

December 30, 2013

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### **Re: Auditor's Reporting Model**

CFA Institute,<sup>1</sup> in consultation with its Corporate Disclosure Policy Council (“CDPC”),<sup>2</sup> appreciates the opportunity to comment on the Public Company Accounting Oversight’s (PCAOB) and the International Auditing and Assurance Standards Board’s (IAASB) (collectively referred to as “Boards”) proposals to reform the auditor’s reporting model.

CFA Institute is comprised of more than 100,000 investment professional members, including portfolio managers, investment analysts, and advisors, worldwide. CFA Institute seeks to promote fair and transparent global capital markets and to advocate for investor protections. An integral part of our efforts toward meeting those goals is ensuring that the quality of corporate financial reporting and disclosures provided to investors and other end users is of high quality.

### **GENERAL COMMENTS**

The IAASB and the PCAOB have issued separate proposals to improve the Standard Auditor’s Report (SAR). CFA Institute is responding with a single letter to the Boards on these proposals since there are a number of overlapping issues and we believe that there should be a single globally relevant report to the extent possible. This would allow investors to compare audits of companies no matter in which region of the globe the auditor issues their report.

Our response is organized into discussions about what we see as the improvements needed to develop a single informative SAR. We observe that in many respects the individual proposals are similar but still contain some notable differences. For example, the PCAOB model does not contain provisions for going concern reporting and disclosure of engagement partner. The IAASB model anticipates future additional reporting for auditor responsibility and findings related to “other information”, which is currently being considered in another project. The PCAOB model currently presents proposals for “other information” in their model. Although these matters are being addressed in separate standard setting initiatives, we

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<sup>1</sup> With offices in Charlottesville, New York, Hong Kong, and London, CFA Institute is a global, not-for-profit professional association of more than 116,000 investment analysts, portfolio managers, investment advisors, and other investment professionals in 137 countries, of whom more than 108,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 138 member societies in 60 countries and territories.

<sup>2</sup> The objective of the CDPC is to foster the integrity of financial markets through its efforts to address issues affecting the quality of financial reporting and disclosure worldwide. The CDPC is comprised of investment professionals with extensive expertise and experience in the global capital markets, some of whom are also CFA Institute member volunteers. In this capacity, the CDPC provides the practitioners’ perspective in the promotion of high-quality financial reporting and disclosures that meet the needs of investors.

believe that because they relate most directly to and are most consistent with a coordinated global approach.

Our response addresses the following areas:

- Investor/User support for enhancing the Standard Auditor's Report
- Retention of pass/fail model
- Key audit matters (IAASB)/Critical audit matters (PCAOB)
- Conclusions regarding going concern
- Auditor's statement regarding "other information"
- Identification of engagement partner

Responses to selected questions from each of the proposals are presented in Appendices A and B.

### **Support for Enhancing the Standard Auditor's Report**

#### *CFA Institute Support for Changes to the Auditor's Reporting Model*

CFA Institute members have consistently supported efforts to enhance the quality, relevance and value of auditor reporting. As previously articulated in our letters to the IAASB and PCAOB we believe that improvements to the SAR are needed to advance a seriously outdated model for communication of important information to investors and other users regarding the auditor's professional examination of a company's financial statements. It is our belief that the SAR along with the financial statements and other narrative sections of an entity's financial report (i.e. management commentary, operating and financial review, etc.) should be considered part of a holistic communication of relevant information to investors to make informed capital allocation decisions. Significant efforts and investor-paid costs go into an audit, yet investors are provided very little information under the current SAR. Through increased transparency, a revised SAR will facilitate better analysis and heighten user confidence in the audited financial statements.

#### *CFA Institute Surveys Support Changes to the Auditor's Reporting Model*

CFA Institute has conducted multiple surveys<sup>3</sup> of our membership over several years on the importance of the SAR to investors and its information content. These surveys have consistently shown that the auditor's report is central to the analysis of financial statements, and should provide more information about the basis for the auditor's opinion.

The more significant survey findings regarding changes to the SAR are:

- Fifty-eight percent of respondents indicated that the auditor's report needs to provide more specific information about how the auditor reaches their opinion.
- Seventy-five percent of respondents believe that risk factors associated with measurement uncertainties in an entity's financial statements should be included in the independent auditor's report.
- A large majority of respondents indicated that more information regarding materiality, the auditor's independence, management's critical accounting judgments and estimates, and key areas of risk is important.

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<sup>3</sup> CFA Institute, Usefulness of the Independent Auditor's Report, March 2011  
[http://www.cfainstitute.org/Survey/usefulness\\_of\\_independent\\_auditors\\_report\\_survey\\_results\\_march\\_2011.pdf](http://www.cfainstitute.org/Survey/usefulness_of_independent_auditors_report_survey_results_march_2011.pdf)  
CFA Institute, Independent Auditor's Report Survey Results, March 2010  
[http://www.cfainstitute.org/Survey/independent\\_auditors\\_report\\_survey\\_results.pdf](http://www.cfainstitute.org/Survey/independent_auditors_report_survey_results.pdf)

These surveys consistently indicate that investors are not satisfied with the current “bare-bones” SAR and seek much more useful and qualitative information about the audit findings and process. Importantly, they also confirm that additional information from the professional auditor in the SAR is of much higher interest and value to an investor in addition to hearing more from the audit committee.

### **CFA Institute Support for Retention of the Pass/Fail Reporting Model**

The current SAR has been commonly described as a pass/fail model since the auditor expresses an opinion on whether the financial statements are fairly presented (pass) or not (fail). This aspect of the SAR is beneficial because it is brief, clear, consistent and comparable. It benefits those investors who want to quickly scan the SAR for departures from the unqualified report. However, it has limited utility for those who desire a more thorough and complete understanding of the audit findings and the audit process. For this reason, we believe that the pass/fail element of the model should be augmented with substantive informative enhancements, explained below. Given the continued significance and relevance of departures from the pass/fail opinion, we believe that this should continue to be presented near the beginning of the audit report.

### **Key Audit Matters (IAASB)/Critical Audit Matters (PCAOB)**

#### Requirement to Report Critical Audit Matters

Both of the Boards’ proposals indicate that determining the audit matters to be reported is based on the auditor’s professional judgment. The PCAOB model states that ordinarily these matters are of such importance that they are required to be (1) documented in the engagement completion document, (2) reviewed by the engagement quality reviewer, (3) communicated to the audit committee; or (4) any combination of the three. Specified audit guidance is provided for each of these items (i.e., AS No. 3 *Audit Documentation*, AS No. 7 *Engagement Quality Review* and AS No. 16 *Communications with Audit Committees*). The IAASB model specifies that the audit matters would be selected from 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. This is also subject to specified audit guidance (i.e., ISA 260 (Revised) *Communication with Those Charged with Governance*).

Our principal concern is that the language used in the proposals prescribes a more subjective approach—what the auditor determines “key” or “critical” to be—rather than a more objective approach. The proposed subjective approach might easily allow an artful avoidance of providing any additional information whatsoever to investors. We fear the Lake Wobegone syndrome, where all issuers suddenly become above average and unremarkable from an audit perspective. Investors have been seeking specific information from the auditor for years, and giving more objective, prescriptive guidance is necessary to ensure that those specific matters are conveyed by the auditor.

The [statements](#) of PCAOB Member Steven Harris noted similar concerns:

*Indeed, having the auditor concisely discuss a precise list of issues of interest to investors as suggested in the IAG survey and similar surveys by the CFA Institute, may well be preferable to a discussion of only issues that auditors, in their discretion, determine to be the most difficult, subjective or complex ones in an audit. Of course the two sets of issues may overlap, but they well may not. I believe we should be seriously considering a requirement that the auditors also report on “any matter that would otherwise be of greatest significance to a reasonable investor in understanding the import of the financial statements.*

*Sir David Tweedie, the former Chairman of the International Accounting Standards Board and national technical partner of KPMG, suggested that investors should learn through the report: (i) what kept the auditor awake at night, (ii) what arguments the auditor had with the CFO, (iii)*

*what the big estimates are, (iv) what the contentious accounting policies are, and (v) what the going concern assumptions are?*

While these comments were made in the context of the release of the PCAOB proposal, we believe the concerns expressed equally apply to the IAASB proposal. We encourage the Boards to develop clear guidance that would not allow for important matters to go unreported.

*Comments on Content of Key Audit Matters (IAASB) and Critical Audit Matters (PCAOB)*

In previous proposals, the Boards considered a form of reporting on the audit by means of auditor commentary (IAASB) or auditor's discussion and analysis (PCAOB). We supported this in our previous letters as an acceptable means of communicating additional information regarding the audit findings and the audit process provided it was subject to professional accountability for quality. Our principal concern is that the information should be reported by the auditor, not the audit committee or otherwise construed to be reported by management.

Although we prefer an auditor commentary which we expect would draw in specific matters of importance in non-boilerplate language, we are supportive of the communication of key audit matters (IAASB) or critical audit matters (PCAOB) (herein, both are considered "audit matters") as an acceptable alternative means of communicating information about the audit.

In our previous letters, we indicated that investors would benefit from the information often contained in what is commonly referred to as the "audit completion document" wherein the auditor identifies all significant findings or issues and incorporates this upon completion of the audit. Our request was to have the auditor report the most relevant of these same matters, whether we refer to them as key or critical, in plain, non-boilerplate language. With this approach there would not be an increase in audit scope or additional procedures, rather the auditor would simply report what was done in the audit, using information already contained in the audit completion memo. As a cost/benefit matter, enhancing the SAR in this way, should not result in a materially significant increase in the cost of audit services. We would support the Boards' specific review and assessment of this issue.

Also as earlier expressed, CFA Institute believes that the following elements in addition to others as outlined in our previous letter should be considered key or critical and routinely reported:

- Audit Risk - Provide a discussion of significant risks identified by the auditor and include factors the auditor evaluated in determining which risks are significant and how they were audited and assessed. This risk assessment should include not only specific financial statement risks, but also the auditor's overall client risk assessment factors. Also discuss why the auditor views these risks as significant. We recommend the Boards present an objective list of audit risks, as a first step towards a type of risk-rating of audits that would be comparable across auditors and countries.
- Auditor Independence - Provide a discussion of any matters that were reported and discussed with the audit committee concerning independence of the audit partner or firm -presumably limited to negative issues.
- Auditor Materiality - Provide details about the quantitative and qualitative materiality levels and factors the auditor considered in establishing materiality levels.
- Assessment of Management's Critical Accounting Judgments and Estimates - Provide a discussion of the critical accounting estimates that were discussed with management or the audit committee, the assumptions underlying the critical accounting estimates, and the auditor's assessment of and findings associated with the evaluation of these critical estimates. This could also include a discussion of movements and ranges around critical estimates.

- Accounting Policies and Practices - Provide a discussion of:
  - a. Discretionary changes in accounting principles or estimates affecting the consistency of reported amounts.
  - b. Qualitative aspects of the company’s accounting practices, financial statements and disclosures discussed with the audit committee or management.
  - c. Material matters that, while in technical compliance with the financial reporting framework, could have enhanced disclosures to improve investor understanding of the matters.
  - d. Significant unusual transactions in the current reporting period.
- Difficult or Contentious Issues, Including “Close Calls”- Discuss any difficult or contentious issues or “close calls” that arose during the audit and the final resolution of each issue.

*Comments on Instances Where There are No Critical/Key Audit Matters*

Both the IAASB and the PCAOB acknowledge that except in certain limited circumstances (expected to be rare), the auditor would not determine at least one audit matter to be reported. CFA Institute agrees that these conditions should be rare, however, each issuer should have at least one audit matter that would be deemed key or critical. Prescribing certain required communications as noted above may result in less transparent auditor reporting.

**Conclusions Regarding Going Concern**

CFA Institute agrees with the IAASB proposal that the auditor shall evaluate whether sufficient appropriate audit evidence has been obtained and conclude regarding the appropriateness of management’s use of the going concern basis of accounting in the preparation of the financial statements. We agree that conclusions and observations regarding going concern should be separately and clearly identified in the audit report. A CFA Institute survey of the membership in March 2012 indicated that 92% of respondents supported this separate mention of going concern matters in the SAR. When the going concern basis is inappropriate or whether there is a material uncertainty has been identified that the auditor’s report should qualitatively describe the uncertainties, conditions or events that have given rise to the doubt.

**Auditor’s Statement Regarding “Other Information”**

CFA Institute supports additional reporting in the SAR for other information that would require the auditor to determine whether other information contains (1) a material inconsistency, (2) a material misstatement of fact, or (3) both. We believe that the auditor’s determination should be limited to reading and considering other information and performing certain specific procedures based on relevant audit evidence obtained and conclusions reached during the audit. We understand that this is routine industry practice currently in the context of a standard integrated audit. We are not in favor of extending the auditor’s responsibilities to providing separate assurance. If the auditor determines that there are material inconsistencies or misstatements of fact that are unresolved prior to issuance of the financial statements, these differences should be clearly communicated within the body of the auditor’s report. We expect that there will be rare instances where differences will be unresolved.

We believe that clarifying the auditor’s responsibilities and findings related to other information further enhances to usefulness of the auditor’s report.

**Identification of Engagement Partner**

CFA Institute **is strongly in favor of mandating the disclosure of the engagement partner** (preferably by signature) in the auditor’s report for audits of all entities. We agree with the IAASB’s conclusion that disclosing the engagement partner’s name improves transparency for users and perhaps more importantly, instills a greater sense of responsibility and accountability which ultimately translates to improved audit quality. This disclosure is already required in many jurisdictions throughout the world and standardizing this requirement will lead to further accountability.

CFA Institute has previously articulated our support for disclosing the engagement partner in our letter to the PCAOB in response to their Concept Release to require disclosure of the engagement partner. We refer you to that letter for a complete response and CFA Institute's rationale.

We urge both the IAASB and the PCAOB to require disclosure of the engagement partner. It is our preference that this disclosure be prominently displayed in the auditor's opinion, rather than through a link to the entity's website or included in some other regulatory filing. Investors and other users should have easy access to the information. We also believe that attaching it to the opinion, further accountability would be established.

### **Improvements to the Auditor's Reporting Model Will Require a Cultural Shift**

In our previous letters to the Boards, we stressed that investor needs should be paramount when considering revisions to the auditor's reporting model. Requirements should be set with a view toward providing transparency and the most pertinent information possible for investors.

We believe that for meaningful changes to be effective, the reporting mindset of the audit committee, management, and independent auditors will need to undergo a cultural shift. The historical reporting relationship has tended to be viewed as the auditor reporting to the audit committee and to management, rather than as a communication to investors. Instead, the reporting considerations of the auditor should be directed to the user, since it is the users (i.e. investors) who foot the bill and approve the retention of the auditor, not management.

We appreciate the Boards' initiative in moving these proposals forward. They provide a vision and a workable path toward more useful and practical tools for finance professionals and investors around the globe. We acknowledge the transformational nature of these shifts and the inevitable industry resistance to change. Yet the markets and the world of finance have advanced so dramatically in terms of the complexity and speed of information in the past decade that all parts of the financial chain must improve and adapt. Auditing services should be no exception. We urge the Boards to be resolved in making these important improvements and stand ready to help as needed.

### **Closing Remarks**

We thank the Boards for the opportunity to express our views on the Standard Auditor's Report. If the Boards have questions or seek further elaboration of our views, please contact Matthew M. Waldron by phone at +1.212.705.1733, or by e-mail at [matthew.waldron@cfainstitute.org](mailto:matthew.waldron@cfainstitute.org).

Sincerely,

*/s/Kurt N. Schacht*

Kurt N. Schacht, JD, CFA  
Managing Director  
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*/s/ Ashwinpaul C. Sondhi*

Ashwinpaul C. Sondhi  
Chair  
Corporate Disclosure Policy Council

cc: CFA Institute Corporate Disclosure Policy Council

**Objectives**

1. *Do the objectives assist the auditor in understanding the requirements of what would be communicated in an auditor's unqualified report? Why or why not?*

We believe that objectives as stated should be sufficient to enable the auditor to understand the requirements for the audit report. However, we also believe that the objective should specifically identify that the investor is the main recipient of the report and that the report is intended to communicate entity-specific information. By highlighting an entity-specific approach boilerplate information will be reduced and/or eliminated.

**Basic Elements**

2. *The proposed auditor reporting standard would require the auditor's report to be addressed at least to (1) investors in the company, such as shareholders, and (2) the board of directors or equivalent body. Are there others to whom the auditor's report should be required to be addressed?*

We believe that the auditor's report should be appropriately addressed to both the shareholders and the company board of directors.

3. *The proposed auditor reporting standard retains the requirement for the auditor's report to contain a description of the nature of an audit, but revises that description to better align it with the requirements in the Board's risk assessment standards. Are there any additional auditor responsibilities that should be included to further describe the nature of an audit?*

We agree that any new standard on auditor reporting should retain the requirement for the report to contain a description of the audit. We agree with the PCAOB aligning this with the established risk assessment standards.

4. *The proposed auditor reporting standard would require the auditor to include a statement in the auditor's report relating to auditor independence. Would this statement provide useful information regarding the auditor's responsibilities to be independent? Why or why not?*

The proposal calls for the auditor to state that they are "required" to be independent with respect to the company in accordance with the United States federal securities laws and applicable rules and regulations of the PCAOB and SEC. We believe that a statement regarding independence is useful to investors and establishes a heightened sense of professional accountability.

However, we note that stating that the auditor is "required" to be independent, rather than is "in fact" independent is a less than optimal positive statement. We believe a more definitive statement is preferable and adds further assurance that the auditor is independent.

5. *The proposed auditor reporting standard would require the auditor to include in the auditor's report a statement containing the year the auditor began serving consecutively as the company's auditor.*

- a. *Would information regarding auditor tenure in the auditor's report be useful to investors and other financial statement users? Why or why not? What other benefits, disadvantages, or unintended consequences, if any, are associated with including such information in the auditor's report?*

We believe that auditor tenure is useful information to the investor, in that there could be instances where in the case of a newly appointed auditor, an investor may feel that the audit contains more risk. This may especially be the case where the new auditor may not have developed a complete understanding of the entity. Or in the case of a longstanding audit relationship, an investor may

question whether the auditor is as objective as possible. In other words, if the company has been a client for numerous years, the existing audit partner may not want to lose the client under his responsibility. This could render him less than objective when confronted with difficult or contentious issues.

- b. Are there any additional challenges the auditor might face in determining or reporting the year the auditor began serving consecutively as the company's auditor?***

No comment.

- c. Is information regarding auditor tenure more likely to be useful to investors and other financial statement users if included in the auditor's report in addition to EDGAR and other sources? Why or why not?***

We are in favor of including the tenure information in the auditor's report in addition to EDGAR. This makes it less difficult for investors to access the information.

- 6. The proposed auditor reporting standard would require the auditor to describe the auditor's responsibilities for other information and the results of the evaluation of other information. Would the proposed description make the auditor's report more informative and useful? Why or why not?***

We agree that the auditor's responsibilities for other information and the results of their evaluation should be clarified in the standard auditor's report. We emphasize that we are not in favor of expanding the auditor's responsibilities to provide assurance on the information, rather simply explain what they are presently required to do—and where there are material misstatements or inconsistencies, to explain them in appropriate detail. We believe that these instances will be rare since management is likely to correct the misstatements.

- 7. Should the Board require a specific order for the presentation of the basic elements required in the auditor's report? Why or why not?***

We do not think that the ordering of the presentation of the basic elements required by the auditor's report is critical, provided that there are clear headings are used to indicate each section. We encourage the PCAOB and the IAASB to work together to arrive at a standard for both form and content.

- 8. What other changes to the basic elements should the Board consider adding to the auditor's report to communicate the nature of an audit, the auditor's responsibilities, the results of the audit, or information about the auditor?***

No comment.

- 9. What are the potential costs or other considerations related to the proposed basic elements of the auditor's report? Are cost considerations the same for audits of all types of companies? If not, explain how they might differ.***

We are aware that some respondents may argue that the costs of implementing the proposed standards will result in an inordinate increase in costs. We agree with the following from the PCAOB proposal regarding costs:

*The Board would expect audit firms to incur minimal one-time costs that relate primarily to updating a firm's methodology regarding auditor reporting. These changes might not result in significant recurring costs because they involve standardized language that, once implemented, would be the same or very similar across different auditors' reports.*



We understand that initially the enhanced reporting could lead to an increase in costs as the auditor works through the language in the report with entity management and legal counsel. However, as noted in our previous letters, in accordance with the PCAOB Auditing Standard No. 3 paragraph 13, the auditor must identify all significant findings or issues in an engagement completion document. This document identifies and discusses the significant findings or issues and the basis for conclusions reached in connection with each engagement. We believe that the information in the completion memo should serve as the basis for identifying and reporting the information in the critical audit matters. Therefore, we are not suggesting any change in audit scope or additional procedures, rather that the auditor simply report what was done in conducting the audit, using information already largely contained in the audit completion memo. Increased costs in this regard ought to be minimal.

Finally with regard to costs, audit fees are paid for ultimately by the shareholders so to the extent that additional useful qualitative information can be supplied, investors would support reasonable additional fees.

### **Critical Audit Matters**

***10. Would the auditor's communication of critical audit matters be relevant and useful to investors and other financial statement users? If not, what other alternatives should the Board consider?***

As noted in our opening remarks, we preferred reporting on the audit by means of an auditor's discussion and analysis. We supported this in our previous letter as an acceptable means of communicating additional information regarding the audit findings and the audit process provided it was subject to professional accountability for quality. Our principal concern was that the information should be reported by the auditor in a way that it is not construed to be reported by management.

We are supportive of the communicating the critical audit matters as an acceptable alternative means of communicating additional information about the audit. We believe that these key/critical matters that the auditor determines to be 1) the most difficult, subjective or complex audit judgments; 2) posed the most difficulty in obtaining sufficient appropriate evidence; or 3) posed the most difficulty in forming the opinion on the financial statements has the potential to inform the users of the areas of high audit risk. Discussing the critical audit matters in an entity specific, non-boilerplate manner will focus attention on issues that are essential to understanding the audit.

We question how the auditor will apply the guidance with respect to discussing the "most difficult" matters. For example, we think that the test should be those audit areas that were the most "significant". We are concerned that given the deep expertise most audit firms have, that "difficulty" could be too subjectively determined. However, "significant" could be a more reasonable threshold to apply. To this point, we believe that the IAASB proposal for "significant" matters appears to strike the right balance.

We are also concerned that the critical audit matters must not become routine boilerplate language. Industry similarities could result in similar or identical audit challenges, so that these should be limited to few matters.

***11. What benefits or unintended consequences would be associated with the auditor's communication of critical audit matters?***

No comment.

***12. Is the definition of a critical audit matter sufficient for purposes of achieving the objectives of providing relevant and useful information to investors and other financial statement users in the auditor's report? Is the definition of a critical audit matter sufficiently clear for determining what***

*would be a critical audit matter? Is the use of the word "most" understood as it relates to the definition of critical audit matters?*

As mentioned above, we believe that using the word “difficult” could lead to a subjective application of the threshold. We believe that “significant” as defined by the IAASB would be a better determinant.

**13. *Could the additional time incurred regarding critical audit matters have an effect on the quality of the audit of the financial statements? What kind of an effect on quality of the audit can it have?***

We believe that there should not be any significant additional time incurred by the auditor to identify and/or report critical audit matters. These matters should be identified as part of the normal course of conducting a high quality audit. One would expect that in today’s environment that identifying these matters would not necessarily enhance audit quality given that they are a component of conducting the audit. However, by elevating these to specific reporting, overall quality should be enhanced.

**14. *Are the proposed requirements regarding the auditor's determination and communication of critical audit matters sufficiently clear in the proposed standard? Why or why not? If not, how should the proposed requirements be revised?***

Applying the requirements will require a significant amount of judgment. As mentioned we believe that there should be set requirements to report matters as noted in our General Comments. Users essentially want to hear directly from the auditor what is keeping them up at night written in an entity specific manner.

**15. *Would including the audit procedures performed, including resolution of the critical audit matter, in the communication of critical audit matters in the auditor's report be informative and useful? Why or why not?***

We are not in favor of the PCAOB prescribing that audit procedures be included as they relate to critical audit matters. The PCAOB should not necessarily exclude them; rather they should draft a standard which emphasizes that the auditor use their professional judgment on what should be included in the explanation of the critical audit matter. However, some brief explanation regarding how the critical audit matter was resolved could be beneficial to the users.

**16. *Are the factors helpful in assisting the auditor in determining which matters in the audit would be critical audit matters? Why or why not?***

No comment

**17. *Are there other factors that the Board should consider adding to assist the auditor in determining which matters in the audit would be critical audit matters? Why or why not?***

No comment.

**18. *Is the proposed requirement regarding the auditor's documentation of critical audit matters sufficiently clear?***

No comment.

**19. *Does the proposed documentation requirement for non-reported audit matters that would appear to meet the definition of a critical audit matter achieve the Board's intent of encouraging auditors to consider in a thoughtful and careful manner whether audit matters are critical audit matters? If not, what changes should the Board make to the proposed documentation requirement to achieve the Board's intent?***

No comment.

**20. Is the proposed documentation requirement sufficient or is a broader documentation requirement needed?**

No comment.

**21. What are the additional costs, including indirect costs, or other considerations related to the auditor's determination, communication, and documentation of critical audit matters that the Board should take into account? Are these costs or other considerations the same for all types of audits?**

We do not believe that would be material additional costs for communicating critical audit matters. These matters should have already been elevated through the audit firm to the appropriate level of responsibility including the engagement quality reviewer. Furthermore, these matters should have been also communicated to those charged with governance (i.e., Board of Directors, Audit Committee, etc.).

**22. What are the additional costs, including indirect costs, or other considerations for companies, including their audit committees, related to critical audit matters that the Board should take into account? Are these costs or other considerations the same for audits of both large and small companies?**

No comment.

**23. How will audit fees be affected by the requirement to determine, communicate, and document critical audit matters under the proposed auditor reporting standard?**

See previous comments.

**24. Are there specific circumstances in which the auditor should be required to communicate critical audit matters for each period presented, such as in an initial public offering or in a situation involving the issuance of an auditor's report on a prior period financial statement because the previously issued auditor's report could no longer be relied upon? If so, under what circumstances?**

We believe that there should be no differential reporting of critical audit matters in the cases of initial public offerings or for prior periods audited by other audit firms.

**25. Do the illustrative examples in the Exhibit to this Appendix provide useful and relevant information of critical audit matters and at an appropriate level of detail? Why or why not?**

We believe that including realistic examples in the proposed standard should enable auditors to better apply the specific requirements. It is essential that the PCAOB test how users view the example disclosures as part of their re-deliberations. The examples shown in the Exhibit to Appendix 5 of the Proposal on the surface appear reasonable and informative, but more extensive testing is essential with preparers, auditors and users.

**26. What challenges might be associated with the comparability of audit reports containing critical audit matters? Are these challenges the same for audits of all types of companies? If not, please explain how they might differ.**

No comment.

**27. What benefits or unintended consequences would be associated with requiring auditors to communicate critical audit matters that could result in disclosing information that otherwise would not have required disclosure under existing auditor and financial reporting standards, such as the examples in this Appendix, possible illegal acts, or resolved disagreements with management? Are there other examples of such matters? If there are unintended consequences, what changes could the Board make to overcome them?**

No comment.

28. *What effect, if any, would the auditor's communication of critical audit matters under the proposed auditor reporting standard have on an auditor's potential liability in private litigation? Would this communication lead to an unwarranted increase in private liability? Are there other aspects of the proposed auditor reporting standard that could affect an auditor's potential liability in private litigation? Are there steps the Board could or should take to mitigate the likelihood of increasing an auditor's potential liability in private litigation?*

No comment.

### **Explanatory Language**

29. *Is it appropriate for the Board to include the description of the circumstances that would require explanatory language (or an explanatory paragraph) with references to other PCAOB standards in the proposed auditor reporting standard?*

No comment.

30. *Is retaining the auditor's ability to emphasize a matter in the financial statements valuable? Why or why not?*

We believe that this option should be retained where matters should be highlighted that are not critical audit matters. Investors benefit from understanding an important matter deserving of emphasis and where it is disclosed in the financial statements.

31. *Should certain matters be required to be emphasized in the auditor's report rather than left to the auditor's discretion? If so, which matters? If not, why not?*

Since the PCAOB has deferred a decision on communications regarding going concern, we believe that material uncertainties regarding going concern should be communicated.

32. *Should additional examples of matters be added to the list of possible matters that might be emphasized in the auditor's report? If so, what matters and why?*

No comment.

### **Amendments to Other PCAOB Standards**

33. *Are the proposed amendments to PCAOB standards, as related to the proposed auditor reporting standard, appropriate? If not, why not? Are there additional amendments to PCAOB standards related to the proposed auditor reporting standard that the Board should consider?*

No comment.

34. *What are the potential costs or other considerations related to the proposed amendments? Are these cost considerations the same for all types of audits? If not, explain how they might differ.*

No comment.

### **Considerations Related to Audits of Specific Entities**

#### **Additional Discussion Related to the Proposed Other Information Standard**

CFA Institute supports additional reporting in the SAR for other information that would require the auditor to determine whether other information contains (1) a material inconsistency, (2) a material misstatement of fact, or (3) both. We believe that the auditor's determination should be limited to reading and considering other information and performing certain specific procedures based on relevant audit evidence obtained and conclusions reached during the audit. We are not in favor of extending the

auditor's responsibilities to providing separate assurance. If the auditor determines that there are material inconsistencies or misstatements of fact that are unresolved prior to issuance of the financial statements, these differences should be clearly communicated within the body of the auditor's report. We expect that there will be rare instances where differences will be unresolved.

We believe that clarifying the auditor's responsibilities and findings related to other information further enhances to usefulness of the auditor's report.

**Considerations Related to Audits of Brokers and Dealers**

No Comments

**Considerations Related to Effective Date**

No Comments

**Considerations Related to Securities Act Documents**

No Comments

**Emerging Growth Companies**

No Comments.

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 determined to be of most significance in the audit will enhance the usefulness of the auditor’s report? If not, why?*

As mentioned in our opening remarks that we prefer a more comprehensive auditor’s commentary to provide entity-specific information regarding the audit. However, we believe that the identification of key audit matters selected from matters communicated with those charged with governance should provide users with more information about the most significant matters confronted by the auditor. We believe that this discussion will assist users in understanding the areas of significant management judgment, uncertainties, risks, etc.

We do not believe that the standard should be overly prescriptive, but as mentioned in the opening remarks, we believe that certain matters should be discussed (e.g., audit risk, assessment of management’s critical accounting judgments and estimates, auditor materiality, modifications of planned audit approach, etc.)

Our principal concern is that the new standard is written in such a way so that the auditor would be required to disclose key audit matters.

2. *Do respondents believe the proposed requirements and related application material in 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?*

No comment.

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?*

No comment.

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 any additional feedback on the usefulness of the individual examples of key audit matters, including areas for improvement.*

We found that the examples of the key audit matters provided a reasonable explanation of the significant matters. We suggest that the IAASB field test the examples and solicit specific input from investors regarding the usefulness of the disclosure.

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?***

We believe that key audit matters should be required for all entities, however, if the matters are voluntarily disclosed, we believe that they should be subject to the requirements.

- 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?***

We believe that every audit should have at least one key audit matter to report. If an auditor determines that there are no key audit matters, this fact should be disclosed and the rationale. We also believe that these instances should be very rare.

***(a) If so, do respondents agree with the proposed requirements addressing such circumstances?***

We believe that by definition, each audit should have at least one key audit matter to communicate. However, should the IAASB determine that this will be permissible in very limited circumstances, then the auditor should expressly state that there were no such matters to report.

***(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?***

We believe by definition, there should always be at least one key audit matter to report.

- 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?***

Financial statement users are interested in comparability and as such, key audit matters should be discussed covering all periods presented. We believe updating the previous period key audit matters provide additional comfort to the user about the quality of the previous period presented.

- 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?***

We agree that the Emphasis of Matter paragraphs and Other Matter paragraphs should be retained to provide a mechanism to alert users to matters that would not otherwise be considered key audit matters. It is especially important that when these paragraphs are used, that they clearly clarify how they differentiate from the key audit matters. We agree that the most widespread use of this paragraph is normally associated with the material uncertainties associated with “going concern” assumptions which under the new proposal will be replaced by the going concern disclosure. However, we believe that Emphasis of Matter paragraphs are an appropriate means of highlighting where management discloses an important matter.

## Going Concern

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 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.*

CFA Institute is strongly in favor of expanded reporting by the auditor to include a specific section regarding going concern. In a survey conducted in March 2012, 81% of respondents said that the accounting concept of going concern is important in their analysis of a company. Also, 92% of respondents think that the independent auditor's report should identify the basis and reasons for their conclusion that the entity may not continue as a going concern. These disclosures are especially important in light of the global financial crisis.

Disclosures in the auditor's report should include the following elements:

- disclosures of risks that directly or indirectly affect the determination that there is a question as to whether the entity is a going concern.
- disclosures on the expected courses of action that bear on the financial flexibility of the entity, and a reasonably detailed discussion of the entity's ability to generate sufficient cash to support its operations during at least the 12 months from the date of the financial statements.

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?*

We are in favor of an explicit statement that neither management nor the auditor can guarantee the entity's ability to continue as a going concern. A statement such as this should narrow any expectations gap for users.

We recognize that the accounting standard setters have active projects addressing going concern and that the active timelines for resolving these issues are still unclear. However, we believe that the IAASB and the PCAOB should continue to move forward with additional auditor reporting in this area and consider any accounting standards outcomes in the final decision for the auditor's report.

## Compliance with Independence and Other Relevant Ethical Requirements

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



We agree that the auditor's report be changed to include a statement that the auditor is independent of the entity within the meaning of the relevant ethical requirements or applicable law or regulation and has fulfilled their ethical responsibilities under those requirements.

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

- 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?***

CFA Institute is strongly in favor of mandating the disclosure of the engagement partner (preferably in the form of signature) in the auditor's report for audits of all entities. We agree with the IAASB's conclusion that disclosing the engagement partner's name improves transparency for users and perhaps more importantly, instills a greater sense of responsibility and accountability which ultimately translates to improved audit quality. This disclosure is already required in many jurisdictions throughout the world, therefore standardizing this requirement leads to further accountability.

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

- 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?***

CFA Institute agrees with the other improvements to the auditor's report which include:

- Improved description of the responsibilities of the auditor and key features of the audit.
- Reference to whom the entity is responsible for overseeing the entity's financial reporting process.
- Other reporting responsibilities to allow additional flexibility for national standard setters to determine how best to place the auditor's communication about the enhanced reporting requirements (i.e., key audit matters, going concern, other information, etc.).

We also agree that the IAASB should not mandate the ordering of the elements of the auditor's report, however each area should be specifically identified with headings.

- 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?***

We agree that the ordering of the sections of the auditor's report should not be mandated. We understand that this flexibility is needed in order to comply with the many different jurisdictions subject to the auditor's reporting model. We do not think that the ordering of the presentation of the basic elements required by the auditor's report is critical, provided that they are all contained in the auditor's report and clear headings are used to indicate each section.

We encourage the PCAOB and the IAASB to work together to arrive at a standard for both form and content.