

Key updates on auditing and assurance

In response to calls from investors, analysts and other users of audited financial statements, in the wake of the global financial crisis, for the auditor to provide more relevant information in the auditor's report, the IAASB has embarked on key projects on auditor reporting and audit quality.

Auditor reporting

In May 2011, the IAASB issued a consultation paper, *Enhancing the Value of Auditor Reporting: Exploring Options for Change*. Its objectives are to:

- (i) Determine whether there are common views among key users and other parties to the financial reporting process about the usefulness and relevance of auditor reporting, and
- (ii) Obtain views about the extent to which an expectations gap or information gap exists.

The consultation paper also sought views about possible options for enhancing the quality, relevance and value of auditor reporting, implications for change and potential implementation challenges, and whether there were factors that would lead to different solutions for different types of entities.

In September 2011, the Institute provided the IAASB with a comment letter. The Institute believes that the reality is that there are both "expectation" and "information" gaps and action will have to be taken to address various perceptions of auditor reporting. It is particularly important to address the "information gap" as mentioned in the consultation paper, as this has implications for the efficiency of capital markets and the cost of capital. The IAASB received more than 80

comment letters on the consultation paper.

Following that, the IAASB issued a consultation document in June 2012, *Invitation to Comment: Improving the Auditor's Report*. The document set out the IAASB's indicative direction proposed for the future auditor's report. A proposed new section in the auditor's report, "Auditor Commentary," was envisaged to be the mechanism by which auditors may draw attention to matters that are, in the auditor's judgment, likely to be most important to the users' understanding of the audited financial statements and the audit.

There were also suggested improvements with respect to new disclosures regarding going concern and other information in documents containing the audited financial statements, the description of the responsibilities of the auditor and key features of the audit itself, and enhancement to the format of the report. As part of the outreach programme, conducted in association with this consultation, the IAASB held three global roundtables in September and October 2012. The Institute's auditing and assurance standards committee chair and executive director attended the Kuala Lumpur roundtable on 8 October 2012. During the same month, the Institute also provided the IAASB with a comment letter.

The IAASB received more than 165 comment letters on the consultation document. The Institute's comments were generally consistent with the comments expressed by most of commentators representing the profession, in particular concerns as to the extent of information provided under "Auditor Commentary."

In July, the IAASB issued an exposure draft, *Reporting on Audited Financial Statements: Proposed New and Revised*

International Standards on Auditing (ISAs). This exposure draft includes proposed new ISA 701 *Communicating Key Audit Matters in the Independent Auditor's Report*, and a number of proposed revised ISAs, including the following:

- Proposed ISA 700 (Revised) *Forming an Opinion and Reporting on Financial Statements* - A proposed standard to establish new required reporting elements, and to illustrate these new elements in example auditor's reports. The IAASB is in the process of considering comments on the exposure draft of proposed ISA 720 (Revised) *The Auditor's Responsibilities Relating to Other Information in Documents Containing or Accompanying Audited Financial Statements and the Auditor's Report Thereon*. Pending finalization of proposed ISA 720 (Revised), proposed ISA 700 (Revised) includes a requirement for the auditor to report in accordance with proposed ISA 720 (Revised), and the illustrative auditor's reports therein include a placeholder for a section on "Other Information." These elements of proposed ISA 700 (Revised) will be finalized when the revision of ISA 720 is completed, such that reporting on other information will come into effect at the same time as the other enhancements addressed by the proposed ISAs.
- Proposed ISA 701 *Communicating Key Audit Matters in the Independent Auditor's Report* - A new standard to establish requirements and guidance for the auditor's determination and communication of key audit matters. Key audit matters, which are selected from matters communicated with those charged with governance, are required to be communicated in

an auditor's report for audits of financial statements of listed entities. The proposed new ISA 701 directs auditors of financial statements of listed entities to communicate in their report those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements.

- Proposed ISA 260 (Revised) *Communication with Those Charged with Governance* – To require auditor communications with those charged with governance, including proposed communication about the significant risks identified by the auditor, in light of proposed ISA 701.
- Proposed ISA 570 (Revised) *Going Concern* – To establish auditor reporting requirements relating to going concern, and to illustrate this reporting within the auditor's report in different circumstances.
- Proposed ISA 705 (Revised) *Modifications to the Opinion in the Independent Auditor's Report* – To clarify how the new required reporting elements of proposed ISA 700 (Revised) are affected when the auditor expresses a modified opinion, and to update the illustrative auditor's reports accordingly.
- Proposed ISA 706 (Revised) *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report* – To clarify the relationship between "Emphasis of Matter" paragraphs, "Other Matter" paragraphs and the "Key Audit Matters" section of the auditor's report.

The Institute has issued an invitation to comment on the IAASB's exposure draft, with comments requested by 29 October.

Auditor responsibilities relating to other information

In November 2012, the IAASB issued an exposure draft on proposed ISA 720 (Revised) *The Auditor's Responsibilities Relating to Other Information in Documents Containing or Accompanying Audited Financial Statements and the Auditor's Report Thereon*. The proposed standard broadens and clarifies the scope of documents to be addressed by the auditor, enhances the auditor's work effort, and introduces reporting requirements.

In March, the Institute provided the IAASB with a comment letter expressing

concerns with the proposed expansion of the auditor's responsibilities in respect of other information, embedded within the audit of financial statements, in order to meet the perceived expectations of users. The IAASB received more than 70 comment letters. At its meeting in June, the IAASB held initial discussions on key issues that had arisen from comment letter responses on the exposure draft. The IAASB will continue its deliberations at its meeting this month.

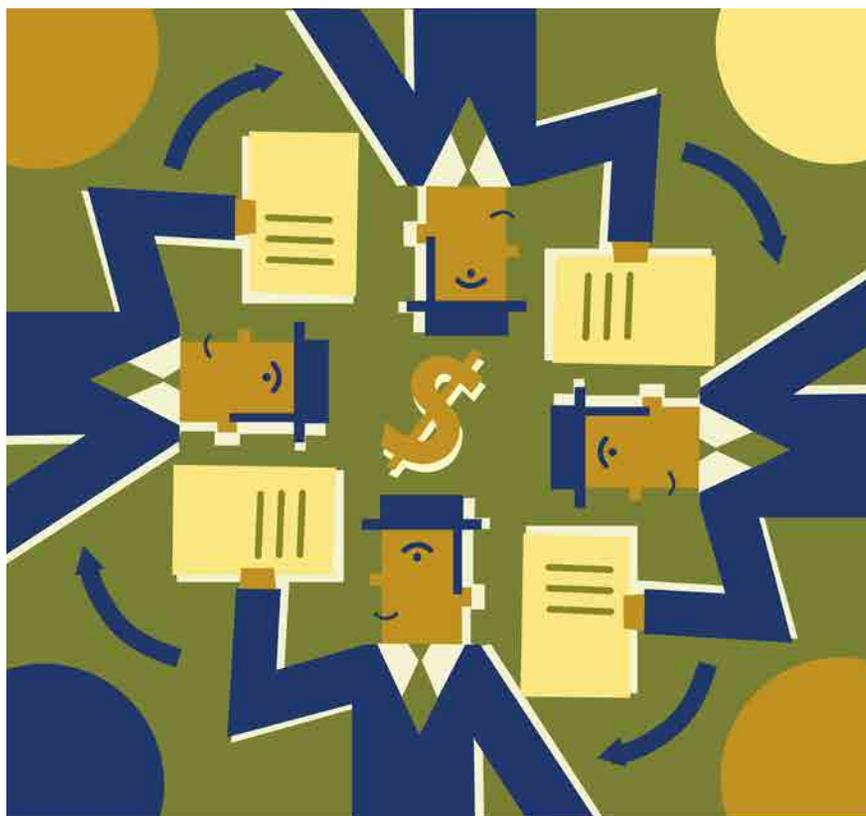
ISAE 3000

In April 2011, the IAASB issued an exposure draft of proposed revised ISAE 3000 (Revised) *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information* and proposed conforming amendments to the *International Framework for Assurance Engagements*, ISAE 3402 and proposed revised ISAE 3410. Proposed ISAE 3000 is a principles-based standard that is designed to be applied effectively to a broad range of assurance engagements.

Such engagements may range from as-

urance on statements about the effectiveness of internal controls, for example, to direct engagements such as performance, operational, or "value for money" audits, to possible future engagements addressing integrated reporting or corporate social responsibility reporting. It reflects those requirements that, in the IAASB's view, enable consistent high quality engagements while being sufficiently flexible to apply to the broad range of relevant engagements. In September 2011, the Institute provided the IAASB with a comment letter. The IAASB received more than 50 comment letters.

At its meeting in April, the IAASB discussed a proposed revised draft of ISAE 3000. Among other matters, the IAASB deliberated issues and options on the approach to be taken with respect to direct engagements. The IAASB noted that addressing both attestation and direct engagements in a single standard would result in a complex document, and that the approach being taken by the IAASB task force may not adequately serve the needs of those that would look to the standard when



Standard setting

performing direct engagements.

Taking into account the need to complete work on ISAE 3000 in the near future and the importance of achieving a high-quality standard, the IAASB agreed that the standard should focus on attestation engagements. Although there will be only limited references to direct engagements, practitioners may use the ISAE, adapted as appropriate, for such engagements. The IAASB also discussed different ways of wording the assurance conclusion for attestation engagements and the definition of limited assurance. The IAASB will consider a revised draft of the ISAE for approval at its meeting this month.

Disclosures

In January 2011, the IAASB issued a discussion paper, *The Evolving Nature of Financial Reporting: Disclosure and Its Audit Implications*. The discussion paper highlights recent trends in the range, volume and complexity of financial statement disclosures, and explores issues and practical challenges in preparing, auditing and using financial statements. It begins with a discussion of recent trends in financial reporting and the impact on financial statement disclosures. It then discusses how the International Standards on Auditing currently deal with disclosures.

The remainder of the discussion paper focuses on audit issues that the IAASB has identified regarding disclosures required by a financial reporting framework. The discussion paper addresses critical issues such as challenges in preparing disclosures, the nature and extent of evidence for different types of disclosures and the application of the concept of materiality to disclosures.

In June 2011, the Institute provided the IAASB with a comment letter recommending that the issues raised by the discussion paper should be addressed when developing accounting standards. The IAASB received more than 50 comment letters. In January 2012, the IAASB issued a feedback statement, which provides an overview of the key messages received on identified issues from the discussion paper

and provides thoughts and recommendations on what can be done to address them.

At its April meeting, the IAASB discussed certain issues and task force recommendations for enhancing the ISAs in relation to auditing financial statement disclosures. In particular, the IAASB provided input on where changes to the ISAs relating to the planning stage of the audit regarding auditing disclosures may be appropriate. The IAASB also discussed the existing assertions for presentation and disclosure, including considerations around their alignment with the qualitative characteristics of the underlying financial reporting frameworks.

The IAASB will further discuss issues and task force recommendations on this project at its meeting this month.

Audit quality

In January, the IAASB issued a consultation paper, *A Framework for Audit Quality*. Through the proposed framework, the IAASB aims to raise awareness of the key elements of audit quality, encourage stakeholders to explore ways to improve audit quality and facilitate greater dialogue between key stakeholders on the topic. The proposed framework describes the input and output factors that contribute to audit quality at the engagement, audit firm and national levels. It also demonstrates the importance of appropriate interactions among stakeholders and the relevance of various contextual factors.

In May, the Institute provided the IAASB with a comment letter seeking clarity on the purpose of the final framework and requesting the IAASB to be more forthcoming on the direction of the IAASB's pronouncements (e.g. ISAs and ISQC) in relation to the framework. It is important for national standard setters, auditors and other stakeholders, to have a broad understanding of the purpose of the framework and its interaction with IAASB pronouncements. The IAASB received more than 70 comment letters.

The Institute's comment letters are avail-

able along with the IAASB's consultation documents on the Institute's website: www.hkicpa.org.hk.

Other IAASB projects

In accordance with the IAASB strategy and work programme 2012-2014, published in June 2012, projects in the pipeline include:

- Exploring whether to develop guidance regarding third-party pricing sources for inclusion in ISA 540 or ISA 500 as appropriate, and considering whether there is a need for further enhancements to ISA 540 or the development of new implementation guidance in light of relevant developments (Third-party pricing sources/ISA 540).
- Determining actions to be taken regarding the topic of the relationship between external auditors and supervisors or regulators based on consultation with the Basel Committee and other stakeholders, and relevant financial reporting, regulatory and other developments (Guidance on auditor/banking supervisor relationship).
- Determining, in tandem with the anticipated completion of the revision of ISA 720, actions to be taken regarding auditor association with preliminary announcements based on research undertaken in consultation with regulators and other stakeholders (Preliminary announcements).
- Revising ISRS 4400 *Engagements to Perform Agreed-upon Procedures Regarding Financial Information*.
- Establishing a working group to identify and research issues and actively monitor relevant developments, in particular in the areas of integrated reporting, sustainability, corporate governance, internal control and XBRL, to inform longer term IAASB strategy and standard-setting activities.



This article is contributed by the Institute's standard setting department.