

20 November 2013

To:

Mr. Schilder  
Chair of the International Auditing and Assurance Standards Board

**Re.: Comment letter from European audit regulators relating to the IAASB's Exposure Draft suite "*Reporting on Audited Financial Statements*"**

Dear Mr. Schilder,

1. A number of independent European audit regulators and/or oversight bodies ("audit regulators") appreciate the opportunity to comment on the IAASB's ("Board") Exposure Draft "*Reporting on Audited Financial Statements*" issued in July 2013. The content of this letter has been discussed and agreed upon by the audit regulators of the following countries:

- Austrian Auditors Supervisory Authority – Austria
- Audit Public Oversight Council – Czech Republic
- Danish Business Authority – Denmark
- Auditors Activities Oversight Council – Estonia
- Haut Conseil du Commissariat aux Comptes – France
- Abschlussprüferaufsichtskommission – Germany
- Hellenic Accounting and Auditing Standards Oversight Board – Greece
- Irish Auditing & Accounting Supervisory Authority – Ireland
- Authority of Audit and Accounting – Lithuania
- Commission du Surveillance du Secteur Financier – Luxembourg
- Accountancy Board – Malta
- Netherlands Authority for the Financial Markets – The Netherlands
- Finanstilsynet – Norway
- Conselho Nacional de Supervisão de Auditoria – Portugal
- Romanian Public Interest Oversight Body of Accounting Profession – Romania
- Auditing Oversight Authority – UDVA – Slovakia
- Slovenian Agency for Public Oversight of Auditing – Slovenia
- Instituto de Contabilidad y Auditoria de Cuentas – Spain
- Eidgenössische Revisionsaufsichtsbehörde – Switzerland
- Revisorsnämnden – Sweden
- Financial Reporting Council – United Kingdom

2. Our comments in this letter reflect those matters on which we have achieved a consensus amongst the above-mentioned audit regulators. Nevertheless, they are not intended to include all comments that might be provided by these individual regulators and their respective jurisdictions.

**Introductory comments**

3. We support the direction taken by the IAASB with regards to the auditor's report in response to users' demands for the auditors to provide greater transparency about the audit of the financial statements.
4. From a regulator's perspective, it is important that auditing standards allow their users to understand them fully and comply effectively with them. Accordingly, clear principles which allow for consistency in their application and enforcement are a key issue for us.

5. We have set out in the following paragraphs our detailed comments regarding the manner in which the principles are formulated in the proposed standards.

## **Comments**

### *Key Audit Matters*

6. We believe that the "Key Audit Matters" (KAM) section could be an appropriate means of informing the users of the financial statements about the audit. It also provides a positive incentive for management to enhance the quality of information disclosed.
7. We welcome the fact that the content of the additional paragraphs on KAM is based on the audit, and that it presents those matters of most importance to the audit of the financial statements, rather than on the content of the financial statements, which are the responsibility of management.
8. However, while we feel that there should be room for judgment from the auditor about what to include in KAM, it should also be made clear in the standards, by creating appropriate and enforceable criteria and supportive guidance, that the auditor is supposed to comment on the aspects of the audit which are useful and relevant to the financial statement users. Accordingly, the standards should provide clearer and more prescriptive requirements on the content of KAM, by using amongst others more objective terminology, less likely to lead to inconsistencies when applied by different auditors.
9. We also would like the standard to provide more indicators to guide the auditor in the selection of items already identified during the audit,<sup>1</sup> by bringing forward into the body of the standard some matters to be specifically considered by the auditor in determining the KAM, currently included as illustrative examples in the application material.<sup>2</sup>
10. This may also have the advantage of promoting more consistency at an international level.
11. In addition, we believe that the standards should be clearer on whether or not ethical issues faced by the auditor that arose during the audit, such as independence threats or safeguards, should constitute a KAM or be included in an Other Matter paragraph if relevant.
12. We agree that the description of each KAM should include a reference to the part of the financial statements to which the matter relates, and why the auditors considered the matter to be a KAM. In addition, we suggest including a requirement to add a brief overview of the actions taken by the auditor to obtain evidence in response to the risks identified.<sup>3</sup>
13. Nevertheless, we find the IAASB's proposal to determine criteria for KAMs in a separate standard appropriate as this could serve to increase the clarity of the relevant requirements.
14. We also welcome the fact that the proposed standard makes provision for situations where a disclaimer or qualified audit opinion is issued.<sup>4</sup> These requirements clarify that the KAM paragraph cannot be used as a substitute for qualifying the audit opinion, or for management's lack of disclosures otherwise required in the financial statements.

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<sup>1</sup> Under ISA 260, ISA 315 etc.

<sup>2</sup> ED ISA 701 A15, A24, A31, A36 ...

<sup>3</sup> See ED ISA 701 A38 including the outcomes of the actions taken

<sup>4</sup> ED ISA 701.11, A10, A11, A25(b)

15. We think it is important to focus on the interaction between KAM, Emphasis of Matter Paragraphs and Other Matter Paragraphs,<sup>5</sup> especially when the opinion is qualified. We would suggest bringing some wording into the body of the standard to highlight the specificities or interactions between these notions.
16. Finally, the standard gives indications as to the fact that the KAM are related to the current period being audited.<sup>6</sup> We support this idea but we suggest re-emphasizing that a KAM, albeit originating in a previously audited period, may still be a key audit matter for the current period. Additional guidance in this regard would be helpful.

*Inclusion of an explicit statement on the auditor's independence and compliance with ethical requirements*

17. We support the inclusion of a statement on the independence of the auditor in the proposed auditor report including a reference to the applicable ethical requirements, encompassing the applicable laws and regulations and the sources of those requirements.<sup>7</sup>

*Scope of the requirements*

18. We recommend that the IAASB consider, in the future, extending the use of KAM<sup>8</sup> to companies and institutions that have a larger public impact, so-called "public interest entities", and to other entities in addition to listed entities. We believe that the reporting of KAM will have a positive influence on the quality of the audit and on the perceived value of the audit. We also recommend taking into account the outcomes of the European audit reform in this regard.
19. We support the inclusion of the name of the engagement partner in all audit reports and not only in those of listed entities.<sup>9</sup> Naming the engagement partner is already current practice in most of Europe. We favour this as it has a positive impact on the involvement and accountability of the engagement partner.

*Other information on materiality*

20. With regards to the need for the inclusion of information about risk assessment and the assessment of materiality in addition to KAM, we recommend that the IAASB further engages with the stakeholders and users of the financial statements, as well as reviewing the experience of jurisdictions that have recently put in place additional disclosures, in order to envisage, if appropriate, the inclusion of such additional information. We also recommend taking into account the outcomes of the European audit reform in this regard.

*Adaptability of requirements*

21. We support the inclusion of minimum requirements<sup>10</sup> where audits are conducted in accordance with the auditing standards of a jurisdiction and with the ISAs. This allows compliance with local laws and regulations with regards to specific content, layout or wording.

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<sup>5</sup> ED ISA 701 A26 and ED ISA 700 Examples 1 and 2

<sup>6</sup> ED ISA 701.2 and A8-A9

<sup>7</sup> ED ISA 700.28(c) and A29

<sup>8</sup> ED ISA 701.4 and ED ISA 700.30 already require this

<sup>9</sup> ED ISA 700 A45

<sup>10</sup> ED ISA 700.46-.48 and A57-A58

22. We believe it would be useful that a preferred order of the paragraphs be established in the audit report, in order to facilitate comparability at an international level. It is, however, important to allow for some flexibility if necessary in order to give more prominence to those matters of most importance to users.

#### *Going concern*

23. We are aware that the issue of the disclosure of information regarding going concern is one that is currently being addressed by both the auditing and accounting professions at a global level. We commend the Board for its efforts to liaise with the accounting standard-setters in this regard.
24. We generally welcome a specific statement in the audit report about the going concern assumption and on any identified material uncertainties in this regard.<sup>11</sup> This enhances the focus of the auditor on going concern issues, which would be a positive incentive, without changing his current responsibilities. We believe that a specific auditor's statement on a management assumption is in line with the role of the auditor.
25. We agree that the auditor can only report on the facts and the conditions that have been identified during the audit and cannot provide a guarantee on the outcome of future events. A statement on inherent limitations regarding future developments and events could be helpful to users in this regard. However, we are not in favour of the inclusion of the proposed statement that neither management nor the auditor can guarantee the entity's ability to continue as a going concern<sup>12</sup> which appears to be more in the nature of a caveat. We believe that the type of wording proposed could create some misunderstanding or doubts in the readers' minds on the ability of the entity to continue as a going concern, when no material uncertainties have, in fact, been identified.

#### *Description of responsibilities*

26. Although we support the need for a clear distinction between the responsibilities of the auditor and the entity, we do not see added value in the proposed descriptions of the various responsibilities in the auditor's report.<sup>13</sup> This is standardized information and is, as such, boiler plate in nature without adding specific information to the audit of the financial statements. Furthermore, the auditor is now given the opportunity to provide information specific to the audit in the content of the KAM which would likely be of more value than a standard description of the auditor's responsibilities.
27. We would like the standards to acknowledge that those descriptions can be tailored as appropriate in the applicable legal framework.

#### *Other information*

28. As specified in the examples of audit reports, we note the need for aligning the content of the requirements on reporting on "Other information"<sup>14</sup> with the prescriptions of the future standard on "Other information" (ISA 720).

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<sup>11</sup> ED ISA 570.20

<sup>12</sup> ED ISA 570.20(d)

<sup>13</sup> ED ISA 700 Management's responsibilities: .32-.34 and A32 – A35; Auditor's responsibilities: .35-.40 and A36 – A41

<sup>14</sup> ED ISA 700.49-.50

*European audit reform on the audit report*

29. The current version of the proposal does not yet include the changes in the European regulation on statutory audit, which are pending. We advise the IAASB to continue to allow for flexibility in its project in order to be in a position to consider those changes.

We thank you for the opportunity to comment on the consultation paper. If you have any questions or would like to further discuss the matters noted in this letter, please contact Marjolein Doblado, technical director of the Haut Conseil du Commissariat aux Comptes (+33 1 44 51 09 36).

Yours sincerely,

Audit regulator of:

- Austria
- Czech Republic
- Denmark
- Estonia
- France
- Germany
- Greece
- Ireland
- Lithuania
- Luxembourg
- Malta
- The Netherlands
- Norway
- Portugal
- Romania
- Slovakia
- Slovenia
- Spain
- Switzerland
- Sweden
- United Kingdom

## **Appendix: Comments on questions included in the exposure draft**

### **Key Audit Matters**

*Question 1 – Do users of the audited financial statements believe that the introduction of a new section in the auditor’s report describing the matters the auditor determines to be of most significance in the audit will enhance the usefulness of the auditor’s report? If not, why?*

Please refer more specifically to §6, 7.

*Question 2 – Do respondents believe the proposed requirements and related application material in the proposed ISA 701 provide an appropriate framework to guide the auditor’s judgment in determining the key audit matters? If not, why? Do respondents believe the application of proposed ISA 701 will result in reasonably consistent auditor judgments about what matters are determined to be the key audit matters? If not, why?*

Please refer more specifically to § 8 to 11 and 13.

*Question 3 – Do respondents believe the proposed requirements and related application material in proposed ISA 701 provide sufficient direction to enable the auditor to appropriately consider what should be included in the descriptions of individual key audit matters to be communicated in the auditor’s report? If not, why?*

Please refer more specifically to § 12.

*Question 4 – Which of the Illustrative Examples of key audit matters, or features of them, did respondents find most useful or informative, and why? Which examples, or features of them, were seen as less useful or lacking in informational value, and why? Respondents are invited to provide and additional feedback on the usefulness of the individual examples of key audit matters, including areas for improvement.*

*Question 5 – Do respondents agree with the approach the IAASB has taken in relation to key audit matters for entities for which the auditor is not required to provide such communication – that is, key audit matters may be communicated on a voluntary basis but, if so, proposed ISA 701 must be followed and the auditor must signal this intent in the audit engagement letter? If not, why? Are there other practical considerations that may affect the auditor’s ability to decide to communicate key audit matters when not otherwise required to do so that should be acknowledged by the IAASB in the proposed standards?*

Please refer more specifically to § 18, 20, 29.

*Question 6 – Do respondents believe it is appropriate for proposed ISA 701 to allow for the possibility that the auditor may determine that there are no key audit matters to communicate?*

- (a) If so, do respondents agree with the proposed requirements addressing such circumstances?*
- (b) If not, do respondents believe that auditors would be required to always communicate at least one key audit matter, or are there other actions that could be taken to ensure users of the financial statements are aware of the auditor’s responsibilities under proposed ISA 701 and the determination, in the auditor’s professional judgment, that there are no key audit matters to communicate?*

*Question 7 –Do respondents agree that, when comparative financial information is presented, the auditor’s communication of key audit matters should be limited to the audit of the most recent financial period in light of the practical challenges explained in paragraph 65? If not, how do respondents suggest these issues could be effectively addressed?*

Please refer more specifically to § 16.

*Question 8 –Do respondents agree with the IAASB’s decision to retain the concepts of Emphasis of Matter paragraphs and Other Matter paragraphs, even when the auditor is required to communicate key audit matters, and how such concepts have been differentiated in the Proposed ISAs? If not, why?*

Please refer more specifically to § 15.

### **Going Concern**

*Question 9 –Do respondents agree with the statements included in the illustrative auditor’s reports relating to:*

- (a) The appropriateness of management’s use of the going concern basis of accounting in the preparation of the entity’s financial statements?*
- (b) Whether the auditor has identified a material uncertainty that may cast significant doubt on the entity’s ability to [omission in the document: “continue as a going”] concern, including when such an uncertainty has been identified (see the Appendix of proposed ISA 570 (Revised))?*

*In this regard, the IAASB is particularly interested in views as to whether such reporting, and the potential implications thereof, will be misunderstood or misinterpreted by users of the financial statements.*

Please refer more specifically to § 23 to 25.

*Question 10 –What are respondents’ views as to whether an explicit statement that neither management nor the auditor can guarantee the entity’s ability to continue as a going concern should be required in the auditor’s report whether or not a material uncertainty has been identified.*

Please refer more specifically to § 25.

### **Compliance with Independence and Other Relevant Ethical Requirements**

*Question 11 –What are respondents’ views as to the benefit and practical implications of the proposed requirement to disclose the source(s) of independence and other relevant ethical requirements in the auditor’s report?*

Please refer more specifically to § 17, 29.

### **Disclosure of the Name of the Engagement Partner**

*Question 12 –What are respondents’ views as to the proposal to require disclosure of the name of the engagement partner for audits of financial statements of listed entities and include a “harm’s way exemption”? What difficulties, if any, may arise at the national level as a result of this requirement?*

Please refer more specifically to § 19.

## **Other Improvements to Proposed ISA 700 (Revised)**

*Question 13 –What are respondents’ views as to the appropriateness of the changes to ISA 700 described in paragraph 102 and how the proposed requirements have been articulated?*

Please refer more specifically to § 26, 27.

*Question 14 –What are respondents’ views on the proposal not to mandate the ordering of sections of the auditor’s report in any way, even when law, regulation or national auditing standards do not require a specific order? Do respondents believe the level of prescription within proposed ISA 700 (Revised) (both within the requirements in paragraphs 20-45 and the circumstances addressed in paragraphs 46-48 of the proposed ISA) reflects an appropriate balance between consistency in auditor reporting globally when reference is made to the ISAs in the auditor’s report, and the need for flexibility to accommodate national reporting circumstances?*

Please refer more specifically to § 21, 22, 29.