

AUDITING STANDARDS BOARD (ASB)

Meeting Summary

August 1-4, 2016

Milwaukee, WI

MEETING ATTENDANCE

ASB Members

Mike Santay, *Chair*

Gerry Boaz

Dora Burzenski

Liz Gantnier

Dan Hevia

Gaylen Hansen

Sandra Johnigan

Ilene Kassman

Ryan Kaye

Dan Montgomery

Steven Morrison

Marc Panucci

Josh Partlow

Rick Reisig

Catherine Schweigel

Chad Singletary

Absent

Rich Miller

Jere Shawver

Steve Glover

AICPA Staff

Amanda Black, *Content Development*

Mimi Blanco-Best, *BRAAS (8/3 only)*

Mike Glynn, *Audit & Attest Standards*

Ahava Goldman, *Audit & Attest Standards*

Hiram Hasty, *Audit & Attest Standards*

Chuck Landes, *Professional Standards*

Teighlor March, *Assistant General Counsel*

Andy Mrakovcic, *Audit & Attest Standards*

Judith Sherinsky, *Audit & Attest Standards*

Lisa Snyder, *Professional Ethics (8/4 only, by phone)*

Linda Volkert, *PCPS Technical Issues Committee*

Observers and Guests

Denny Ard, *Dixon Hughes*

Michael Auerbach, *U.S. Department of Labor (8/2-3 only)*

Sally Ann Bailey, *Deloitte & Touche LLP*

Brian Collins,

Jim Dalkin, *GAO*

David Ford, *EY*

Bridget Gyofri, *KPMG LLP*

Chris Halterman, *EY (8/3 only)*

Susan Jones, *KPMG LLP*

Ken Kumor, *AON*

Sara Lord, *RSM*

Nigyar Mamedova, *NASBA*

Tammy Mooney, *Thomson Reuters*

Laura Schuetze, *Grant Thornton*

Darrel Schubert, *Ernst & Young LLP (8/2 only)*

Chair's and Director's Report

Mr. Santay informed the ASB that Marcia Marien has resigned from the ASB due to health issues. We wish her a full and speedy recovery. Gaylen Hansen has been appointed to fill the remainder of Marcia's term and Mr. Santay welcomed him to the ASB.

Mr. Santay reported on current activities, including the recent issuance of exposure drafts for proposed Statements on Auditing Standards *The Auditor’s Consideration of Entity’s Ability to Continue as a Going Concern* and *Auditor Involvement With Exempt Offering Documents*. Mr. Santay discussed with the ASB an issue related to SAS No. 131 about when the auditor performs an audit in accordance with both GAAS and the standards of the PCAOB. The question is whether it is permitted to issue two separate reports, one that refers to GAAS and one that refers to PCAOB standards. Some ASB members think that in some circumstances, such as non-issuers filings with the SEC that are required to use the PCAOB report, separate reports are less confusing for users. While some firms believe that two separate reports are allowed under GAAS, the majority of ASB members do not. The ASB will prepare an interpretation clarifying that when an audit is conducted in accordance with two sets of auditing standards, any report that is issued is required to refer to both sets of standards.

Mr. Landes informed the ASB that errors in Professional Standards sometimes come to staff’s attention. These errors are corrected in what is referred to as a “silent change”; the changes are shown in a monthly report to licensees and are described as editorial changes but are not flagged in brackets in the standards as conforming amendments are. One such recent change to the requirement in SSAE No. 18 to document when a presumptively mandatory requirement is not followed. The requirement was changed from *should* to *must* to be consistent with the comparable requirement in the SASs and SSARs. Mr. Santay requested that the ASB Chair be informed of future silent changes in advance of the change.

1. Direct Engagements

Ms. Schweigel led the ASB through the discussion paper on direct engagements. The Direct Engagements Task Force has been charged with developing an attestation standard that would enable practitioners to report on an examination or review engagement under the attestation standards without having to request a written assertion from the responsible party. The ASB discussed issues related to direct engagements and concluded that

- the proposed direct engagement standard may refer to the phenomenon that is measured or evaluated against criteria as *subject matter*, which is consistent with the term used in SSAE No. 18, *Attestation Standards: Clarification and Recodification*. Canadian Standard on Assurance Engagements 3001, *Direct Engagements*, uses the term *underlying subject matter*.
- most engagements performed under the assertion-based attestation standards may also be performed under the direct engagements standards. However, factors such as the following are relevant to the practitioner’s decision about whether to perform the engagement under the direct engagements standards:
 - Law or regulation may require that the engagement be performed under the assertion-based attestation standards
 - The subject matter is internal control based on the COSO criteria. (If management is unable to provide an assertion because it is unable to evaluate the subject matter against the criteria, the likelihood is that the opinion will be modified.)

- in most direct engagements the practitioner is the measurer or evaluator of the subject matter
- it does not have any preference about whether there should be provision in the engagement letter acknowledging that the responsible party is not required to provide an assertion
- modified opinions are as applicable to direct engagements as they are to assertion-based engagements; the fact that the practitioner is the measurer or evaluator of the subject matter in a direct engagement does not affect the practitioner's ability to express a modified opinion
- An engaging party's request to change from an assertion-based engagement to a direct engagement
 - would be considered justifiable if the responsible party misunderstood the terms of the engagement, which the responsible party states were not sufficiently specific with respect to the assertion
 - would not be considered justifiable if during the course of the engagement, the practitioner identifies misstatements in the subject matter that the responsible party was not aware of and the responsible party is no longer confident in its assertion or does not wish to provide an assertion that identifies the misstatements.
- a direct report should not necessarily be a restricted-use report.

The ASB had the following suggestions about how the practitioner's report on a direct engagement should differ from a practitioner's report on an assertion-based engagement:

The direct report should

- state that the practitioner is the measurer or evaluator of the subject matter
- include an opinion and may include findings; alternatively, include findings rather than an opinion
- include a statement that the responsible party did not provide the practitioner with a written assertion

2. Specified Procedures

Mr. Ard, Chair of the Specified Procedures Task Force, led a discussion, the objective of which was to review and obtain feedback on issues related to the proposed specified procedures standard and to review a first-read draft of the proposed standard.

Applicability of the Standard

Mr. Ard stated that while the ASB directed that the proposed standard include no preconditions, to clarify when the standard would not apply, the Task Force felt it was necessary to identify situations in which the standard should not be applied. Therefore, the Task Force proposed that

the draft standard include the following as paragraph X.4 (and corresponding application paragraph X.A1):

X.4 This section does not apply to engagements to

- a. apply agreed-upon procedures;
- b. issue letters (commonly referred to as *comfort letters*) to underwriters and certain other requesting parties;
- c. conclude that the subject matter is in accordance with the criteria; or
- d. measure the subject matter against certain criteria (for example, regulations).

Additionally, an engagement to perform specified procedures may not be sufficient when the engaging party is required by law, regulation, or contract to engage a practitioner to perform an agreed-upon procedures engagement. (Ref: par. X.A1)

X.A1 Nothing in this standard is intended to preclude a practitioner from performing a specified procedures engagement and an agreed-upon procedures engagement on the same subject matter.

Mr. Santay stated that neither of the proposed paragraphs are necessary as the standard should not drive a practitioner to specified procedures or agreed-upon procedures. Mr. Ard stated that the Task Force felt that guidance needed to be provided because, unlike an engagement on financial statements where an accountant would not perform an audit and a review on the same set of financial statements, a practitioner may perform specified procedures and agreed-upon procedures on the same subject matter. Because practitioners are accustomed to reporting only on the highest level of service performed, guidance that separate reporting is permitted may be needed.

Mr. Dalkin questioned the need for subparagraph d to proposed paragraph X.4.

Mr. Montgomery stated that, at least in its infancy, practitioners will need guidance as to how to differentiate a specified procedures engagement from an agreed-upon procedures engagement. Mr. Montgomery suggested that perhaps the scope paragraphs could be drafted in such a way as to provide a clear differentiation from agreed-upon procedures engagements and also provide a reference to the agreed-upon procedures literature if the engagement fits the agreed-upon procedures criteria. Such paragraphs should focus on what a specified procedures engagement is as opposed to what it is not.

Ms. Burzenski stated that the introduction section should clearly state what the user will get that they would not get from a report on agreed-upon procedures.

Mr. Santay stated that the proposed standard should not imply that a specified procedures engagement is always a two-party engagement as the engaging party may not be the responsible party.

Ms. Kassman questioned whether it is appropriate to have two separate engagements – specified procedures and agreed-upon procedures – and suggested that perhaps it would be appropriate to revise the agreed-upon procedures literature so that it mirrors the proposed specified procedures engagement. Mr. Santay suggested that a specific question could be included in the exposure draft of the proposed standard asking respondents whether the proposed engagement should supplement, revise, or replace agreed-upon procedures engagements.

Responsibility for the Sufficiency of the Procedures

Mr. Ard reminded the ASB members that, at its meeting in May 2016, the Board directed that the standard not require the engaging party to accept responsibility for the sufficiency of the procedures performed as the engaging party may not have a basis for making such a determination. Subsequently, the Task Force drafted the proposed standard such that there would be no requirement for any party to accept responsibility for the sufficiency of the procedures.

Mr. Ard directed the ASB to paragraph X.A23 of the proposed standard which reads:

X. A23 The specified procedures may be designed by the practitioner, the engaging party, or an other party. Neither the practitioner, engaging party, nor any other party are required to take responsibility that the specified procedures are sufficient to meet the objectives of the engagement or the anticipated expectations of any potential user of the practitioner’s specified procedures report. However, nothing precludes the engaging party or an other party from taking such responsibility or the practitioner from requesting that the engaging party or other party take such responsibility.

Ms. Kassman questioned how an engagement could be performed in which no one accepts responsibility for the sufficiency of the procedures performed.

Mr. Kaye stated that the report will need to clearly state that procedures were designed to meet the objectives of the engagement but may not be sufficient for all purposes.

The proposed standard may need to provide differential requirements when the practitioner accepts responsibility for the sufficiency of the procedures versus the engaging party, an other party, or no one taking responsibility.

Mr. Panucci questioned the statement in paragraph X.2 of the proposed standard which states that the subject matter is the responsibility of “another party”. Mr. Panucci stated that, if it is required that a party take responsibility for the subject matter, that the standard will need to explain the difference between taking responsibility for the subject matter versus the procedures.

Using the Work of a Practitioner’s External Specialist

Ms. Kassman expressed concern about the potential over use of an external specialist in the performance of a specified procedures engagement and suggested that the proposed standard include application guidance reminding practitioners that they need to have the appropriate skills, knowledge, and expertise to perform the engagement.

Other Information

Mr. Panucci questioned why requirements with respect to other information is necessary in an engagement in which the report provides no opinion or conclusion on the subject matter. Ms. Schweigel suggested that application guidance be included to warn practitioners of the dangers of general use reporting.

Reporting

Mr. Ard directed the ASB members to paragraphs X.25 – X.27 of the draft proposed standard which include the general reporting requirements. Mr. Ard pointed out that some key elements of the report include the following:

- The report is required to include an appropriate addressee. Application guidance is included stating that the addressee is most commonly the engaging party as opposed to anticipated users of the report.
- The report is required to include an identification of the party that is responsible for the subject matter of the engagement.
- Unless the practitioner is taking responsibility for the sufficiency of the procedures, the report is required to state that the practitioner makes no representation regarding the sufficiency of the procedures.
- While not required, application guidance is included to state that the practitioner may make clear in the report that an agreed-upon procedures engagement was not performed.
- While not required, application guidance is included to state that the practitioner may consider communicating that a written assertion was not obtained.

Additionally, in order to illustrate how the Task Force envisions the specified procedures report to look, the Task Force has presented two illustrations in an exhibit to the proposed standard. Those examples illustrate:

- An independent accountant's report on applying specified procedures in connection with a lottery drawing
- An independent accountant's report on applying specified procedures in connection with a union election

Mr. Montgomery suggested that the report simply state the objective of the engagement and that the procedures were developed to meet the objective and not include a statement regarding whether the procedures may be sufficient for other purposes.

Mr. Kaye questioned what the practitioner would do if the practitioner determined that the report was potentially misleading and suggested that the proposed standard include requirements and guidance when the practitioner considers that the report may be misleading. Mr. Panucci suggested that perhaps instead of a requirement for the practitioner to consider whether the report

may be potentially misleading, that application guidance could be included that provides examples of procedures and findings that may be potentially misleading.

Ms. Burzenski stated that application guidance is needed that makes clear that the practitioner is not precluded from including personally identifiable information in the findings.

Ms. Kassman stated that the illustrative reports include a significant amount of language stating what the engagement is not and suggested that clear statements as to what the practitioner did do along with a simple statement that no opinion or conclusion is expressed should be sufficient.

Restricted Use Report

Mr. Panucci stated that he is concerned that some of the application guidance with respect to consideration as to whether the procedures, findings, or the report itself may not be appropriate for general distribution seemed to direct practitioners to restrict the use of the report. Mr. Panucci reminded the ASB that the Task Force was directed to draft a standard that would include a general-use report.

Mr. Montgomery suggested that the requirements and guidance included in the draft regarding restricted use reporting should be removed as restricted use reporting may be an element that would direct the practitioner to performing an agreed-upon procedures engagement.

Ms. Schweigel suggested that application guidance be included that states that while the practitioner is not required to restrict the use of any specified procedures report that there is no preclusion from doing so.

Consideration of Subsequent Events and Subsequently Discovered Facts

Ms. Gantnier questioned why the proposed standard included a requirement for the practitioner to consider subsequent events and subsequently discovered facts and suggested that such a procedure would just be an additional specified procedure that the practitioner may perform and report on.

Mr. Panucci suggested that, in the situation where the practitioner accepts responsibility for the sufficiency of the procedures, the practitioner be required to consider subsequent events and subsequently discovered facts.

Effective Date

The ASB stated that perhaps the proposed standard should include an effective date six months after issuance so that practitioners can properly consider the requirements of the standard as well as training of staff.

Next Steps

Mr. Ard stated that the Task Force will plan to present a revised draft of the proposed standard to the ASB at its meeting in October 2016. While the Task Force may ask the ASB to vote to expose the proposed standard for public comment at the October 2016 meeting, it is more likely that such a vote would be requested for the January 2017 meeting.

3. Data Analytics

Brian Collins, Chair of the ASEC Data Analytics Guide Working Group, discussed the Audit Data Analytics (ADA) Guide and reviewed the slide deck provided to the ASB. He explained that the Working Group had met the day before and decided to expand the flow chart into three charts. A draft of the chapter will be sent to the ASB next week.

Topics discussed, all of which will be addressed in the Guide, included

- The use of audit data analytics at various stages of the audit, including planning, substantive procedures, and review.
- Data validation: completeness and accuracy, as well as management’s ability to manipulate internally-prepared data and the need to determine the relevance of external data and that it has been imported correctly.
- That the topics and information in the Analytical Procedures Guide, which the ADA Guide will replace, are being tracked and included in the ADA Guide.
- What to title the Guide to inform potential users that it encompasses both audit data analytics and analytical procedures (analytical procedures are a subset of audit data analytics).
- That the Guide will be written at a basic level and will be tool-agnostic; many of the analytics can be performed using Excel. CPE is being developed around the Guide.

4. Auditor Reports on ERISA Audits

Mr. Schubert, chair of the EBP Auditor Reporting Task Force (EBP task force), led the ASB in a discussion of issues relating to developing a new standard to address performance and reporting requirements for audits of financial statements of employee benefit plans subject to ERISA.

Issue 1 — Reporting on Specific Considerations Relating to Selected Plan Provisions

The ASB discussed various titles for the new reporting element in the proposed SAS. The ASB supported changing the title to “Reporting on Specific Plan Provisions Relating to the Financial Statements.”

The ASB discussed the content in paragraph .37 of the proposed SAS and provided the task force with specific feedback. The ASB:

- asked the task force to revise the proposed SAS to better reflect that the required procedures relating to the specific plan provisions are part of the audit of the financial statements and that there is a new reporting component related to such audit procedures
- directed the task force to include a requirement that the auditor needs to obtain a plan document (or its equivalent). Without a plan document, the auditor would not be able to audit the plan
- directed the task force to include the audit assertions in the application material relating to the required procedures for reporting on the specific plan provisions

- supported allowing the option for a separate report but suggested the proposed SAS encourage the report be combined with the auditor’s report
- asked the task force to include all areas that are tested in the description in the *Report on Specific Plan Provisions Relating to the Financial Statements*
- asked that the report include a specific reference to the proposed SAS so that there is context for this new report.

Issue 2 — Listing of Findings and the DOL’s Voluntary Fiduciary Correction Program

The ASB discussed the DOL’s VFCP program. The ASB continues to support the inclusion of the findings from the procedures performed as part of the audit, in the *Report on Specific Plan Provisions Related to the Financial Statements*. The ASB asked the task force to

- include illustrations of example findings
- include application material to explain that the findings may be either general or more specific.
- consider including a warning about personally identifiable information.

Issue 3 — Revised Report on ERISA-Permitted Scope Limitation is Imposed

The ASB discussed the example auditor’s report when the ERISA-permitted scope limitation is imposed. The ASB asked the task force to

- consider whether portions of the report could be scaled back due to the informational nature of the content
- consider adding the percentage of investments that are certified to the auditor’s report to provide users of the financial statements with context
- revise the wording of the opinion paragraph because as drafted, it is perceived to be a qualified opinion. The ASB supports the development of a standalone report for ERISA plan financial statements when the ERISA-permitted scope limitation is imposed. Such opinion wording would not be tied to AU-C 700, *Forming an Opinion and Reporting on Financial Statements* or AU-C 705, *Modifications to the Opinion in the Independent Auditor’s Report*. The ASB asked the task force to consider whether there needs to be reference to the auditor’s use of the certification for completeness and accuracy of the certified investment information. In addition, the ASB asked the task force to consider other alternatives for the wording of the opinion.

Other Comments

The ASB provided feedback on the proposed SAS. The ASB directed the task force to

- include all relevant reporting requirements in the proposed SAS and scope ERISA plan audits out of AU-C 700
- consider consistent use of plan administrator and plan management throughout the document and better define it earlier in the proposed SAS

- add a reference to the AICPA Audit and Accounting Guide, *Employee Benefit Plans* and include a reminder that the guide is an interpretive publication. Look for ways to leverage the guide material without repeating it in the proposed SAS
- consider including the use of special purpose frameworks, as permitted by ERISA

This topic will be discussed at a future meeting.

5. Cybersecurity

Chris Halterman, chairman of the ASEC Cybersecurity Working Group, updated the ASB on the status of the ASEC/ASB project to develop an entity-wide cybersecurity examination engagement to be performed under the attestation standards and a related practitioner guide. The purpose of the cybersecurity examination is to provide a variety of stakeholders with useful information about an entity's cybersecurity risk management program and a CPA's opinion on whether that information is presented in accordance with suitable criteria. The CPA's opinion enhances the degree of confidence that users can place in the information.

In the cybersecurity examination described in this guide, useful information about an entity's cybersecurity risk management program includes the following:

- A description of the entity's cybersecurity risk management program based on the *description criteria*.
- An assessment of the effectiveness of the controls included in that program to achieve the entity's cybersecurity objectives based on the *control criteria*.

The following issues were discussed:

- The difference between information security and cybersecurity. Practically, there is little difference between these two terms.
- The auditor's responsibility for cybersecurity in a financial statement audit. While the auditor understands and tests security controls over financial reporting in the financial statement audit, the auditor is not responsible for the broader range of controls the entity has designed, implemented, and maintains to achieve its cybersecurity objectives, many of which support the entity's operations and compliance objectives. This topic is addressed in CAQ Alert #2014-3, *Cybersecurity and the External Auditor*.
- The competencies required to perform these engagements. Amanda Black updated the group on other efforts underway at the AICPA related to the cybersecurity project, including the development of web casts, e-learning, and a resource website for members.
- The use of specialists in the cybersecurity examination. The responsibility to express an opinion is the practitioner's, regardless of the extent to which he or she use the work of specialists. If the practitioner is unable to properly supervise the work of the specialists, or if the work of the specialist on the engagement is extensive, questions may arise about the practitioner's ability to express an opinion.

- The focus of the proposed cybersecurity examination on an entity-wide cybersecurity program. While the guide will provide guidance on performing and reporting on an entity-wide engagement, it also enables practitioners to perform an engagement on a business unit or division of an entity, or on a specific type of information or system used by an entity.
- The preparation and maintenance of mappings of the revised trust services criteria for security, availability and confidentiality — which are suitable *control criteria* in the cybersecurity engagement— to other security frameworks to assist the practitioner in determining whether such other frameworks are suitable for use as description criteria in the engagement.
- Whether the proposed form of practitioner’s report is in accordance with the requirements of AT-C section 205. The report is in compliance with those requirements, but contains additional information in some cases. Many believe this is appropriate based on the communications that might be necessary when new subject matter, such as cybersecurity, is being reported on.
- Whether an assertion should be required in the proposed engagement. Because of the business risk associated with the engagement, many believe that the engagement should not be performed without an assertion by management in which it accepts responsibility for the entity’s cybersecurity risk management program and indicates that it has a reasonable basis for its assertion.
- Whether a financial statement auditor would be able to rely on a practitioner’s cybersecurity examination report when performing the financial statement audit. When such engagements are performed, the auditor would be able to rely on it.
- Whether a financial statement auditor can provide cybersecurity consulting services (sometimes referred to as *readiness engagements*) to his or her audit client without impairing independence. PEEC is currently looking into this issue and will develop guidance if needed.
- Whether to use the term *fair presentation* in the practitioner’s opinion on the description of the entity’s cybersecurity risk management program rather than *presented in accordance with*? This issue will be discussed with the AITF/ASB joint working group formed to assist the ASEC Cybersecurity Working Group with technical issues related to the proposed engagement.

Mr. Halterman also discussed the process used to develop the *description criteria* and to revise the trust services criteria. The trust services criteria were revised to align with the seventeen principles in the 2013 COSO framework and to address cybersecurity risks in trust services engagements. (The revised trust services criteria for security, availability and confidentiality constitute suitable *control criteria* for evaluating the design and operating effectiveness of controls in the cybersecurity engagement; however, management is responsible for selecting the

criteria and may select any criteria as long as it is considered suitable in accordance with the attestation standards.)

ASEC is currently reviewing drafts of exposure drafts of both the description criteria and the revised trust services criteria. Once ASEC has cleared the exposure drafts, they will be issued with a 75-day comment period. A mid-September issuance is expected.

The Working Group expects to bring a draft of the cybersecurity attestation guide to the ASB sometime in October 2016. Mr. Halterman plans to attend the October ASB meeting to update the ASB on the status of the project.

6. Auditor Reporting

Mr. Montgomery led a discussion about certain elements of the auditor's report relating to ASB's convergence with the International Auditing and Assurance Standards Board (IAASB) International Standards on Auditing (ISA) 700 (Revised) *Forming an Opinion and Reporting on Financial Statements*, and the proposed way forward on guidance for the communication of key audit matters.

Issue 1 — Key Audit Matters/Critical Audit Matters

Mr. Montgomery provided the ASB with an education session about the IAASB's key audit matters as compared to the PCAOB's reproposal on critical audit matters. The ASB supported convergence with ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report* and asked the task force to consider, as they develop the proposed SAS, ways to reconcile the ASB's proposed SAS on key audit matters to the PCAOB's auditor reporting model of critical audit matters. The ASB will discuss key audit matters at a future meeting.

Issues 2 and 3 — Illustrative Reports and Report Elements

Mr. Montgomery led the ASB through a discussion regarding certain elements of the proposed report. The ASB supported the proposed AU-C 700 wording for many of the elements. The ASB also —

- Asked the task force to consider identifying possible “other ethical responsibilities” as part of the application material and/or requiring the applicable ethical responsibilities to be identified in the auditor's report.
- Asked the task force to consider the guidance relating to going concern and to
 - consider revising the wording in the proposed SAS relating to describing management's responsibilities to not only assess the entity's ability to continue as

a going concern but also whether the use of the going concern basis of accounting is appropriate (consistent with ISA 700 (revised))

- consider ways to make the proposed standard framework neutral as it relates to going concern
- consider ways to better balance the auditor's report content such that the discussion about management's responsibilities for going concern is on par with that of the auditor's responsibilities
- Questioned the use of the word "guarantee" within the context of defining reasonable assurance. The task force was asked to research the use of "guarantee" in the professional standards.
- Asked the task force to reconsider the ISA 700 wording that says the risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error..." because certain members of the ASB believe the words imply a level of audit work related to fraud beyond that required by the auditing standards.
- Asked the task force to reconsider the wording in the requirements relating to divided responsibility in a group audit situation.
- Asked the task force to provide application material to better explain Other Reporting Responsibilities in the United States.
- Directed the task force to change the auditor's address requirement to include the city and state where the auditor's report is issued rather than where the auditor practices.

The ASB will discuss this topic again at the October 2016 ASB meeting.

7. Other Information

Ms. Gantnier, Chair of the Other Information Task Force (Task Force), led a discussion of issues with respect to the Task Force's project to revised AU-C section 720, *Other Information in Documents Containing Audited Financial Statements*.

Background

A first draft of a proposed revised AU-C section 720 was presented to the ASB at its meeting in May 2015. The proposed revised SAS used ISA 720 (Revised) as a base and represented the Task Force's efforts to harmonize AU-C section 720, with ISA 720 (Revised) while minimizing differences with the proposed PCAOB standard dealing with other information. At the meeting, the ASB directed the Task Force to redraft the proposed revised SAS and instead of using ISA 720 (Revised) as a base, to use extant AU-C 720 as a base and:

- Define the term *annual report* so that practitioners are clear as to what documents are in the scope of the standard
- Retain work effort/performance requirements from extant AU-C section 720
- Retain reporting requirements from extant AU-C section 720 (that is, while the auditor is not precluded from reporting, there is no reporting requirement)

A revised draft standard was included in the agenda materials for the ASB's July 2015 meeting. However, the discussion was deferred and subsequently, the ASB decided that the proposed standard should not be presented again to the Board until after the PCAOB finalizes its standard.

The Task Force was asked to present a draft standard to the Board at its August 2016 meeting— but using ISA 720 (Revised) as a base. Mr. Montgomery stated that the PCAOB had bifurcated the auditor report and other information projects and at the present time, other information is not on the PCAOB's agenda. Mr. Santay stated that the potential PCAOB standard should not be emphasized. Ms. Burzenski stated that she sees no reason to not use ISA 720 (Revised) as a base given the ASB's commitment to converge with the ISAs.

Composition of the Task Force

Mr. Dalkin stated that it is important that the Task Force include government representation. Ms. Gantnier stated that she and Mr. Glynn will work with Ms. Goldman to make sure that the composition of the Task Force is appropriate.

Definition of *annual report* and clarification of the documents in the scope of the SAS

Ms. Gantnier stated that an issue with extant AU-C section 720 is that practitioners often misapply the standard as they feel that it applies to all instances where the audited financial statements are included in documents containing other information – when, in fact, the scope of the standard is limited to “annual reports or similar documents that are issued to owners or similar stakeholders and annual reports of governments and organizations for charitable or philanthropic purposes that are available to the public that contain audited financial statements and the auditor's report thereon”.

To clarify that AU-C section 720 is required to be applied only to the annual report, the Task Force proposes to revise the title of the section to “The Auditor's Responsibilities Regarding Other Information in Annual Reports”. In addition, the Task Force proposes to include the following definition of *annual report* in the proposed revised AU-C section 720:

Annual report. A document prepared typically on an annual basis by management or those charged with governance, the purpose of which is to provide owners (or similar stakeholders) with information on the entity's operations and the entity's financial results and financial position as set out in the financial statements. An annual report contains or incorporates by reference the financial statements and the auditor's report thereon. Annual reports include annual reports of governments and organizations for charitable or philanthropic purposes that are available to the public. (Ref: Para. A5–A6)

The Task Force also determined to include the following application guidance from ISA 720 (Revised):

A5. An annual report is typically prepared on an annual basis. However, when the financial statements being audited are prepared for a period less than or more than a year, an annual report may also be prepared that covers the same period as the financial statements.

A6. An annual report may be made available to users in printed form, or electronically, including on the entity's website. A document may meet the definition of an annual report, irrespective of the manner in which it is made available to users.

While the definition of *annual report* is primarily from ISA 720 (Revised), there are a few differences of note:

- 1) The proposed SAS definition excludes “combination of documents” and “documents accompanying the audited financial statements and the auditor’s report thereon” as the annual report is intended to be one document which contains, or incorporates by reference, the audited financial statements and the auditor’s report thereon. Mr. Greene stated that occasionally annual reports are in multiple documents so, it may not be appropriate to exclude the language. Mr. Panucci expressed concern that “combination of documents” wording may scope in certain documents that are not intended to be part of the annual report and stated that “included or incorporated by reference” may be more appropriate as the IAASB was addressing documents that are not relevant in the United States of America. Mr. Reisig stated that he does not have a firm understanding as to how “incorporated by reference” would apply in an audit of a nonissuer and stated that the proposed standard may be more understandable if it ran to what is included in the annual report document. Mr. Montgomery stated that “incorporated by reference” would not be needed if the ISA 720 (Revised) definition of annual report is used as “combination of documents” would cover. Mr. Santay stated, however, that “combination of documents” cannot be used unless there is a fence around what documents are included.
- 2) For clarity, the proposed SAS excludes the phrase “in accordance with law, regulation or custom” as such phrase is not deemed necessary for American auditors.
- 3) “Contains or incorporates by reference” wording added to the proposed SAS definition to make clear that to be considered an annual report (and therefore within the scope of the standard), the document must contain or incorporate by reference the audited financial statements and the auditor’s report thereon.
- 4) The proposed SAS includes the concept of annual reports of governments and charitable organizations from extant AU-C section 720.

In response to a question from Mr. Hansen, Ms. Gantnier stated that it is the intent to be clear that the proposed standard, consistent with extant AU-C section 720, does not apply to all documents – just those contained in “annual reports or similar documents that are issued to owners or similar

stakeholders and annual reports of governments and organizations for charitable or philanthropic purposes that are available to the public that contain audited financial statements and the auditor's report thereon.”

Mr. Kaye suggested that application guidance be added that clarifies that while an entity may refer to a document as an “annual report” that such document may not meet the definition of annual report for purposes of the proposed standard.

Ms. Gantnier stated that ISA 720 (Revised) includes an exercise that the auditor is required to go through with management to determine what the annual report consists of. That exercise includes:

- Discussions with management as to what is in the annual report and the timing of issuance of documents
- Making arrangements with management to obtain the documents
- If documents will not be available until after the date of the auditor's report, get a representation that the documents will be provided to the auditor and that the auditor will apply the required procedures prior to issuance of those documents.

Ms. Gantnier stated that given the proposed definition of “annual report”, the Task Force does not believe that there is a need for the auditor to go through the ISA exercise. Ms. Schweigel stated that she sees value in going through the exercise with management so that there is no misunderstanding as to what the auditor is reading. Mr. Reisig stated that the proposed standard should include a requirement for the auditor to obtain a written representation regarding management's understanding as to what the annual report consists of.

Omitted Information

Ms. Gantnier stated that ISA 720 (Revised) includes the concept that the other information is misleading if it “omits or obscures information necessary for a proper understanding of a matter disclosed in the other information”. However, extant AU-C section 720 does not include requirements with respect to omitted information. The Task Force did not include a requirement or guidance with respect to omitted information in the draft proposed standard.

Further, Ms. Gantnier stated that ISA 720 (Restated) states that a misstatement of the other information exists when the other information is incorrectly stated or otherwise misleading (including because it omits or obscures information necessary for a proper understanding of a matter disclosed in the other information). The proposed SAS does not run to “misstatements of the other information” but instead retains the concepts from AU-C section 720 of *inconsistency* (other information that conflicts with information contained in the audited financial statements) and *misstatement of fact* (other information that is unrelated to matters appearing in the audited financial statements that is incorrectly stated or presented). The proposed SAS also retains the

AU-C section 720 required responses when the auditor identifies a material inconsistency or a material misstatement of fact.

Ms. Gantnier reminded the ASB members that at the January 2015 ASB meeting, Don Pallais stated that the definition of *misstatement of the other information* in ISA 720 (Revised) is fatally flawed as the ASB has avoided the use of the term *misleading* in the standards as no criteria exists as to what *misleading* means. Ms. Gantnier also stated that Mr. Landes had advised that retaining the construct from extant AU-C section 720 would not result in an ISA minus scenario as long as the work effort is the same.

Ms. Johnigan stated that if the AICPA *Code of Professional Conduct* does not include language from the International Ethics Standards Board for Accountants *Code of Ethics for Professional Accountants* regarding requirements for the auditor to avoid being knowingly associated with information that the auditor believes contains a materially false or misleading statement, statements or information furnished recklessly, or omits or obscures information required to be included where such omission or obscurity would be misleading, the ASB needs to avoid use of the term *misleading*. Mr. Santay stated that the ASB will need to know what the AICPA Code states.

Ms. Gantnier asked whether it would be possible to include omitted information as an inconsistency between the other information and the audited financial statements. If so, perhaps an application paragraph could be developed.

Reporting

Messrs. Montgomery and Hansen stated that some form of required auditor reporting is in the public interest.

Next Steps

Ms. Gantnier stated that the Task Force will plan to present a draft of the proposed standard to the ASB at its meeting in October 2016, using ISA 720 (Revised) as a base.

8. IAASB and ITC Update

Mr. Hasty and Ms. Goldman provided an update to the ASB on the recent activities of the IAASB. Ms. Snyder discussed the IAASB NOCLAR project and PEEC's approach to that project.

The meeting adjourned at 11am on Thursday, August 04, 2016.