial statements on which the firm will express an opinion.*
- Any fees, other than those disclosed under (d) (i) and(ii), charged to any other related entities over which the audit client has direct or indirect control for the provision of services*

by the firm or a network firm when the firm knows, or has reason to believe, that such fees are relevant to the evaluation of the firm's independence.

- iv. *If applicable, the fact that the total fees received by the firm from the audit client represent, or are likely to represent, more than 15% of the total fees received by the firm for two consecutive years, and the year that this situation first arose.*

We believe that guidance is required even though it was not noted as “IRBA Guidance Required” in the Summary of the Results Table included in the Explanatory Memorandum.

As per our response to your consultation paper on enhanced auditor reporting, we believe that regardless of whether the disclosures of fees paid to the auditor(s) is made by management or the auditor, we have identified the following practical challenges which we believe required further consideration and guidance from IRBA:

- In instances where joint audits are conducted which is required for Banks per the Banks Act No. 94 of 1990, consideration should be given whether the fees paid to the joint auditors should be disclosed as a singular amount for matters (i) to (iv) or split between each joint auditor.
- In instances where non-audit or non-assurance services are required to be performed by auditors, which we experience in the banking and insurance industries, simply disclosing the quantum of these fees paid may lack clarity to users without the context being provided. Therefore, consideration should be given whether additional explanations by management or in the auditor's report may provide more understanding to users.
- Where fees are paid other than for audit services and assurance services, consideration should be given whether the other fees that relate to various services should be disclosed separately and the extent of categorisation. Such groupings may include:
 - A. The statutory audit including all interim and other similar reporting required by law (Example: JSE Listings requirements) with each being disclosed as sub-components and the reason,
 - B. Assurance work required by the other regulators,
 - C. Assurance or related assurance work (ISRS 4400) requested by entity and
 - D. All other non-assurance work.

More detailed information such as this would provide a better and more transparent view of the impacts of the work on independence and the relationship between the auditor and the company.

- In group audits where the audit involves the component auditors which are not within the same network of firms as the group auditor, consideration should be given as to whether fees paid only to the group auditor and its network of firms is disclosed, or whether fees paid to non-network firms over the group audit should be disclosed separately.
- Where part (iv) is applicable, if total fees received by the firm from the audit client exceeds 15% of the total fees received by the firm in two consecutive years is being disclosed in isolation without further explanation about the auditor's safeguards to the threat to independence, this may not be useful to the users. Consideration should be given whether and how to further provide context as to the safeguards put in place by the auditor which may be more useful.

Part 2(a) of the proposed IRBA Rule: *For the audit of all Public Interest Entities as defined in the IRBA Code, the audit firm, shall disclose in the independent auditor's report additional disclosures in the auditor's report about the scope of the audit in the context of group audits.*

We believe guidance is required to support Part 2(a) of the proposed IRBA rule.

We suggest the disclosures about the scope of the audit to be aligned to the requirements in the UK and limited to the extent of components that are in-scope for the group audit and coverage of key financial metrics. Guidance should be provided to assist the overall consistencies for disclosing the number of in-scope components and the coverage of the audit.

We also note below some concerns around the practical application which would require further guidance:

- What is meant with “additional disclosures” to direct the extent of disclosure;
- Guidance is required to clarify whether to include comparatives as part of the disclosure in the auditor’s report or not, and if we are required to include comparatives what to disclose if it is an initial audit; and
- What to disclose for a PIE audit if it is not a group context.

Number of “in-scope” components

- Guidance is required on the determination of the number “in-scope” components to be disclosed. For instance, the group auditor may determine that some components between “full scope” and “specific scope” where audit work is performed, and some “review scope” which entails analytical procedures. Clarity would need to be provided whether only components where audit work is performed can count towards the number of components in-scope and towards coverage, or whether this can and should also include review scope components. We also suggest such disclosures are kept at a high level and in a precise and concise manner to enable the users to understand the audit rather than create confusion, such as simply describing the total number of components and the total coverage, rather than going into detail about the scope assigned. Noting scope would in our view require more detail for it to be relevant. The percentage coverage would then need to be outlined per scope per metric rather than using number of components per scope; and
- Whether to include the names of the in-scope components in the proposed disclosure.

Coverage of Key financial Metrics

Guidance should be provided to promote consistency of the application by various auditors and audit firms in the calculation of the coverage of the audit for each key financial metric. The guidance should clarify:

- Which metrics should be disclosed: We suggest that the metrics to be focused on should be similar to the UK, i.e., revenue, profit before tax and assets. However, should the benchmark used to determine materiality be a different metric, we believe the coverage on that metric should also be disclosed;
- We also note that key financial metrics for listed entities and non-listed Public Interest Entities may be different. Key financial metrics between listed entities may also be different based on the nature of the entity and focus of the users. Which key metric to use should thus not be rigidly applied;
- The effects of consolidation and inter-company adjustments: We are conscious that consolidation and inter-company adjustments are often necessary between the financial reporting of a component and that of the consolidated group financial information. Clarity should be provided whether the calculation of coverage should be based on amounts before or after consolidation adjustments. This can often lead to vastly different outcomes, and at the same time, it may be difficult to calculate the post-consolidation coverage for large group structures with complex consolidation adjustments or processes; and
- When divestments in components occur that results in the separate presentation of financial performance for continuing and discontinued operations, users may be interested as to the scoping of the audit between the continuing and discontinued operations, for example, the number of in-scope components and/or the coverage of the audit shown separately for continuing and discontinued operations.

Part 2(b) of the proposed IRBA Rule: *For the audit of all Public Interest Entities as defined in the IRBA Code, the audit firm, shall disclose in the independent auditor’s report the communication of Key Audit Matters, as defined in International Standard on Auditing 701 Communicating Key Audit Matters in the Independent Auditor’s Report (ISA 701)*

We do not believe guidance is required for Part2(b) of the proposed IRBA Rule as the existing guidance in *International Standard on Auditing 701 Communicating Key Audit Matters in the Independent Auditor’s Report (ISA 701)* suffice.

Part 3 of the proposed IRBA Rule: *Where the auditor has communicated Key Audit Matters, as defined in ISA 701, the outcome of audit procedures or key observations with respect to Key Audit Matters shall be disclosed in the independent auditor's report.*

Yes, should the Rule be passed, we believe that additional guidance would be necessary for auditors on how to describe outcomes or key observations while at the same time avoiding wording that suggests discrete opinions or that might cause confusion to the users.

We believe that it is especially important to note in the description of the outcome that the outcome is written in the context of the financial statements taken as a whole to provide clarity that the communication of the outcome is not a piecemeal opinion.

Example illustration

*"... Taking this into consideration, based on the results of our audit procedures performed, which is consistent with Management's assessment, we consider the estimates prepared by the Company and the related disclosures acceptable, **in the context of the financial statements as a whole.**"*

The guidance should also clarify the extent of disclosure required regarding the outcome of audit procedures. The guidance should further clarify whether the outcome of audit procedures **and** key observations disclosures are required for each key audit matter or does the auditor have optionality in disclosing key observations or the outcome of audit procedures.

Question 3:

Do you agree with the effective date for the proposed IRBA Rule on Enhanced Auditor Reporting for the Audit of Financial Statements, as indicated in paragraph 29 of the Explanatory Memorandum? Yes / No.

If "No", please indicate the reason(s) for disagreeing and also suggest an effective date what will be appropriate.

We support the effective date. However, we believe it is vital that all of the guidance to the Proposed IRBA rule should be issued and available well in advance of the effective date of the Proposed IRBA Rule.