



cutting through complexity

Lebanese Association of Certified Public
Accounts (LACPA) 20th Congress

International Standard on Auditing
(ISA 701)

Communicating Key Audit Matters In
The Independent Auditor's Report

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Introduction

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Thank you for the opportunity to present our knowledge and experience of International Standards on Auditing through LACPA 20th Congress.

Our presentation will be related to International Standard on Auditing 701, Communicating Key Audit Matters In The Independent Auditor's Report (referred to as "ISA 701").

In this presentation we will address several significant aspects related to this standard including the following:

- Reasons for issuing ISA 701.
- Objectives, scope and effective date of the implementation of ISA 701.
- Entities and circumstances in which ISA 701 apply.
- ISA 701 overview.
- Key Audit Matters Not a Substitute for Expressing a Modified Opinion.
- Example auditor report based on ISA 701.
- Responses and opinions of public accounting firms and international committees on ISA 701.

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Reasons for issuing ISA 701

Reasons for issuing ISA 701

Issuance of ISA 701

The International Auditing and Assurance Standards Board (IAASB) commenced an initiative to commission a research to identify, provide information and insights on user perceptions regarding the financial statement audit and the auditor's report among different classes of financial statement users, the overall objectives of this initiative are to:

- (a) Appropriately enhance the communicative value and relevance of the auditor's report through proposed revisions to International Standards on Auditing (ISAs) requirements that address its structure and content; and
- (b) Determine whether and how the IAASB's reporting ISAs, in their design, can be modified to accommodate evolving national financial reporting regimes, while at the same time ensuring that common and essential content is being communicated.

This initiative emphasized because boards and committees in certain jurisdictions have identified the need to explore enhancements to auditor reporting as well as corporate reporting more broadly, such as:

- (a) The European Commission (**EC**) currently has efforts underway to reform audit policy arising from lessons from the global financial crisis including proposed regulation and directives that address in part the content of public auditors' reports as well as auditors' reports to audit committees

Reasons for issuing ISA 701

- (b) The U.S. Public Company Accounting Oversight Board (**PCAOB**) has several initiatives underway to explore changes to the auditor reporting model, including (a) its concept release on possible options for changes to the auditor's report to increase its communicative value; and (b) proposed rules relating to enhanced transparency in auditor's reports through disclosure of the name of the engagement partner and others participating in the audit.
- (c) The U.K. Financial Reporting Council (**FRC**) made recommendations to enhance reporting responsibilities for audit committees to the full Board of Directors, via an expanded report made public by inclusion in the entity's annual report. Auditors would then provide an expanded auditor's report to include (i) a new section that addresses the completeness and reasonableness of the audit committee's report; and (ii) identification of any matters in the annual report that the auditors believe are incorrect or inconsistent with the information contained in the financial statements or obtained in the course of their audit. The FRC completed an earlier initiative to facilitate more concise audit reports and revised U.K. audit reports to specifically refer to the auditor's responsibilities in relation to other information that accompanies the audited financial statements.

On June 2013 meeting, the IAASB unanimously approved a set of proposed new and revised ISAs for exposure and among these standards and revised standards was International Standard on Auditing ISA 701.

On September 2013 meeting, the IAASB approved a set of new and revised ISAs including the International Standard on Auditing ISA 701.

On January 2015 the IAASB has released its new and revised Intentional Standards on Auditing including the International Standard on Auditing ISA 701.

**Objectives, scope and effective
date of the implementation of ISA
701**

Objectives, scope and effective date of the implementation of ISA 701

Objectives

The objectives of ISA 701 are to determine key audit matters and, having formed an opinion on the financial statements, communicate those matters by describing them in the auditor's report.

Scope of ISA 701

The International Standard on Auditing (ISA 701) deals with the auditor's responsibility to communicate key audit matters in the auditor's report. It is intended to address both the auditor's judgment as to what to communicate in the auditor's report and the form and content of such communication.

The purpose of communicating key audit matters is to enhance the communicative value of the auditor's report by providing greater transparency about the audit that was performed. Communicating key audit matters provides additional information to intended users of the financial statements to assist them in understanding those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Communicating key audit matters may also assist intended users in understanding the entity and areas of significant management judgment in the audited financial statements.

The communication of key audit matters in the auditor's report may also provide intended users a basis to further engage with management and those charged with governance about certain matters relating to the entity, the audited financial statements, or the audit that was performed.

Objectives, scope and effective date of the implementation of ISA 701

Communicating key audit matters in the auditor's report is in the context of the auditor having formed an opinion on the financial statements as a whole. Communicating key audit matters in the auditor's report is not:

- (a) A substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation;
- (b) A substitute for the auditor expressing a modified opinion when required by the circumstances of a specific audit engagement in accordance with ISA 705 (Modifications To The Opinion In The Independent Auditor's Report);
- (c) A substitute for reporting in accordance with ISA 570 (Going Concern) when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern; or
- (d) A separate opinion on individual matters.

Effective date of the implementation of ISA 701

ISA 701 is effective for audits of financial statements for periods ending on or after December 15, 2016.

**Entities and circumstances in
which ISA 701 apply**

Entities and circumstances in which ISA 701 apply

Audits of listed entities

ISA 701 applies to audits of complete sets of general purpose financial statements of listed entities. It is intended to address both the auditor's judgment as to what to communicate in the auditor's report and the form and content of such communication.

Audits of entities other than listed entities

ISA 701 also applies when auditors of financial statements of entities other than listed entities communicate key audit matters in the auditor's report, when an auditor otherwise decides to communicate key audit matters in the auditor's report.

Audits conducted in accordance with basis other than International Standards on Auditing

ISA 701 is applicable for audits conducted in accordance with international auditing standards and not for audits conducted in accordance with PCAOB, AICPA or similar standards setters.

Local laws and regulations

ISA 701 also applies when the auditor is required by law or regulation to communicate key audit matters in the auditor's report.

ISA 701 overview

ISA 701 overview

Key Audit Matters (KAMs)

Key audit matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Key audit matters are selected from matters communicated with those charged with governance.

Those who charged with governance

Those charged with governance: The person(s) or organization(s) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.

Management

Management: The person(s) with executive responsibility for the conduct of the entity's operations. For some entities in some jurisdictions, management includes some or all of those charged with governance, for example, executive members of a governance board, or an owner-manager.

ISA 701 overview

Determining Key Audit Matters

The auditor shall determine which of the matters communicated with those charged with governance are the key audit matters. In making this determination, the auditor shall take into account areas of significant auditor attention in performing the audit, including:

- Areas of higher assessed risk of material misstatement, or significant risks identified

Areas Identified as a significant risks:

Significant risk – An identified and assessed risk of material misstatement that, in the auditor’s judgment, requires special audit consideration.

In exercising judgment as to which risks are significant risks, the auditor shall consider at least the following:

- (a) Whether the risk is a risk of fraud;
- (b) Whether the risk is related to recent significant economic, accounting or other developments and, therefore, requires specific attention;
- (c) The complexity of transactions;
- (d) Whether the risk involves significant transactions with related parties;
- (e) The degree of subjectivity in the measurement of financial information related to the risk, especially those measurements involving a wide range of measurement uncertainty; and
- (f) Whether the risk involves significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual.

ISA 701 overview

Assessed risk of material misstatement

The auditor's assessment of the risks of material misstatement at the assertion level may change during the course of the audit as additional audit evidence is obtained. Revision to the auditor's risk assessment and reevaluation of the planned audit procedures with respect to a particular area of the financial statements may result in an area being determined as one requiring significant auditor attention.

Fraud risk

It may not be the case for all significant risks to be determined as a key audit matter. For example, ISA 240 (The Auditor's Responsibilities Relating To Fraud In An Audit Of Financial Statements) presumes that there are risks of fraud in revenue recognition and requires the auditor to treat those assessed risks of material misstatement due to fraud as significant risks. In addition, ISA 240 indicates that, due to the unpredictable way in which management override of controls could occur, it is a risk of material misstatement due to fraud and thus a significant risk. Depending on their nature, these risks may not require significant auditor attention, and therefore would not be considered in the auditor's determination of key audit matters.

ISA 701 overview

- Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty.

ISA 260 requires the auditor to communicate with those charged with governance the auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures. In many cases, this relates to critical accounting estimates and related disclosures, which are likely to be areas of significant auditor attention, and also may be identified as significant risks.

However, users of the financial statements have highlighted their interest in accounting estimates that have been identified as having high estimation uncertainty in accordance with ISA 540 that may have not been determined to be significant risks. Among other things, such estimates are highly dependent on management judgment and are often the most complex areas of the financial statements, and may require the involvement of both a management's expert and an auditor's expert. Users have also highlighted that accounting policies that have a significant effect on the financial statements (and significant changes to those policies) are relevant to their understanding of the financial statements, especially in circumstances where an entity's practices are not consistent with others in its industry.

ISA 701 overview

- The effect on the audit of significant events or transactions that occurred during the period.

Events or transactions that had a significant effect on the financial statements or the audit may be areas of significant auditor attention and may be identified as significant risks. For example, the auditor may have had extensive discussions with management and those charged with governance at various stages throughout the audit about the effect on the financial statements of significant transactions with related parties or significant transactions that are outside the normal course of business for the entity or that otherwise appear to be unusual. Management may have made difficult or complex judgments in relation to recognition, measurement, presentation or disclosure of such transactions, which may have had a significant effect on the auditor's overall strategy.

Significant economic, accounting, regulatory, industry, or other developments that affected management's assumptions or judgments may also affect the auditor's overall approach to the audit and result in a matter requiring significant auditor attention.

Determining Key Audit matters (matters of the most significance)

The auditor shall determine which of the matters in accordance to the criteria above were of most significance in the audit of the financial statements of the current period and therefore are the key audit matters.

Matter of most significance:

Matters that required significant auditor attention also may have resulted in significant interaction with those charged with governance. The nature and extent of communication about such matters with those charged with governance often provides an indication of which matters are of most significance in the audit. For example, the auditor may have had more in-depth, frequent or robust interactions with those charged with governance on more difficult and complex matters, such as the application of significant accounting policies that were the subject of significant auditor or management judgment.

The concept of matters of most significance is applicable in the context of the entity and the audit that was performed. As such, the auditor's determination and communication of key audit matters is intended to identify matters specific to the audit and to involve making a judgment about their importance relative to other matters in the audit.

Other considerations that may be relevant to determining the relative significance of a matter communicated with those charged with governance and whether such a matter is a key audit matter include:

- (a) The importance of the matter to intended users' understanding of the financial statements as a whole, in particular, its materiality to the financial statements.
- (b) The nature of the underlying accounting policy relating to the matter or the complexity or subjectivity involved in management's selection of an appropriate policy compared to other entities within its industry.

ISA 701 overview

- (c) The nature and materiality, quantitatively or qualitatively, of corrected and accumulated uncorrected misstatements due to fraud or error related to the matter, if any.
- (d) The nature and extent of audit effort needed to address the matter.

Determining which, and how many, of those matters that required significant auditor attention were of most significance in the audit of the financial statements of the current period is a matter of professional judgment. The number of key audit matters to be included in the auditor's report may be affected by the size and complexity of the entity, the nature of its business and environment, and the facts and circumstances of the audit engagement. In general, the greater the number of matters initially determined to be key audit matters, the more the auditor may need to reconsider whether each of these matters meets the definition of a key audit matter. Lengthy lists of key audit matters may be contrary to the notion of such matters being those of most significance in the audit.

ISA 701 overview

The auditor's decision-making process in determining key audit matters is designed to select a smaller number of matters from the matters communicated with those charged with governance, based on the auditor's judgment about which matters were of most significance in the audit of the financial statements of the current period.

The auditor's determination of key audit matters 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 (i.e., even when the auditor's opinion refers to each period for which financial statements are presented).

Notwithstanding that the auditor's determination of key audit matters is for the audit of the financial statements of the current period and this ISA does not require the auditor to update key audit matters included in the prior period's auditor's report, it may nevertheless be useful for the auditor to consider whether a matter that was a key audit matter in the audit of the financial statements of the prior period continues to be a key audit matter in the audit of the financial statements of the current period.

ISA 701 overview

Communicating Key Audit Matters

The auditor shall communicate the key audit matters determined in a separate section of the auditor's report under the heading "Key Audit Matters." The auditor's report shall state that:

- (a) Key audit matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements [of the current period/year];
- (b) These matters were addressed in the context of the audit of the financial statements as a whole, and in forming the auditor's opinion thereon, and the auditor does not provide a separate opinion on these matters.

Presentation within the auditor's report

Separate Key Audit Matters Section in the Auditor's Report;

- (a) Placing the separate Key Audit Matters section in close proximity to the auditor's opinion may give prominence to such information and acknowledge the perceived value of engagement-specific information to intended users.
- (b) The order of presentation of individual matters within the Key Audit Matters section is a matter of professional judgment. For example, such information may be organized in order of relative importance, based on the auditor's judgment, or may correspond to the manner in which matters are disclosed in the financial statements.
- (c) When comparative financial information is presented, the introductory language of the Key Audit Matters section is tailored to draw attention to the fact that the key audit matters described relate to only the audit of the financial statements of the current period, and may include reference to the specific period covered by those financial statements (e.g., "for the year ended December 31, 20X1").

ISA 701 overview

- (d) The description of each key audit matter in the Key Audit Matters section of the auditor's report shall include a reference to the related disclosure(s), if any, in the financial statements and shall address:
- Why the matter was considered to be one of most significance in the audit and therefore determined to be a key audit matter; and
 - How the matter was addressed in the audit.

Circumstances in Which a Matter Determined to Be a Key Audit Matter Is Not Communicated in the Auditor's Report

The auditor shall describe each key audit matter in the auditor's report unless:

- (a) Law or regulation precludes public disclosure about the matter; or
- (b) In extremely rare circumstances, the auditor determines that the matter should not be communicated in the auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication. This shall not apply if the entity has publicly disclosed information about the matter.

ISA 701 overview

Communication with Those Charged with Governance

The auditor shall communicate with those charged with governance:

- (a) Those matters the auditor has determined to be the key audit matters; or
- (b) If applicable, depending on the facts and circumstances of the entity and the audit, the auditor's determination that there are no key audit matters to communicate in the auditor's report.

Circumstances in which the Auditor Has Determined There Are No Key Audit Matters:

When the auditor has determined there are no key audit matters to communicate in the auditor's report may provide an opportunity for the auditor to have further discussion with others who are familiar with the audit and the significant matters that may have arisen (including the engagement quality control reviewer). These discussions may cause the auditor to re-evaluate the auditor's determination that there are no key audit matters.

Documentation

The auditor shall include in the audit documentation:

- (a) The matters that required significant auditor attention, and the rationale for the auditor's determination as to whether or not each of these matters is a key audit matter;
- (b) Where applicable, the rationale for the auditor's determination that there are no key audit matters to communicate in the auditor's report; and
- (c) Where applicable, the rationale for the auditor's determination not to communicate in the auditor's report a matter determined to be a key audit matter.

**Key Audit Matters Not a Substitute
for Expressing a Modified Opinion**

Key Audit Matters Not a Substitute for Expressing a Modified Opinion

The Interaction between Key Audit Matters and Emphasis of Matter and/or other matter paragraphs to be Included in the Auditor's Report

ISA 706 establishes mechanisms for auditors of financial statements of all entities to include additional communication in the auditor's report through the use of Emphasis of Matter paragraphs and Other Matter paragraphs when the auditor considers it necessary to do so. In such cases, these paragraphs are presented separately from the Key Audit Matters section in the auditor's report. When a matter has been determined to be a key audit matter, the use of such paragraphs is not a substitute for the description of the individual key audit matter. ISA 706 provides further guidance on the relationship between key audit matters and Emphasis of Matter paragraphs in accordance with that ISA.

Key Audit Matters Not a Substitute for Expressing a Modified Opinion

Interaction between Key Audit Matters and qualified, adverse opinion and/or going concern issues to Be Included in the Auditor's Report

A matter giving rise to a qualified or adverse opinion or the existence of a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with proposed is by its nature a key audit matter. However, the auditor shall:

- (a) Report on these matter(s) in accordance with the applicable ISA(s);
- (c) Include a reference to the Basis for Qualified (or Adverse) Opinion or the Going Concern section(s) in the introductory language of the Key Audit Matters section.

When the auditor expresses a qualified or adverse opinion in accordance with ISA 705, presenting the description of a matter giving rise to a modified opinion in the Basis for Qualified (Adverse) Opinion section helps to promote intended users' understanding and to identify such circumstances when they occur. Separating the communication of this matter from other key audit matters described in the Key Audit Matters section therefore gives it the appropriate prominence in the auditor's report. The Appendix in ISA 705 includes illustrative examples of how the introductory language in the Key Audit Matters section is affected when the auditor expresses a qualified or adverse opinion and other key audit matters are communicated in the auditor's report.

Key Audit Matters Not a Substitute for Expressing a Modified Opinion

When the auditor expresses a qualified or adverse opinion, communicating other key audit matters would still be relevant to enhancing intended users' understanding of the audit, and therefore the requirements to determine key audit matters apply. However, as an adverse opinion is expressed in circumstances when the auditor has concluded that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements:

- Depending on the significance of the matter(s) giving rise to an adverse opinion, the auditor may determine that no other matters are key audit matters. In such circumstances.
- If one or more matters other than the matter(s) giving rise to an adverse opinion are determined to be key audit matters, it is particularly important that the descriptions of such other key audit matters do not imply that the financial statements as a whole are more credible in relation to those matters than would be appropriate in the circumstances, in view of the adverse opinion.

Key Audit Matters Not a Substitute for Expressing a Modified Opinion

Interaction between Key Audit Matters and disclaimer of opinion

ISA 705 prohibits the auditor from communicating key audit matters when the auditor disclaims an opinion on the financial statements, unless such reporting is required by law or regulation.

**Example auditor report based on
ISA 701**

Example auditor report based on ISA 701

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

To: The Shareholders ABC company.

Report on the Audit of the Financial Statements 201X

Opinion

We have audited the accompanying financial statements 201X of ABC (the company), based in (town/city).

In our opinion:

- The consolidated financial statements give a true and fair view of the financial position of ABC company on December 31, 201X and its financial performance and its cash flows for the year then ended 201X in accordance with International Financial Reporting Standards.

The consolidated financial statements comprise:

1. the consolidated statement of financial position as at December 31, 201X;
2. the following statements for 201X: consolidated statements of profit and loss and other comprehensive income, changes in equity and cash flows for the year then ended; and
3. notes comprising a summary of the significant accounting policies and other explanatory information.

Example auditor report based on ISA 701

Materiality

Misstatements can arise from fraud or error and will be considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements. The materiality affects the nature, timing and extent of our audit procedures and the evaluation of the effect of identified misstatements on our opinion.

Based on our professional judgment we determined the materiality for the financial statements as a whole at XX. The materiality is based on ... (% to be filled in for the relevant benchmark e.g. profit, turnover or other criteria). We have also taken into account misstatements and/or possible misstatements that in our opinion are material for the users of the financial statements for qualitative reasons. We agreed with the Board that misstatements in excess of XX, which are identified during the audit, would be reported to them, as well as smaller misstatements that in our view must be reported on qualitative grounds.

Example auditor report based on ISA 701

Scope of the Group Audit

ABC is at the head of a group of entities. The financial information of this group is included in the consolidated financial statements of ABC.

Because we are ultimately responsible for the opinion, we are also responsible for directing, supervising and performing the group audit. In this respect we have determined the nature and extent of the audit procedures to be carried out for group entities. Decisive were, the size and/or risk profile of the group entities or operations. On this basis, we selected group entities for which an audit had to be carried out on the complete set of financial statements or specific items.

By implementing the procedures mentioned above- at group entities, together with additional procedures at group level, we have been able to obtain sufficient and appropriate audit evidence about the group's financial information to provide an opinion about the consolidated financial statements.

Our Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements. We have communicated the key audit matters to the Board. The key audit matters are not a comprehensive reflection of all matters discussed.

These matters were addressed in the context of our audit on the financial statements as a whole and in forming our opinion thereon and we do not provide a separate opinion on these matters.

Descriptions for key audit matters contain the following elements:

- A description of the key audit matter;
- A summary of audit procedures performed;
- If relevant, key observations relating to key audit matters;
- If relevant, references to information or notes in the financial statements.

Example auditor report based on ISA 701

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards. Furthermore, management is responsible for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Our Responsibilities for the Audit of the Financial Statements

Our objective is to plan and perform the audit assignment in a manner that allows us to obtain sufficient and appropriate audit evidence for our opinion.

Our audit included:

- Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, designing and performing audit procedures responsive to those risks, and obtaining audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

Example auditor report based on ISA 701

- Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control.
- Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Concluding on the appropriateness of management's use of the going concern basis of accounting, and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause an the company to cease to continue as a going concern.
- Evaluating the overall presentation, structure and content of the financial statements, including the disclosures; and
- Evaluating whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We provide the Board with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Board, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, not communicating the matter is in the public interest.

Example auditor report based on ISA 701

Report on Other Legal and Regulatory Requirements

(as apply by local laws and regulations.)

Place, date

... (Name of Audit firm)

... (Name statutory auditor and signature)

**Responses and opinions of public
accounting firms and international
committees on ISA 701**

Responses and opinions of public accounting firms and international committees on ISA 701

The following section describes the opinion of public accounting firms and international committees on ISA 701, these responses glanced by IAASB through the exposure draft published on June 2013.

This exposure draft aimed to obtain the views from stakeholders in relation to the IAASB's proposals to enhance auditor reporting globally. The proposals respond to calls from investors, analysts, and other users of audited financial statements for the auditor to provide more relevant information in the auditor's report, and build upon the indicative direction.

This exposure draft included the proposed new ISA 701, Communicating Key Audit Matters in the Independent Auditor's Report, and a number of proposed revised and new ISAs.

KPMG

In agreement with IAASB

We are in agreement with the IAASB that there has been a clear message from users that the auditor's report needs to become more informative and transparent. We also believe that the proposals set out in the exposure draft are responsive to the feedback received from stakeholders by the IAASB on the Invitation to Comment: Improving the Auditor's Report. We are therefore supportive of the thrust of the current proposals in the exposure draft.

The proposals when implemented will represent a significant change to the information provided in today's auditor's report. We therefore believe that the proposed and revised standards, especially proposed ISA 701 Communicating Key Audit Matters in the Independent Auditor's Report, will be an important first step towards meeting the needs of users who want more insights from auditors than is provided under today's model.

Comments and other point of views

- (a) We are not supportive of including original information about an entity in the auditor's description of a key audit matter because it is the role of management and those charged with governance to provide information about the entity to users. However, we acknowledge that in rare cases it may be necessary when the description of a key audit matter would be incomplete without disclosing original information about the entity.

- (c) It is important that the description of a key audit matter in the auditor's report does not undermine the opinion on the financial statements as a whole. For this reason, we are not supportive of the illustrative examples in the exposure draft that include a conclusion in the description of a key audit matter.
- (d) We are supportive of having the auditor include a description of the auditor's response to each key audit matter in the report. Including this information in the report is consistent with the objective of providing more transparency into the audit.
- (e) We compared the criteria in proposed ISA 701 to those provided by the Public Company Accounting Oversight Board (PCAOB) in its proposal on critical audit matters. We note the two sets of proposals are similar, but not identical. This could lead to different matters being reported under each standard. We are concerned that users of financial statements for entities listed in the US and in other jurisdictions where ISAs apply may not understand why the same auditor is reporting different matters for the same set of financial statements. We recommend that the IAASB seek to work with the PCAOB to ensure that the criteria for identifying key or critical audit matters result in similar reporting of such matters under both standards, because we do not believe that differences in this area will be meaningful or helpful to users of the financial statements.

Ernst and Young

In agreement with IAASB

We strongly support the approach and direction the IAASB has taken in developing the proposed standard on reporting on audited financial statements and believe the changes will provide meaningful enhancements to, and increase the relevance of, the auditor's report. Based on the outreach of the IAASB to investor groups, we understand these changes should increase the usefulness of the auditor's report to such users through the insights into the key areas of the audit. Enhancing the auditor's report should contribute to the ongoing relevance of the financial statement audit and to serving the public interest.

The communication of Key Audit Matters (KAMs) in the auditor's report should contribute to enhancing its informational value to all users by highlighting matters that were of most significance to the audit of the financial statements. Communicating such matters may also assist users in understanding the areas of significant management judgment and draw users' attention to management's disclosures of those matters.

Comments and other point of views

- (a) We suggest adding application material that makes clear that the auditor is not expected to provide a follow up in the current year on the outcomes of any KAMs disclosed in the prior year.

Responses and opinions of public accounting firms and international committees on ISA 701

- (b) We believe that the auditor's report should disclose that an audit conducted in accordance with ISAs requires communication of KAMs only for listed entities. This will be even more important if some jurisdictions define a listed entity differently than the ISAs.
- (c) There are concerns raised regarding the practical test application of the standard, which suggest the need for the IAASB to provide additional implementation guidance to promote consistent application of the proposed standard once it is issued.
- (d) We welcome the inclusion of examples in the illustrative auditor's reports, because they help illustrate the application of the requirements of the standard. We expect that the examples, although purely illustrative in nature, are likely to be used extensively by auditors seeking to understand the level of detail to be included in a KAM.

PwC

In agreement with IAASB

We fully support the IAASB's initiative to expand auditor's reports to make them more informative by sharing insight from the audit. Such expanded reports would help to reaffirm the relevance and value of the audit to users. We can also see the benefits this will bring to the robust dialogue about significant matters we have with those charged with governance and management.

Making changes as fundamental as those being proposed will present some challenges. Our focus in developing our response to the proposals has been to explore those challenges and look to how the desired outcomes can be achieved practically. With the refinements we set out in this letter, we believe that the Board's proposed requirements and guidance will achieve the desired aims

Comments and other points of views

- (a) Refining and making clearer the framework that guides the judgments auditors will need to make in selecting the key audit matters that are reported.
- (b) Avoiding the reporting of matters that could inadvertently risk unintended market consequences, which would not be in the public interest.
- (d) Clarification on the treatment of matters discussed with the audit committee that have no relationship to the financial statements.

Deloitte and Touche

In agreement with IAASB

We support the Board's efforts to enhance the informational value, usefulness, and relevance of the auditor's report to a broad range of users, and acknowledges and appreciates the Board's leadership efforts to date. The more information of value auditors are able to provide to the users of audited financial statements, the greater the value and relevance audits will have to the user community, including the global capital markets. Additional transparency regarding the audit also stands to enhance

The proposed changes to the auditor's report clearly represent a significant expansion of information about a financial statement audit provided by auditors to the user community (especially users of audited financial statements for listed entities)

Comments and other point of views

- (a) The possibility that the KAM reporting requirements will likely be inconsistently applied in the early years as auditors gain experience.
- (b) The likely increased pressure on senior audit resources as well as on management during the concluding and reporting phase of the audit.

Basel Committee on Banking Supervision

In agreement with IAASB

The Committee supports the proposed changes to the auditor's report and the new and revised ISAs. The proposed changes would significantly improve auditor reporting, which should reduce the information and expectation gaps of auditors and users of audited financial statements. The Committee strongly believes that reporting on key audit matters (KAMs) informs users on how the auditor has applied professional judgment and reached an audit opinion, thus helping to strike the right balance between information provided by the auditor and that provided by management.

Comments and other point of views

- (a) The exposure draft mandates the use of the enhanced auditor's report for listed entities only. Given the critical role of banking organizations in maintaining financial stability and the nature of their business, we believe enhanced audit reporting could lead to consequential improvements in the quality of audits. Therefore, the Committee recommends that the IAASB require enhanced auditor's reports to be provided for all banking organizations (regardless of whether they are listed).
- (b) The Committee strongly supports a requirement for a prominent placement of the auditor's opinion in the auditor's report.

- (c) The required elements of the description of each KAM as set out the proposed ISA 701 are minimal and may not provide sufficient useful information to users. These requirements could be enhanced to call for more robust and entity-specific descriptions of KAMs.

IFAC Small and Medium Practices (SMP)

In agreement with IAASB

We believe that the current proposals continue to retain a substantial emphasis on the users of listed entities financial statements. We recognize the heightened attention to auditor reporting in the recent economic environment and consider that within the constraints of being unable to change the audit mandate, aspects of the IAASB's suggested improvements should enhance the perceived value of the audit report and strike a reasonable balance between global consistency and national flexibility.

In general, we believe that the new section on key audit matters is an appropriate response to the demand for auditors to provide more information to users of auditor's reports of companies listed on the capital markets.

Comments and other point of views

Our concern remains that the proposed expansion of auditor reporting, (with or without reporting of key audit matters,) may adversely impact the cost/benefit of SME audits and may also result in audit reports becoming excessively long.



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Thank You

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