



## AUDITING STANDARDS BOARD (ASB)

### Meeting Highlights

January 11-14, 2021

### Videoconference

#### MEETING ATTENDANCE

##### ASB Members

Tracy Harding, *Chair*  
Brad Ames  
Monique Booker  
Patricia Bottomly (1/13-14)  
Sherry Chesser  
Harry Cohen  
Jeanne Dee  
Horace Emery  
Audrey Gramling  
Diane Hardesty  
Robert Harris  
Kathy Healy  
Jon Heath  
Clay Huffman  
Kristen Kociolek  
Sara Lord  
Maria Manasses  
Chris Rogers  
Tania Sergott

##### AICPA Staff

Linda Delahanty, *Senior Technical Manager—A&A Standards*  
Mike Glynn, *Senior Technical Manager—A&A Standards*  
Ahava Goldman, *Associate Director—A&A Standards*  
Hiram Hasty, *Associate Director—A&A Standards*  
Judith Sherinsky, *Senior Technical Manager—A&A Standards*  
Teighlor March, *Asst. General Counsel—General Counsel & Trial Board*  
Andy Mrakovcic, *Technical Manager— A&A Standards*

Note: The meeting was open to observers, whose names are not listed.

#### Chair and Chief Auditor Report

Mr. Harding provided an update on recent activities.

The highlights of the October and December 2020 ASB meetings were approved unanimously.

#### 1. NOCLAR

Mr. Cohen, chair of the NOCLAR Task Force (the Task Force) presented the proposed revisions to AU-C section 210, *Terms of Engagement*, to the ASB. Mr. Dustin, a NASBA staff member recently added to the Task Force, provided a summary to the ASB of NASBA's views with respect to requiring communication between predecessor and successor auditors regarding fraud and

NOCLAR.

Mr. Cohen noted that the Professional Ethics Executive Committee (PEEC) is also considering proposed revisions to the AICPA Code of Professional Conduct regarding NOCLAR. The ASB agreed that its exposure draft will be issued on the same date and have the same comment period end date as the PEEC ED as a convenience for potential commenters that are interested in both proposals. As the PEEC meeting at which it will be requested to vote to expose its ED is February 9, 2021, the proposed SAS is expected to be issued in late February and have a comment period end date of at least 90 days.

The following are the substantive revisions made to the draft standard or to the draft explanatory (wrap) material as directed by the ASB:

- Deleted the definition of *successor auditor* proposed to be included in paragraph .04 of AU-C section 210. Consistent with extant, the successor auditor would be referred to as simply *auditor*. Such approach is consistent with the International Standards on Auditing.
- Because the auditor is proposed to have differential courses of action based on whether management authorizes the predecessor auditor to respond to the auditor's inquiries, references to "respond fully" were changed to "respond" in paragraphs .11-.13 when such references apply to management's authorization.
- Added a statement that "such circumstances are expected to be rare" to proposed paragraphs .13 and .A34 to address concerns expressed by some members about misuse by the predecessor auditor of the ability to limit its response to the successor auditor's inquiries due to "unusual circumstances". The ASB also added to the explanatory/wrap document of the ED a statement that it is unaware of significant practice issues involving predecessor auditors inappropriately limiting their responses, and that it believes that the statement in the AICPA Code of Professional Conduct that members are expected to cooperate with each other helps protect against the potential of a predecessor auditor inappropriately limiting the response to the auditor's inquiries.

Mr. Heath stated he has significant concerns about the timing of the ASB proposal and believes that the PEEC ED should be exposed first and issued as final before the ASB considers any changes to the auditing standards. Further, Mr. Heath stated that confidentiality is just as much in the public interest as communication is.

The ASB discussed staff's plans to reach out to state boards of accountancy through NASBA and to state CPA societies to raise awareness of the existence of the exposure draft and request that they comment.

After discussion and consideration of a revised draft, Mr. Cohen affirmed that the Task Force does not believe that any further deliberation is necessary. After a motion to vote by Mr. Huffman seconded by Ms. Hardesty, 18 of the 19 members voted affirmatively to expose the proposed revisions for public comment. For the reasons described above, Mr. Heath dissented to the public exposure of the proposed revisions. Mr. Heath's detailed explanation of the reasons for his dissent will be included in the exposure draft.

## 2. Quality Standards

Sara Lord, chair of the QM1 Task Force, and Jon Heath, chair of the QM2/220 Task Force, led a discussion of proposed quality management standards: Proposed Statement on Quality Management Standard (SQMS) No. 1, *A Firm's System of Quality Management*, proposed SQMS No. 2, *Engagement Quality Reviews*, and proposed Statement on Auditing Standards (SAS), *Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards* (AU-C section 220).

The ASB directed that application material addressing the requirement for the engagement partner to review the auditor's report, including key audit matters, before dating the auditor's report be added to the proposed conforming amendments in various AU-C sections. There were only minor editorial revisions to the drafts of three proposed standards presented as agenda materials.

After affirmation from the Task Force chairs that they do not believe that any further deliberation is necessary, the ASB voted unanimously to expose the proposed standards for comments for at least 120 days.

## 3. Risk Assessment

Ms. Manasses, chair of the ASB Risk Assessment Task Force (Task Force) led a discussion with the ASB of issues arising from the comment letters on the Exposure Draft of proposed Statement on Auditing Standards (SAS), *Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and its Environment*.

While the ASB's discussion was focused on matters that require the ASB's strategic direction, the ASB also discussed the Task Force's preliminary views on certain matters raised by responders. Additional matters raised by responders are expected to be further deliberated by the Task Force.

Significant comments or observations by the ASB members related to the strategic direction of the proposed SAS were as follows:

**Length, Complexity, and Understandability of the Proposed Standard** – In response to concerns in comment letters about the length, complexity, and understandability of the proposed SAS, the Task Force suggested the following options to amend the application material:

1. move certain content to a new appendix within the proposed standard, or
2. relocate content to the AICPA's Audit Guide, *Assessing and Responding to Risks of Material Misstatements* (Audit Guide).

ASB members generally expressed the following broad views:

1. The ASB's overall strategy is to use International Standards on Auditing (ISAs) as the base (as discussed in the following bullet on convergence), and relocation might imply difference with the ISAs.

2. Relocating content might cause more confusion by making it more difficult to find in various sources of literature, and it might be difficult to develop “criteria” about which content to relocate.

The ASB instructed the Task Force not to relocate content from the application guidance but to consider additional refinements, clarifications, or examples that would enhance the understandability of the proposed SAS, including consideration of whether guidance exists in the Audit Guide that is responsive to comments received and that could be incorporated in the application material of the proposed standard, without significantly impacting the length of the standard.

- **Convergence** – The ASB reiterated the strategy to converge with ISAs. Accordingly, the Task Force was directed to primarily consider clarifications in the application material and only those changes to the requirements that would be necessary in our jurisdiction, considering the comments received.
- **Scalability** – ASB members expressed the view that the proposed SAS is scalable and could be applied to all entities, including governmental entities. The ASB discussed how length and complexity might impact an auditor’s understanding of how to scale the proposed SAS. The ASB directed the Task Force to consider whether to include additional application material that
  - provides better linkages to the auditor’s responses to the assessment of the risks of material misstatement
  - further explains the “why” of the requirements.

The ASB also discussed the issuance of implementation guidance, such as specific examples in the Audit Guide as well as visualizations of the requirements.

- **Understanding internal control, including evaluating design and determining implementation** – Various views were expressed with respect to the “work effort” necessary to understand the control environment, the entity’s risk assessment process, and the entity’s monitoring of controls, while evaluating design and determining implementation of certain control activities. It was noted that the extant standard is being applied differently in practice with respect to design and implementation. Individual members of the ASB commented about
  - the importance of the control environment, in particular, and the need to evaluate controls therein from a design and implementation perspective.
  - a potential variance of the requirements with those of the PCAOB.
  - bifurcating the requirement to evaluate the design and to determine whether the controls have been implemented into two separate requirements.

After discussion, the ASB instructed the Task Force to consider further refinements to better articulate the requirements, considering the “convergence” strategy. This includes clarifying the requirement to “evaluate” certain matters with respect to each of the components of internal control.

The ASB was supportive of the Task Force's preliminary views regarding:

- Considering whether additional changes are necessary to further align with PCAOB standards; certain guidance in PCAOB standards may address comments from responders
- Revisiting whether additional coordination with AU-C section 940 is necessary; however, the ASB continued to support not including specific AU-C section 940 concepts within the proposed SAS, which is consistent with prior Board decisions. It was noted that the understanding of the components of internal control as part of an audit of internal control over financial reporting differs from that in a financial statement only audit
- Retaining separate inherent and control risk assessments; however, additional guidance may be provided, particularly with respect to how the auditor's understanding of the design and implementation of controls may influence the auditor's response to identified and assessed risks
- Retaining the notion of the spectrum of inherent risk; however, additional guidance may be provided with respect to the concepts of "reasonable possibility" as well as "significant risks"
- Clarifying the requirements related to understanding controls related to journal entries
- Considering adding guidance to better explain the use of walkthroughs
- Retaining the notion of significant risks; however, additional guidance may be provided to address comments from responders
- Retaining the proposed stand back requirement in paragraph 36 of the proposed SAS; however, additional guidance may be provided to further explain "why" the auditor performs a stand back, the relationship between material and significant, and whether or how the stand back is documented
- Clarifying the documentation requirements; responders provided several observations and suggestions related to the alignment of the documentation requirements with the requirements for understanding the entity and its environment, including internal control
- Retaining revised paragraph 18 of AU-C Section 330, as proposed

The Task Force will continue to evaluate the comment letters received and will present a revised draft of the proposed SAS at the next ASB meeting. In particular, the Task Force will consider comments related to general IT controls and automated tools and techniques, as well as paragraph-specific comments.

The ASB also discussed further outreach to responders and service providers as well as the development of implementation guidance.

#### **4. ASEC liaison meeting**

The ASB met with the Assurance Services Executive Committee and discussed items of mutual interest.

## 5. TIC liaison meeting

The ASB met with the PCPS Technical Issues Committee and discussed items of mutual interest.

## 6. Attestation Standards (Direct Reviews)

Ms. Dee, chair of the Attestation Standards Task Force, led a discussion of concepts associated with proposed revisions to the attestation standards to

- provide for direct review engagements
- eliminate the prohibition on reviews of (a) prospective financial information; (b) internal control; and (c) compliance with requirements of specified laws, regulations, rules, contracts, or grants.

Mr. Glynn reminded the Board that the October 2018 exposure draft, *Proposed Revisions to Statement on Attestation Engagements No. 18* proposed revisions to AT-C section 210 that would allow for direct reviews. The Board had made the decision to issue separate final standards for the proposed revisions to AT-C section 215 (SSAE No. 19, *Agreed-Upon Procedures Engagements*), to permit direct examinations (SSAE No. 21, *Direct Examination Engagements*), and for the revisions to AT-C section 210 excepting the direct review proposal (SSAE No. 22, *Review Engagements*). The only proposed revisions included in the October 2018 exposure draft that have not been issued as a final standard are with respect to permitting direct reviews.

Significant comments or observations by various ASB members about developing a standard for direct review engagements were as follows:

- Concern about whether the Board has ample bandwidth for this project, given the other significant projects that it is working on. Mr. Harding reminded the Board that it shares the authority to issue SSAEs with the Accounting and Review Services Committee (ARSC). Mr. Harding stated that he had spoken to the Chair of the ARSC and ARSC would be willing to take up the project if the ASB determines that it does not have the bandwidth.
- Concern that users will be confused by a service that would require procedures like those performed in an examination engagement but less extensive than those procedures.
- A suggestion to wait to see if there are any issues with direct examinations engagements before allowing additional direct engagements
- An expression of increased interest in the concept of a direct review now that a standard has been issued permitting direct examination engagements and the belief that because attestation reviews are performed with respect to Environmental, Social, and Corporate Governance (ESG) issues, there may be a significant market for direct reviews. However, another member stated that he does not currently see such a market for direct reviews.
- A reminder that direct reviews are permitted in the international standards and a suggestion that it would be better to develop a standard than wait and be reactionary.

The ASB agreed to the following actions:

- Continue to consider whether to permit direct review engagements.
- Perform outreach about obtaining limited assurance on subject matter and issues involving performing the initial measurement or evaluation of underlying subject matter to practitioners who have performed
  - reviews in accordance with AR-C section 90, *Reviews of Financial Statements*.
  - direct examinations in accordance with recently issued SSAE No. 21, *Direct Examination Engagements*.
  - direct review engagements in accordance with international attestation standards.
- Retain the prohibition on reviews of the specific subject matters listed above but continue to consider the issue.
- Perform a post-implementation review of SSAE No. 21, after sufficient time for practitioners to implement SSAE 21 to allow for more useful feedback, and consider whether revisions might be needed, including consideration of concerns with respect to the provision in SSAE No. 21 that prohibits a direct examination of subject matter covered by AT-C section 315, *Compliance Attestation*.

## 7. Group Audits

Dora Burzenski, Chair of the ASB's Group Audits Task Force (ASB Task Force) and member of the IAASB's ISA 600 Task Force (ISA 600 Task Force), provided an update on the IAASB's December 2020 discussion of comments on the April 2020 exposure draft, Proposed International Standard on Auditing (ISA) 600 (Revised), *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)* (ED). The objective of the IAASB's December 2020 discussion was to obtain the IAASB's input on the initial views and recommendations of the ISA 600 Task Force related to respondents' comments on the scope and applicability of the proposed standard, the definition of component, the definition of engagement team, and the risk-based approach, including the involvement of component auditors. The ASB Task Force is monitoring the changes being made to ISA 600 in anticipation of converging extant AU-C section 600 with ISA 600 (Revised).

The following is a high-level summary of the comments on the ED and responses to those comments from the ISA 600 Task Force:

- **Consolidation Process**  
In response to concerns about references in the ED to the term *consolidation process* being confusing because that term as used in the ED has a broader meaning than the term *consolidation* as defined in applicable financial reporting frameworks, the ISA 600 Task Force recommended that a cross-reference to paragraph 11 be included in the definition

of *group financial statements* so that the definition is linked more closely with detail about what constitutes a consolidation process.

- Paragraph 11 of the ED states that the consolidation process includes the aggregation of the financial information of branches or divisions. Paragraph A17 of the ED indicates that a centralized process for branch or divisional accounting in which there is no separately prepared financial information requiring aggregation may cause the aggregated information to be excluded from the “consolidation process.” Some respondents found paragraph A17 confusing in light of paragraph 11 and were concerned that this may result in inconsistency in the application of the ED. The ISA 600 Task Force is considering clarifying paragraph A17 by (1) indicating that if a single entity is aggregated by branches or divisions, ISA 600 is applicable or (2) providing factors to consider in determining whether the branches or divisions comprise a group. The ISA 600 Task Force is continuing to consider this item to determine a way forward.

### **Definition of Component**

- The definition of *component* in paragraph 9 of the ED accommodates the various ways in which the group engagement team might view the group structure in designing the overall group audit strategy and plan (auditor’s view). Some respondents believe that focusing on the auditor’s view will cause the group engagement team to disregard management’s view of the group structure. The ISA 600 Task Force indicates that this was not the intent of the ED, which predicates the group audit on an understanding of the group and its environment, including the group’s financial reporting processes, as required by ISA 315. The ISA 600 Task Force is considering the need to reemphasize several points in the revised standard including that the flexibility in the group engagement team’s approach is based on the understanding required by ISA 315 and that in practice, many group engagement teams consider the group structure as a starting point.

### **Risk Based Approach Including the Involvement of Component Auditors**

- Paragraph 31 of the ED requires the group engagement team to take responsibility for the identification and assessment of the risks of material misstatement of the group financial statements. Some respondents noted that the strong focus on the group engagement team’s responsibility may undermine the role of the component auditor and result in the group engagement team overlooking significant risks at the component level. Other respondents noted that it may be challenging for auditors to consistently apply the risk-based approach because there is no guidance for the minimum work effort required to be performed on components. The ISA 600 Task Force noted that there may be a need for a framework to help the group engagement team apply the risk-based approach.

### **Removal of the Concept of Significant Components**

- Because the IAASB believes that identifying and assessing the related risks of material misstatement of the group financial statements (compared to a focus on significant components) more closely aligns with ISA 315, the ED eliminates the requirement for the group engagement team to obtain an understanding of the group sufficient to identify significant components. Most respondents were supportive of this approach; however,

some respondents noted that in certain group audits, a risk-based approach may not be the best approach. They indicate that when there is no requirement to perform an audit of the financial information of the component, and component auditors are not involved, the group engagement team may (1) inappropriately identify and assess risks of material misstatement or fail to obtain information from the audit of significant components that would help the group engagement team identify and assess the risks of material misstatement. In defense of the approach, it was noted that nothing precludes the group engagement team from performing a full scope audit of a component.

### **Revised Definition of Engagement Team**

- The definition of *group engagement team* in the ED does not include component auditors while the definition of *engagement team* in ISA 220 does include component auditors. Respondents noted that the new definition of engagement team could lead to practical challenges, for example related to compliance with independence and ethical requirements; direction, supervision, and review of component auditors; and the competence and capabilities of component auditors. These are particularly challenging when component auditors are from a non-network firm or from a different country. To address some of the concerns, the ISA 600 Task Force is considering, among other things, changing the term *group engagement team* to *group auditor* so that the engagement team would be defined as comprising the group auditor and component auditors and liaising with the IESBA to discuss challenges related to compliance with independence and ethical requirements

The ISA 600 Task Force will present issues related to this project at the March 2021 IAASB meeting.

## **8. Fraud/Going Concern**

Dr. Gramling led a discussion of a draft comment letter responding to the IAASB Discussion Paper, *Fraud and Going Concern in an Audit of Financial Statements: Exploring the Differences Between Public Perceptions About the Role of the Auditor and the Auditor's Responsibilities in a Financial Statement Audit*. The discussion included a summary of the feedback received through a public survey conducted by the AICPA about the questions in the IAASB Discussion Paper from a U.S. GAAS perspective.