AUDITOR REPORTING: FREQUENTLY ASKED QUESTIONS

This publication has been prepared by the Auditor Reporting Implementation Working Group (ARIWG). It does not constitute an authoritative pronouncement of the International Auditing and Assurance Standards Board (IAASB), nor does it amend or override the International Standards on Auditing (ISAs). Further, this publication is not meant to be exhaustive and reading this publication is not a substitute for reading the ISAs.

The IAASB's new and revised Auditor Reporting standards[1] and ISA 720 (Revised)[2] (the Standards) were issued in January 2015 and April 2015 respectively, and become effective for periods ending on or after December 15, 2016. Since the Standards were issued, the IAASB has performed extensive outreach across numerous jurisdictions to encourage the adoption and support the implementation of the Standards. More recently, the IAASB has heard from stakeholders regarding actual experiences in implementing the new Standards, including practical challenges or areas where there are common differences in interpretation of the Standards. Accordingly, the ARIWG has developed this publication to address some of the common questions relating to the requirements in the ISAs. This publication does not address the responsibilities of the auditor that may exist in law, regulation or national standards, which may contain requirements in addition to those established by the Standards.

The New and Revised Auditor Reporting Standards

1. **Paragraph 5 of ISA 701 indicates that ISA 701 applies to:**

   - **Audits of complete sets of general purpose financial statements of listed entities.**
   - **Circumstances when the auditor is required by law or regulation to communicate key audit matters (KAM) in the auditor's report.**
   - **Circumstances when the auditor otherwise decides to communicate KAM in the auditor's report.**

   (a) Which entities are considered to be "listed entities" when applying ISA 701?

   ISA 220[3] defines a listed entity as follows:

   > An entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are marketed under the regulations of a recognized stock exchange or other equivalent body.

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[1] The new and revised Auditor Reporting Standards comprise ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*; New ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*; ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*; ISA 706 (Revised), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*; ISA 570 (Revised), *Going Concern*; ISA 260 (Revised), *Communication with Those Charged with Governance*; and conforming amendments to other ISAs.

[2] ISA 720 (Revised), *The Auditor's Responsibilities Relating to Other Information*

[3] ISA 220, *Quality Control for an Audit of Financial Statements*

The determination of which entities fall within that definition can only be established at a jurisdictional level. The National Standard Setter (NSS) or others with the appropriate authority in the jurisdiction typically would make that determination.

The determination of whether a stock exchange is "recognized" may include consideration of matters such as the following:

(i) Whether the exchange is a public exchange.

(ii) Whether there is a generally accepted framework, criteria or standards that govern admission to listing on the exchange (e.g., "listing rules").

(iii) Whether the exchange on which entities' shares are traded sets forth trading related regulations, for example, those in respect of offering securities to the public, announcements etc.

In some jurisdictions, listed entities may form part of a broader definition of "public interest entity," with a requirement in the jurisdiction that all public interest entities comply with the requirements in the ISAs that apply to audits of financial statements of listed entities.

(b) When the auditor is required to communicate KAM in respect of the audit of the consolidated financial statements, and the auditor is also required to express an audit opinion (in either the same auditor's report or in a separate auditor's report) on the separate financial statements of the parent or holding company (hereinafter referred to as separate financial statements), is the auditor also required to communicate KAM in respect of the audit of the separate financial statements?

Paragraph 5 of ISA 701 indicates that the standard applies to audits of complete sets of general purpose financial statements of listed entities. Paragraph 8 of ISA 700 (Revised) states "the requirements of the applicable financial reporting framework determine the form and content of the financial statements, and what constitutes a complete set of financial statements."

Accordingly, the determination of whether the communication of KAM is required in respect of the audit of the separate financial statements depends on whether the separate financial statements are viewed as a complete set of general purpose financial statements (as defined in paragraph 7(b) of ISA 700 (Revised)) under the requirements of the applicable financial reporting framework.

In circumstances where the separate financial statements are not a complete set of general purpose financial statements under the applicable financial reporting framework, the auditor may voluntarily communicate KAM.

There are a variety of possible scenarios regarding the presentation of the consolidated and separate financial statements. For example, the consolidated and separate financial statements could be presented in separate annual reports, presented as discrete financial statements in a single document (e.g., in separate sections of a single annual report), or presented side-by-side in a single annual report (also known as a four-column format). The table in the Appendix sets out these circumstances and how KAM could be presented.

Regardless of how the consolidated and separate financial statements and related auditor's report(s) are presented, the auditor would need to determine KAM in respect of the audit of the consolidated financial statements, and KAM in respect of the audit of the separate financial statements. In making this determination, the auditor may identify a matter that gives rise to KAM for both audits. For example, a cash generating unit that is experiencing deteriorating financial performance may affect both audits, but in different ways -- the estimate of the impairment of goodwill for the audit of the consolidated financial statements, and the valuation of the underlying investment for the audit of the separate financial statements. Accordingly, when describing such KAM in the auditor's report(s), the description should be tailored to each of the respective audits.

2. **Can the auditor's report refer to the International Standards on Auditing (ISAs) if the jurisdiction has not adopted the new and revised Auditor Reporting standards as of their effective date?**

Paragraph 18 of ISA 200[4] indicates that the auditor shall comply with all ISAs relevant to the audit, and that an ISA is relevant to the audit when the ISA is in effect and the circumstances addressed by the ISA exist.[5] In addition, paragraph 20 of ISA 200 indicates that the auditor shall not represent compliance with ISAs in the auditor's report unless the auditor has complied with the requirements of ISA 200 and all other ISAs relevant to the audit.

Paragraph 4 of ISA 700 (Revised) highlights that consistency in the auditor's report, when the audit has been conducted in accordance with ISAs, promotes credibility in the global marketplace by making more readily identifiable those audits that have been conducted in accordance with globally recognized standards. Assuming the jurisdiction has a program in effect for the adoption of the ISAs, the timing of the adoption of the new and revised auditor reporting standards for a particular jurisdiction would be determined by the NSS, or another authority as appropriate. It is recognized that there are jurisdictions that, based on their ISA adoption program, will only adopt the new and revised auditor reporting standards after the effective date of December 15, 2016. NSS (or another authority as appropriate) in those jurisdictions would need to ascertain how best to indicate in the auditor's report which auditing standards have been applied so as not to inappropriately represent compliance with the full suite of ISAs in effect for audits of financial statements with periods ending on or after December 15, 2016. For example, the auditor's report could instead refer to the jurisdictional (i.e., national) auditing standards and the NSS could provide transparency on its website about its ISA adoption program.

A similar principle would apply when complying with paragraph 28(c) of ISA 700 (Revised). In circumstances when the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) has not been adopted in full in the jurisdiction, NSS in that jurisdiction would need to specify how the relevant ethical requirements should be described in the auditor's report in the jurisdiction, so as not to inappropriately represent compliance with the IESBA Code in effect at the time the auditor's report is issued. For example, the auditor's report could instead refer to the jurisdiction of origin of the relevant ethical requirements and the NSS, or other body that

[4] ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

[5] Paragraph 21 of ISA 210, *Agreeing the Terms of Audit Engagements,* also addresses circumstances where law or regulation of the relevant jurisdiction prescribes the layout or wording of the auditor's report in a form or in terms that are significantly different from the requirements of the ISAs.

prescribes the relevant ethical requirements such as a regulator or professional organization, could provide transparency on its website about what such ethical requirements comprise.

3. **Can the auditor's report indicate that the audit was conducted in accordance with the ISAs and the auditing standards of a specific jurisdiction?**

Question 2 addresses the considerations regarding whether the auditor's report may refer to the ISAs if the jurisdiction has not adopted the new and revised Auditor Reporting standards.

In some circumstances, the audit is conducted in accordance with the ISAs, as well as the auditing standards of a specific jurisdiction (national auditing standards). Paragraph 51 of ISA 700 (Revised) indicates that in such cases, the auditor's report may refer to the ISAs in addition to the national auditing standards, but the auditor shall do so only if:

(a) There is no conflict between the requirements in the national auditing standards and those in ISAs that would lead the auditor (i) to form a different opinion, or (ii) not to include an Emphasis of Matter (EOM) paragraph or Other Matter (OM) paragraph that, in the particular circumstances, is required by ISAs; and

(b) The auditor's report includes, at a minimum, each of the elements set out in paragraphs 50(a)–(o) of ISA 700 (Revised) when the auditor uses the layout or wording specified by the national auditing standards.

If the auditor is unable to meet the requirements in paragraph 51, the auditor may have no alternative but to issue two separate auditor's reports: an auditor's report that relates to the audit conducted in accordance with the ISAs (provided that the minimum elements required by ISA 700 (Revised) are included in such report), and an auditor's report that relates to the audit conducted in accordance with national auditing standards.

In circumstances where the auditor meets the requirements in paragraph 51 and issues an auditor's report that refers to both the ISAs and the national auditing standards, paragraph 52 of ISA 700 (Revised) indicates that the auditor's report shall identify the jurisdiction of origin of the national auditing standards.

4. **What is the effect, if any, on the KAM previously communicated in the auditor's report in circumstances when the auditor reissues the report or amends the report previously issued?**

In certain circumstances under ISA 560,[6] the auditor may be required to issue a new auditor's report or amend the auditor's report previously issued. For example, this may occur when facts become known to the auditor after the financial statements have been issued that may have caused the auditor to amend the auditor's report had such facts been known to the auditor at the date of the auditor's report. In this circumstance, if management amends the financial statements, ISA 560 requires that an EOM paragraph or OM paragraph be included in the new or amended auditor's report that refers to a note to the financial statements that more extensively discusses the reason for the amendment of the previously issued financial statements and to the earlier report provided by the auditor.

Although the auditor is required to include an EOM or OM paragraph in the auditor's report to comply with the ISA 560 requirement, ISA 706 indicates that an EOM or OM paragraph cannot be a substitute

[6] ISA 560, *Subsequent Events*

for a KAM when KAM are communicated. In circumstances where the auditor reissues the auditor's report, the auditor therefore may also need to consider whether the matter that has resulted in the new or amended auditor's report (i) gives rise to an additional KAM that should be communicated, or (ii) relates to a matter previously communicated as a KAM and whether revisions to the description of that KAM are therefore necessary. Other matters previously communicated as KAM are not likely to be affected because such matters were previously determined to be matters of most significance in the audit for purposes of the original auditor's report.

Considering whether any updates to the KAM may be necessary, in addition to the EOM or OM paragraph required by ISA 560, relates to the objective of communicating KAM. The description of a KAM is intended to provide additional information to intended users of the financial statements beyond what is included in an EOM paragraph (i.e., more than a reference to the matter being emphasized and to relevant disclosures in the financial statements). The auditor also may consider cross-referencing the respective descriptions in the EOM or OM paragraph and the updated KAM in the auditor's report to clarify that both are in respect of the same matter.

5. **Should KAM be communicated in respect of each period for which the financial statements are presented when comparative financial statements[7] are presented?**

Paragraph 10 of ISA 701 indicates that the auditor shall determine which of the matters were of most significance in the audit of the financial statements of the <u>current</u> period. Paragraph A10 of ISA 701 states that the auditor's determination of KAM is limited to those matters of most significance in the audit of the financial statements of the current period, even when comparative financial statements are presented. The IAASB's decision to limit the KAM to the audit of the current period was primarily because of its understanding that users are interested in the most recent information to make informed decisions, and therefore are more likely to value information from the auditor about matters of significance in the audit of the current period. Furthermore, the IAASB believed that there are practical challenges in communicating KAM in relation to the prior period, which could also further lengthen the auditor's report and result in a presentation that could be potentially confusing to users.

6. **Are all significant risks considered to be KAM?**

Paragraphs 14–17 of ISA 260 (Revised) require the auditor to communicate various matters with those charged with governance (TCWG), including the auditor's responsibilities in relation to the audit, the planned scope and timing of the audit, significant findings from the audit and auditor independence. In this regard, the auditor is required to communicate about the significant risks identified by the auditor, as part of communicating an overview of the planned scope and timing of the audit.

From those matters communicated with TCWG, the auditor determines the matters that required <u>significant auditor attention</u>. From the matters that required significant auditor attention, the auditor determines which were the <u>matters of most significance</u> and therefore are the key audit matters.

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[7] In terms of ISA 710, *Comparative Information—Corresponding Figures and Comparative Financial Statements,* comparative financial statements exist when amounts and other disclosures for the prior period are included for comparison with the financial statements of the current period but, if audited, are referred to in the auditor's opinion. Under paragraph 15 of ISA 710, when comparative financial statements are presented, the auditor's opinion should refer to each period for which financial statements are presented and on which an audit opinion is expressed.

Paragraphs A27–A30 of ISA 701 provide guidance and factors that may influence this determination. This process is depicted in a publication of the IAASB, *Determining and Communicating KAM*.

Paragraph A20 of ISA 701 explains that areas of significant management judgment and significant unusual transactions may often be identified as significant risks and therefore significant risks are often areas that require significant auditor attention. However, paragraph A21 of ISA 701 highlights that this may not be the case for all significant risks. For example, ISA 240[8] presumes that there are risks of fraud in revenue recognition and management override of controls and accordingly requires the auditor to treat these assessed risks of material misstatement due to fraud as significant risks. Depending on their nature, these risks may not require significant auditor attention, and therefore would not be considered KAM.

Other Information

7. **Can the auditor's report refer to the ISAs if the jurisdiction has not adopted ISA 720 (Revised)?**

As explained in question 2, paragraph 18 of ISA 200 indicates that the auditor shall comply with all ISAs relevant to the audit, and that an ISA is relevant to the audit when the ISA is in effect and the circumstances addressed by the ISA exist. Furthermore, paragraph 20 of ISA 200 indicates that the auditor shall not represent compliance with ISAs in the auditor's report unless the auditor has complied with the requirements of ISA 200 and all other ISAs relevant to the audit.

Assuming the jurisdiction has a program in effect for the adoption of the ISAs, the timing of the adoption of ISA 720 (Revised) for a particular jurisdiction would be determined by the NSS, or other authority as appropriate. It is recognized that there are jurisdictions which, based on their ISA adoption program, will only adopt ISA 720 (Revised) after the effective date of December 15, 2016. NSS in those jurisdictions would need to ascertain how best to reflect which auditing standards have been applied so as not to inappropriately represent compliance with the full suite of ISAs in effect at December 15, 2016. For example, the auditor's report could instead refer to the jurisdictional (i.e., national) auditing standards and the NSS could provide transparency on its website about its ISA adoption program.

8. **What are the auditor's reporting responsibilities with respect to other information?**

The requirements in ISA 720 (Revised) apply to all audits when other information is presented in an annual report (as defined by ISA 720 (Revised)). Paragraph 21 of ISA 720 (Revised) requires the auditor to include a separate section in the auditor's report with a heading "Other Information" (or other appropriate heading) when, at the date of the auditor's report:

- For a listed entity, the auditor has obtained, or expects to obtain, the other information; or
- For an entity other than a listed entity, the auditor has obtained some or all of the other information.

[8] ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

The Other Information section of the auditor's report includes in all cases:

- A statement that management is responsible for the other information;
- A statement that the auditor's opinion does not cover the other information and, accordingly, that the auditor does not express (or will not express) an audit opinion or any other form of assurance conclusion thereon; and
- A description of the auditor's responsibilities relating to reading, considering and reporting on the other information as required by ISA 720 (Revised).

In addition, the following information is included depending on whether the entity being audited is listed or not, and the status of the other information received by the auditor as of the report date:

Status of the other information received	Listed entities	Entities other than listed entities
The auditor has obtained some or all of the other information at the date of the auditor's report	• Identification of the other information obtained prior to the date of the auditor's report • In respect of information obtained prior to the date of the auditor's report, either: ○ A statement that the auditor has nothing to report; or ○ If the auditor has concluded that there is an uncorrected material misstatement of the other information, a statement that describes the uncorrected material misstatement of the other information	The same requirements apply as for audits of listed entities
The auditor expects to obtain other information after the date of the auditor's report	• Identification of the other information expected to be obtained after the date of the auditor's report	No reporting required, although the auditor still has responsibilities under ISA 720 (Revised) to perform the necessary procedures on the other information

9. **What are the auditor's responsibilities in relation to other information in circumstances when the auditor reissues the report or amends the report previously issued?**

In certain circumstances under ISA 560, the auditor may be required to issue a new auditor's report or amend the auditor's report previously issued. For example, this may occur when facts become known to the auditor after the financial statements have been issued, that may have caused the auditor to amend the auditor's report had such facts been known to the auditor at the date of the auditor's report.

In circumstances when the auditor provides a new auditor's report, or amends the auditor's report that was previously issued, the auditor may need to reconsider the auditor's responsibilities relative to the other information, the nature and extent of which would depend on whether the auditor restricts the audit procedures on subsequent events to the amendment of the financial statements:

(a) *The auditor is permitted to restrict the audit procedures on subsequent events to the effects of the subsequent event or events causing the amendment, i.e., the circumstances in paragraph 12 of ISA 560 apply*. In such cases, the auditor's responsibility relates to (i) considering the effect on the other information as reported in the auditor's report that was previously issued, and (ii) determining whether updates to the Other Information section in the auditor's original report are necessary. With respect to other information that the auditor previously reported on, the auditor needs to consider whether appropriate updates have been made to the other information in relation to the subsequent event and the auditor may need to revise the Other Information section of the auditor's report to refer to the amended other information. The auditor is not required to report on any other information obtained after the date of the original report.

(b) *The auditor does **not** restrict the audit procedures on subsequent events to the amendment of the financial statements, i.e., the circumstances in paragraph 12 of ISA 560 do not apply.* In such cases, the Other Information section in the reissued auditor's report would cover all other information obtained as of the date of the reissued report. For audits of listed entities, the Other Information section would need to be updated to identify any other information that is expected to be obtained after the date of the auditor's report.

In both cases, the auditor would still be responsible for performing the necessary procedures on any other information obtained after the date of the auditor's report, as described in paragraph 19 of ISA 720 (Revised).

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Appendix

Presentation of KAM when it has been determined that KAM are required to be communicated in respect of the audit of the separate financial statements[9]

Consolidated and separate financial statements presented in separate documents	Consolidated and separate financial statements presented discretely in a single document	Financial statements presented side-by-side in a single document (4-column format)
In such a case, it is presumed that the auditor would prepare separate auditor's reports on the consolidated and separate financial statements as the related audited financial statements are contained in separate documents. The KAM in respect of the audit of each set of financial statements should be clearly described in each report, since each report should comply with the requirements of paragraph 30 of ISA 700 (Revised). This paragraph indicates that ISA 701 is required to be applied in its entirety for an audit of a complete set of general purpose financial statements of a listed entity.	In such a case, there are two possibilities: • A single auditor's report addressing both sets of financial statements. In such a case the considerations in the column to the right would apply. • Separate auditor's reports for each set of financial statements. In such a case the auditor's reports would need to be standalone, that is, the auditor would need to fully comply with the requirements of paragraph 30 of ISA 700 (Revised) for each report. Accordingly, merely including a cross-reference in the auditor's report on the separate financial statements to the KAM in the auditor's report on the consolidated financial statements would be insufficient.	Because the auditor in this case would likely issue a single auditor's report addressing both the consolidated and separate financial statements, the single report would include KAM relating to the audits of both sets of financial statements. This could be presented in a variety of ways, for example: • Indicating for each KAM how it applies to each audit, i.e., the audit of the consolidated and separate financial statements (see last paragraph of question 1(b) of this FAQ). • Presenting the KAM for the consolidated financial statements in one section, and those for the separate financial statements in another section (the auditor could cross-refer to the related KAM in the respective sections if the auditor believes it appropriate and useful to do so).

9 That is, the separate financial statements are considered to be a complete set of general purpose financial statements. Furthermore, it is presumed in these scenarios that there are KAM to communicate in respect of both the audit of the consolidated and separate financial statements (see paragraph A59 of ISA 701, which indicates that it may be rare that the auditor would not determine at least one KAM to be communicated in the auditor's report).

Consolidated and separate financial statements presented in separate documents	Consolidated and separate financial statements presented discretely in a single document	Financial statements presented side-by-side in a single document (4-column format)
		• When each of the KAMs and their related effect on the audit is the same for the audit of the separate financial statements and the audit of the consolidated financial statements, it may be appropriate to include a general statement in the single auditor's report to indicate that the KAM apply to both the audit of the consolidated and separate financial statements.

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