



**Agenda Item 6A**

***PROPOSED AU-C Section 701, Communicating Key Audit Matters in the Independent Auditor’s Report  
(MARKED TO ISA 701, Communicating Key Audit Matters in the Independent Auditor’s Report)***

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<b>Application and Other Explanatory Material</b>		
<b>Communicating Key Audit Matters in the Independent Auditor’s Report</b>		Proposed AS 3101, <i>The Auditor’s Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion</i>	
<b>Introduction</b>			
<b>Scope of this <del>ISA</del> <u>Proposed SAS</u></b>			
1. This <del>International Standard</del> <u>proposed Statement</u> on Auditing <del>(ISA) deals with Standards</del> <u>(SAS)</u> addresses the auditor’s			

† †The proposed wording for AU-C 701 uses certain International Federation of Accountants (IFAC) copyright material, used with the permission of IFAC.

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
<p>responsibility <del>to communicate</del><u>when</u> key audit matters <u>are communicated</u> in the auditor’s report. It is intended to address both the auditor’s judgment as to what to communicate in the auditor’s report and the form and content of such communication.</p>			
<p>2. The purpose of communicating key audit matters is to <del>enhance the communicative value of the auditor’s report by providing</del><u>provide</u> greater transparency about the audit that was performed. <del>Communicating key audit matters provides additional information to intended users of the financial statements (“intended users”) to assist them in understanding those matters that, in the auditor’s professional judgment, were of most significance in the audit of the financial statements of the current period. Communicating key audit matters may also assist intended users in understanding the entity and areas of significant management judgment in</del><u>The communication of key audit matters in</u></p>	<p><b>Scope of this <del>ISA</del><u>Proposed SAS</u></b> (Ref: <del>Para</del><u>par.</u> 2)</p> <p><u>A1. Communicating key audit matters provides additional information to intended users of the financial statements (“intended users”) to assist them in understanding those matters that, in the auditor’s professional judgment, were of most significance in the audit of the financial statements of the current period. Communicating key audit matters may also assist intended users in understanding the entity and areas of significant management judgment in the audited financial statements.</u></p> <p><u>A2. A1.</u> Significance can be described as the relative importance of a matter, taken in context. The significance of a matter is judged by the auditor in the context in which it is being considered. Significance can be considered in the context of quantitative and qualitative factors, such as relative magnitude, the nature and effect on the subject matter and the expressed interests of intended users or recipients. This involves an objective analysis of the facts and circumstances, including the nature and extent of communication with those charged with governance.</p>		

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<p><u>the auditor's report may also provide intended users a basis to further engage with management and those charged with governance about certain matters relating to the entity, the audited financial statements, or the audit that was performed.</u> (Ref: <del>Para</del><u>par.</u> .A1–.A3)</p>			
	<p><del>A2.— Users of financial statements have expressed an interest in these matters about which the auditor had the most robust dialogue with those charged with governance as part of the two-way communication required by ISA 260 (Revised)† and have called for additional transparency about those communications. For example, users have expressed particular interest in understanding significant judgments made by the auditor in forming the opinion on the financial statements as a whole, because they are often related to the areas of significant management judgment in preparing the financial statements.</del></p>		<p>The task force believes that paragraph .A2 is not needed in the U.S.</p>
	<p><del>A3.— Requiring auditors to communicate key audit matters in the auditor's report may also enhance communications between the auditor and those charged with governance about those matters, and may increase attention by management and those charged with governance to the disclosures in the financial statements to which reference is made in the auditor's report.</del></p>		<p>Not necessary in the proposed SAS because KAM is voluntary.</p>

†—ISA 260 (Revised), *Communication with Those Charged with Governance*

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	<p><del>A3. A4. ISA 320</del><sup>21</sup><u>AU-C 320</u><sup>1</sup> <i>Materiality in Planning and Performing an Audit</i> explains that it is reasonable for the auditor to assume that users of the financial statements:</p> <ul style="list-style-type: none"> <li>(a) Have a reasonable knowledge of business and economic activities and accounting and a willingness to study the information in the financial statements with reasonable diligence;</li> <li>(b) Understand that the financial statements are prepared, presented and audited to levels of materiality;</li> <li>(c) Recognize the uncertainties inherent in the measurement of amounts based on the use of estimates, judgment and the consideration of future events; and</li> <li>(d) Make reasonable economic decisions on the basis of the information in the financial statements.</li> </ul> <p>Because the auditor's report accompanies the audited financial statements, the users of the auditor's report are considered to be the same as the intended users of the financial statements.</p>		

<sup>21</sup> [ISA AU-C 320](#), *Materiality in Planning and Performing the Audit*, paragraph 4

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<p><del>3. The communication of key audit matters in the auditor's report may also provide intended users a basis to further engage with management and those charged with governance about certain matters relating to the entity, the audited financial statements, or the audit that was performed.</del></p>			
<p><u>3.</u> <del>4.</del> Communicating key audit matters in the auditor's report is in the context of the auditor having formed an opinion on the financial statements as a whole. Communicating key audit matters in the auditor's report is not:</p>			
<p>(a) A substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation;</p>			
<p>(b) A substitute for the auditor expressing a modified opinion when required by the circumstances of a specific</p>			

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<p>audit engagement in accordance with <del>ISA</del><a href="#">proposed AU-C 705 (Revised)</a>;<sup>3</sup> <a href="#">Modifications to the Opinion in the Independent Auditor's Report.</a></p>			
<p>(c) A substitute for reporting in accordance with <del>ISA—570 (Revised) when a material uncertainty exists relating to events that may cast significant doubt on an</del><a href="#">proposed AU-C 570 Going Concern</a> if, after <a href="#">considering identified conditions or events and management's plans, the auditor concludes that substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time remains</a>; or</p>			<p>This is a placeholder – need to add reporting requirements in 570 and add par reference once there is one.</p>

<sup>3</sup>—ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*

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<p>(d) A separate opinion on individual matters. (Ref: <del>Parapar. A4-A76</del>)</p>	<p><i>Relationship between Key Audit Matters, the Auditor’s Opinion and Other Elements of the Auditor’s Report</i> (Ref: <del>Parapar. 3, 11, 14</del>)</p> <p><del>A4. A5. ISA 700 (Revised)</del><u>Proposed AU-C 700 Forming an Opinion and Reporting on Financial Statements</u> establishes requirements and provides guidance on forming an opinion on the financial statements.<sup>42</sup> Communicating key audit matters is not a substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation. <del>ISA Proposed AU-C 705 (Revised)</del> addresses circumstances in which the auditor concludes that there is a material misstatement relating to the appropriateness or adequacy of disclosures in the financial statements.<sup>53</sup></p> <p><del>A5. A6. When the auditor expresses a qualified or adverse opinion in accordance with ISA 705 (Revised) proposed AU-C 705, communicating key audit matters would still be relevant to enhancing intended users’ understanding of the audit. In these circumstances, presenting the description of at the matter giving rise to a modified opinion in the Basis for Qualified (Adverse) Opinion section helps to promote intended users’ understanding and to identify such circumstances when they occur.</del></p>		<p>Paragraph .A6 – need to consider wording relating to GC</p> <p>Task force supports precluding KAM when the auditor issues an adverse opinion or disclaims an opinion.</p> <p>IAASB – only precludes KAM when disclaiming an opinion.</p> <p>PCAOB precludes CAM for both adverse and disclaimer.</p>

<sup>4</sup> ~~ISA 700 (Revised);~~<sup>2</sup> Proposed AU-C 700, paragraphs 10–15 and A14–A1014

<sup>5</sup> ~~See paragraph A7 of ISA 705 (Revised).~~

<sup>3</sup> See paragraph A7 of AU-C 705.

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	<p><del>Separating</del><a href="#">Opinion section gives it the appropriate prominence in the auditor's report (see paragraph 14) and separates</a> the communication of this matter from <a href="#">any</a> other key audit matters described in the Key Audit Matters section <del>therefore gives it the appropriate prominence in the auditor's report (see paragraph 14). The Appendix in ISA 705 (Revised). The Exhibit in proposed AU-C 705</del> includes illustrative examples of how the introductory language in the Key Audit Matters section is affected when the auditor expresses a qualified <del>or adverse</del> opinion and other key audit matters are communicated in the auditor's report. Paragraph <del>A5755</del> of this <del>ISA</del><a href="#">proposed SAS</a> illustrates how the Key Audit Matters section is presented when the auditor has determined that there are no other key audit matters to be communicated in the auditor's report beyond matters addressed in the Basis for Qualified <del>(Adverse)</del> Opinion section or <del>Material Uncertainty Related to</del> Going Concern section of the auditor's report.</p> <p><del>A7. When the auditor expresses a qualified or adverse opinion, communicating other key audit matters would still be relevant to enhancing intended users' understanding of the audit, and therefore the requirements to determine key audit matters apply. However, as an adverse opinion is expressed in circumstances when the auditor has concluded that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.<sup>6</sup></del></p>		

<sup>6</sup>—ISA 705 (Revised), paragraph 8

~~• Depending on the significance of the matter(s) giving rise to an adverse opinion, the auditor may determine that no other matters are key audit matters. In such circumstances, the requirement in paragraph 15 applies (see paragraph A58).~~

~~• If one or more matters other than the matter(s) giving rise to an adverse opinion are determined to be key audit matters, it is particularly important that the descriptions of such other key audit matters do not imply that the financial statements as a whole are more credible in relation to those matters than would be appropriate in the circumstances, in view of the adverse opinion (see paragraph A47).~~

A6. A8. ISA 706 (Revised)<sup>7</sup> Proposed AU-C 706, *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report* establishes mechanisms for auditors of financial statements of all entities to include additional communication in the auditor's report through the use of ~~Emphasis of Matter~~emphasis-of-matter paragraphs and ~~Other Matter~~other-matter paragraphs when the auditor considers it necessary to do so. ~~In such cases, these paragraphs are presented separately from~~However, when proposed AU-C 701 applies, the use of an emphasis-of-matter or other-matter paragraph is not a substitute for including a matter in the Key Audit Matters section ~~in the auditor's report. When a matter has been determined to be a key audit matter, the use of such paragraphs is not a substitute for the description of the individual key audit matter in accordance with paragraph 13.~~<sup>8</sup> ISA 706 (Revised) of the auditor's report if it meets the definition of a key audit matter.

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	<p><a href="#">Proposed AU-C 706</a> provides further guidance on the relationship between key audit matters and <del>Emphasis of Matter</del><a href="#">emphasis-of-matter</a> paragraphs <del>in accordance with that ISA</del><a href="#">and other-matter paragraphs</a>.<sup>94</sup></p>		
<p><del>4.</del> <del>5.</del>—This <del>ISA</del><a href="#">proposed SAS</a> applies to audits of complete sets of general purpose financial statements <del>of listed entities and circumstances</del> when the <a href="#">terms of the engagement include an agreement for the</a> auditor <del>otherwise decides</del> to communicate key audit matters in the auditor’s report. This <a href="#">proposed SAS</a> <del>ISA</del> also applies when the auditor is required by law or regulation to communicate key audit matters in the auditor’s report.<sup>40</sup> However, <del>ISA</del><a href="#">AU-C 705 (Revised)</a> prohibits the auditor from communicating key audit matters when the auditor <a href="#">issues an adverse opinion or</a> disclaims an opinion on the</p>		<p><i>Proposed AS 3105 Departure From Unqualified Opinions and Other Reporting Circumstances</i></p> <p><u>.03 When the auditor expresses a qualified opinion, the auditor's report must include the same basic elements and communication of critical audit matters as would be required in an unqualified auditor's report under AS 3101.</u></p> <p><u>.40 When the auditor expresses an adverse opinion, the auditor's report must include the opinion as described in paragraph .41 and the same other basic elements as would be required</u></p>	<p>AU-C 705 to be amended to prohibit KAM when issuing an adverse opinion or disclaiming an opinion.</p> <p>PCAOB Reproposal includes this guidance in AS 3105 and not 3101.</p>

<sup>7</sup>—ISA 706 (Revised), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*

<sup>8</sup>—See paragraphs 8(b) and 10(b) of ISA 706 (Revised).

<sup>9</sup>—ISA 706 (Revised), paragraphs A1–A3

<sup>4</sup> [Proposed AU-C 706, paragraphs Ax–Ax](#)

<sup>10</sup>—ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraphs 30–31

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<p>financial statements, unless such reporting is required by law or regulation.<sup>445</sup></p>		<p><u>in an unqualified auditor's report under AS 3101, modified appropriately.</u></p> <p><u>Note: The requirements as to critical audit matters described in AS 3101 do not apply when the auditor expresses an adverse opinion.</u></p> <p><u>.46 When the auditor disclaims an opinion, the auditor's report must include the same basic elements as would be required in an unqualified auditor's report under AS 3101, modified appropriately.</u></p> <p><u>Note: The requirements as to critical audit matters described in AS 3101 do not apply when the auditor disclaims an opinion.</u></p>	

<sup>44</sup>—ISA 705 (Revised), paragraph 29

<sup>5</sup> [Proposed AU-C 705, paragraph xx](#)

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<b>Effective Date</b>			
<p><u>5.</u> <del>6.</del>—This <del>ISA</del><u>proposed SAS</u> is effective for audits of financial statements for periods ending on or after December 15, <del>2016</del><u>20xx</u>.</p>			
<b>Objectives</b>		<i>Objectives</i>	
<p><u>6.</u> <del>7.</del>—The objectives of the auditor are to determine key audit matters <del>and, having formed an opinion on the financial statements,</del><u> and</u> communicate those matters by describing them in the auditor’s report.</p>		<p>.04 The objectives of the auditor when the auditor concludes that an unqualified opinion is appropriate are to:</p> <p>a. Issue a written report that expresses an unqualified opinion on the financial statements and describes the basis for that opinion; and</p> <p>b. Communicate in the auditor’s unqualified report <b>critical audit matters</b>,<sup>426</sup> relating to the audit of the financial statements or state that the auditor determined that there are no critical audit matters.</p>	<p>Revised because the task force thought the reference to “having formed an opinion” might be confusing given that KAM will be precluded for an adverse opinion.</p>

<sup>426</sup> Fn215 This term is defined in Appendix A, *Definitions*, and is set in **boldface type** the first time it appears.

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<b>Definition</b>		<b>APPENDIX A – Definition</b>	
<p><del>7.</del> <del>8.</del>—For purposes of <del>the ISAs</del>GAAS, the following term has the meaning attributed below:</p>		A1. For purposes of this standard, the term listed below is defined as follows:	
<p>Key audit matters—Those matters that, in the auditor’s professional judgment, were of most significance in the audit of the financial statements of the current period. Key audit matters are selected from matters communicated with those charged with governance.</p>		<p>A2. Critical audit matter – Any matter arising from the audit of the financial statements that was communicated or required to be communicated to the audit committee and that: (1) relates to accounts or disclosures that are material to the financial statements and (2) involved especially challenging, subjective, or complex auditor judgment.</p> <p>Note: Required audit committee communications are set forth in PCAOB standards, including AS 1301 (currently Auditing Standard No. 16), <i>Communications with Audit Committees</i>, and Appendix B of</p>	

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		that standard which refers to other PCAOB standards.	
<b>Requirements</b>	<b>Determining Key Audit Matters</b> (Ref: Para. 8–9)	<b>Critical Audit Matters</b>	
<b>Determining Key Audit Matters</b>		<i>Determination of Critical Audit Matters</i>	
<p><u>8.</u> <del>9.</del>—The auditor <del>shall</del><u>should</u> determine, from the matters communicated with those charged with governance, those matters that required significant auditor attention in performing the audit. In making this determination, the auditor <del>shall</del><u>should</u> take into account the following: (Ref: <del>Para</del><u>Par.</u> <del>A87</del><u>A17</u><del>16</del>)</p>	<p><u>A7.</u> <del>A9.</del>—The auditor’s decision-making process in determining key audit matters is designed to select a smaller number of matters from the matters communicated with those charged with governance, based on the auditor’s judgment about which matters were of most significance in the audit of the financial statements of the current period.</p>	<p>.11 The auditor must determine whether there are any critical audit matters in the audit of the current period’s financial statements. A critical audit matter is any matter arising from the audit of the financial statements that was communicated or required to be communicated to the audit committee and that:</p>	
	<p><u>A8.</u> <del>A10.</del>—The auditor’s determination of key audit matters is limited to those matters of most significance in the audit of the financial statements of the current period, even when comparative financial statements are presented (i.e., even when the auditor’s opinion refers to each period for which financial statements are presented).<sup>43</sup></p>		
	<p><u>A9.</u> <del>A11. Notwithstanding that the auditor’s determination of key audit matters is for the audit of the financial statements of the current period and this ISA</del><u>This proposed SAS</u> does not require</p>		Revised to make the paragraph clearer.

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	the auditor to update key audit matters included in the prior period's auditor's report. <u>However</u> , it may nevertheless be useful for the auditor to consider whether a matter that was a key audit matter in the audit of the financial statements of the prior period continues to be a key audit matter in the audit of the financial statements of the current period.		
	<i>Matters that Required Significant Auditor Attention (Ref: Para. 8)</i>		
	<del>A10, A12.</del> The concept of significant auditor attention recognizes that an audit is risk-based and focuses on identifying and assessing the risks of material misstatement of the financial statements, designing and performing audit procedures responsive to those risks, and obtaining audit evidence that is sufficient and appropriate to provide a basis for the auditor's opinion. For a particular account balance, class of transactions or disclosure, the higher an assessed risk of material misstatement at the assertion level, the more judgment is often involved in planning and performing the audit procedures and evaluating the results thereof. In designing further audit procedures, the auditor is required to obtain more persuasive audit evidence the higher the auditor's assessment of risk. <sup>14Z</sup> <del>When obtaining more persuasive audit evidence because of a higher assessment of risk, the auditor may increase the quantity of the evidence, or obtain evidence that is more relevant or reliable, for example, by placing more</del>		Last sentence deleted because the task force believes it is not needed in the context of this proposed SAS.

<sup>14Z</sup> ISA AU-C 330, *The Auditor's Responses to Assessed Risks*, paragraph 7(b)

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	<p><del>emphasis on obtaining third party evidence or by obtaining corroborating evidence from a number of independent sources.<sup>45</sup></del></p>		
	<p><del>A11. A13.</del>—Accordingly, matters that pose challenges to the auditor in obtaining sufficient appropriate audit evidence or pose challenges to the auditor in forming an opinion on the financial statements may be particularly relevant in the auditor’s determination of key audit matters.</p> <p><del>A12. A14.</del>—Areas of significant auditor attention often relate to areas of complexity and significant management judgment in the financial statements, and therefore often involve difficult or complex auditor judgments. In turn, this often affects the auditor’s overall audit strategy, the allocation of resources and extent of audit effort in relation to such matters. These effects may include, for example, the extent of involvement of senior personnel on the audit engagement or the involvement of an auditor’s expert or individuals with expertise in a specialized area of accounting or auditing, whether engaged or employed by the firm to address these areas.</p>		
	<p><del>A13. A15.</del>—Various <del>ISAs</del><u>AU-C sections</u> require specific communications with those charged with governance and others that may relate to areas of significant auditor attention. For example:</p>		

<sup>45</sup>—ISA 330, paragraph A19

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	<ul style="list-style-type: none"> <li>• <del>ISA</del><a href="#">AU-C</a> 260—(Revised) requires the auditor to communicate significant difficulties, if any, encountered during the audit with those charged with governance.<sup>168</sup> <del>The ISAs acknowledge potential difficulties in relation to, for example:</del> <ul style="list-style-type: none"> <li>○ <del>Related party transactions,<sup>17</sup> in particular limitations on the auditor’s ability to obtain audit evidence that all other aspects of a related party transaction (other than price) are equivalent to those of a similar arm’s length transaction.</del></li> <li>○ <del>Limitations on the group audit, for example, where the group engagement team’s access to information may have been restricted.<sup>18</sup></del></li> </ul> </li> </ul>		Task force believes the first example is not needed.
	<ul style="list-style-type: none"> <li>• <del>ISA</del><a href="#">AU-C</a> 220 establishes requirements for the engagement partner in relation to undertaking appropriate consultation on difficult or contentious matters.<sup>199</sup> For example, the auditor may have consulted with others within the firm or outside the firm on a significant technical matter, which may be an indicator that it is a key audit matter. The engagement partner is also required to discuss, among</li> </ul>		

<sup>168</sup> ~~ISA~~[AU-C](#) 260 (Revised), paragraphs ~~16~~[14](#)(b) and ~~A2~~[13](#)~~2~~

<sup>17</sup> ~~ISA~~ 550, *Related Parties*, paragraph ~~A~~[4](#)~~2~~

<sup>18</sup> ~~ISA~~ 600, *Special Considerations—Audits of Group Financial Statements (Including the Work of Component Auditors)*, paragraph ~~4~~[9](#)(d)

<sup>199</sup> ~~ISA~~[AU-C](#) 220, *Quality Control for an Audit of Financial Statements*, paragraph ~~18~~[20](#)

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	other things, significant matters arising during the audit engagement with the engagement quality control reviewer. <sup>2010</sup>		
	<i>Considerations in Determining Those Matters that Required Significant Auditor Attention</i> (Ref: <a href="#">p</a> Para. 8)		
	<del>A14, A16.</del> The auditor may develop a preliminary view at the planning stage about matters that are likely to be areas of significant auditor attention in the audit and therefore may be key audit matters. The auditor may communicate this with those charged with governance when discussing the planned scope and timing of the audit in accordance with <del>ISA-260 (Revised)</del> . <a href="#">AU-C 260</a> . However, the auditor's determination of key audit matters is based on the results of the audit or evidence obtained throughout the audit.		
	<del>A15, A17.</del> Paragraph 8 includes specific required considerations in the auditor's determination of those matters that required significant auditor attention. <del>These considerations focus on the nature of matters communicated with those charged with governance that are often linked to matters disclosed in the financial statements, and are intended to reflect areas of the audit of the financial statements that may be of particular interest to intended users. The fact that these considerations are required is not intended to imply that matters related to them are always key</del>		

<sup>20</sup> ~~ISA 220, paragraph 19~~

<sup>10</sup> [AU-C 220, paragraph 21](#)

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	<p><del>audit matters; rather, matters related to such specific considerations are key audit matters only if they are determined to be of most significance in the audit in accordance with paragraph 10.</del> As the considerations may be interrelated (e.g., matters relating to the circumstances described in paragraphs 8(b)-(c) may also be identified as significant risks), the applicability of more than one of the considerations to a particular matter communicated with those charged with governance may increase the likelihood of the auditor identifying that matter as a key audit matter.</p>		
	<p><del>A16. A18.</del> In addition to matters that relate to the specific required considerations in paragraph <del>9.8.</del> there may be other matters communicated with those charged with governance that required significant auditor attention and that therefore may be determined to be key audit matters in accordance with paragraph 9. Such matters may include, for example, matters relevant to the audit that was performed that may not be required to be disclosed in the financial statements. For example, the implementation of a new IT system (or significant changes to an existing IT system) during the period may be an area of significant auditor attention, in particular if such a change had a significant effect on the auditor's overall audit strategy or related to a significant risk (e.g., changes to a system affecting revenue recognition).</p>		

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<p>(a) <del>reas</del>Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with <del>ISA 315 (Revised)</del>.<sup>24</sup> AU-C 315.<sup>11</sup> (Ref: <del>Parapar</del>. A18<del>17</del>-A24<del>20</del>)</p>	<p>Areas of Higher Assessed Risk of Material Misstatement, or Significant Risks Identified in Accordance with <del>ISA</del>AU-C 315 (<del>Revised</del>) (Ref: <del>Parapar</del>. 8(a))</p> <p><del>A17. A19. ISA</del>Proposed AU-C 260 (<del>Revised</del>) requires the auditor to communicate with those charged with governance about the significant risks identified by the auditor.<sup>22</sup><del>12</del> Paragraph A13<del>.XX</del> of <del>ISA</del>proposed AU-C 260 (<del>Revised</del>) explains that the auditor may also communicate with those charged with governance about <del>how the auditor plans to address</del> areas of higher assessed risks of material misstatement.</p>	<p>(1) relates to accounts or disclosures that are material to the financial statements and</p>	<p>Need to make changes to 260 to align par .A18</p>
	<p><del>A18. A20. ISA</del>AU-C 315 (<del>Revised</del>) defines a significant risk as an identified and assessed risk of material misstatement that, in the auditor's judgment, requires special audit consideration. Areas of significant management judgment and significant unusual transactions may often be identified as significant risks. Significant risks are therefore often areas that require significant auditor attention.</p>		

<sup>24</sup> ~~ISA 315 (Revised), Identifying~~<sup>11</sup> AU-C 315, *Understanding the Entity and Its Environment* and Assessing the Risks of Material Misstatement ~~through Understanding the Entity and Its Environment~~

<sup>22</sup> ~~ISA 260 (Revised)~~,<sup>12</sup> ~~Proposed AU-C 260~~, paragraph ~~15~~<sup>xx</sup>

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	<p><del>A19. A21.</del> However, this may not be the case for all significant risks. For example, <del>ISA</del><u>AU-C</u> 240 presumes that there are risks of fraud in revenue recognition and requires the auditor to treat those assessed risks of material misstatement due to fraud as significant risks.<sup>2313</sup> In addition, <del>ISA</del><u>AU-C</u> 240 indicates that, due to the unpredictable way in which management override of controls could occur, it is a risk of material misstatement due to fraud and thus a significant risk.<sup>2414</sup> Depending on their nature, these risks may not require significant auditor attention, and therefore would not be considered in the auditor's determination of key audit matters in accordance with paragraph <del>40.9.</del></p>		

<sup>23</sup> ~~ISA 240, The Auditor's Responsibilities Relating to~~<sup>13</sup> AU-C 240, Consideration of Fraud in ~~an Audit of a~~ Financial ~~Statements~~Statement Audit, paragraphs 26–27

<sup>2414</sup> ~~ISA~~AU-C 240, paragraph 31

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p><u>A20. A22. ISAAU-C 315 (Revised)</u> explains that the auditor’s assessment of the risks of material misstatement at the assertion level may change during the course of the audit as additional audit evidence is obtained.<sup>2515</sup> Revision to the auditor’s risk assessment and reevaluation of the planned audit procedures with respect to a particular area of the financial statements <del>(i.e., a significant change in the audit approach, for example, if</del><u>may result in an area being determined as one requiring significant auditor attention, particularly when the revision results in a higher assessed risk of material misstatement. For example,</u> the auditor’s risk assessment <del>was</del><u>may have been</u> based on an expectation that certain controls were operating effectively <del>and</del><u>but</u> the <del>auditor has obtained</del> audit evidence <u>obtained may indicate</u> that <del>they</del><u>such controls</u> were not operating effectively throughout the audit period, <del>particularly in an area with higher assessed risk of material misstatement)</del> <u>may result in an area being determined as one requiring significant auditor attention leading to a change in audit strategy and additional audit effort.</u></p>		<p>Moved example to end of paragraph to avoid splitting the flow of the paragraph.</p>

<sup>25</sup>—ISA 315 (Revised),<sup>15</sup> AU-C 315, paragraph 31xx

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
<p>(b) Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty. (Ref: <a href="#">Parapar. A2221–A2322</a>)</p>	<p>Significant Auditor Judgments Relating to Areas in the Financial Statements that Involved Significant Management Judgment, Including Accounting Estimates that Have Been Identified as Having High Estimation Uncertainty (Ref: <a href="#">Parapar. 8(b)</a>)</p> <p><a href="#">A21. A23-ISA</a><a href="#">Proposed AU-C 260 (Revised)</a> requires the auditor to communicate with those charged with governance the auditor’s views about significant qualitative aspects of the entity’s accounting practices, including accounting policies, accounting estimates and financial statement disclosures.<sup>2616</sup> In <del>many cases</del><a href="#">particular</a>, this <del>relates to critical accounting estimates and related disclosures, which are likely to be areas of significant auditor attention, and also may be identified as significant risks</del><a href="#">may include accounting policies that have a significant effect on the financial statements (and significant changes to those policies), especially in circumstances when an entity’s practices are not consistent with others in its industry.</a></p>	<p>(2) involved especially challenging, subjective, or complex auditor judgment.</p>	

<sup>26</sup> ~~ISA 260 (Revised)~~,<sup>16</sup> [Proposed AU-C 260](#), paragraph ~~16(a)~~[exx](#)

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p><del>A22. A24. However, users of the financial statements have highlighted their interest in</del> <u>In many cases, the auditor's communication with those charged with governance relates to critical accounting estimates and related disclosures, which are likely to be areas of significant auditor attention, and may be identified as significant risks. However, some critical</u> accounting estimates <del>that may not be significant risks, even if such estimates</del> have been identified as having high estimation uncertainty <del>in accordance with ISA 540<sup>27</sup> that may have not been determined to be significant risks.</del> Among other things, such estimates are highly dependent on management judgment and are often the most complex areas of the financial statements, and may require the involvement of both a management's expert and an auditor's expert. <del>Users have also highlighted that accounting policies that have a significant effect on the financial statements (and significant changes to those policies) are relevant to their understanding of the financial statements, especially in circumstances where an entity's practices are not consistent with others in its industry.</del></p>		<p>Removed references to users because focus of ISA 701 relates to listed entities – may not be relevant for nonissuers.</p>

<sup>27</sup>—See paragraphs 10–11 of ISA 540, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*.

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<p>(c) The effect on the audit of significant events or transactions that occurred during the period. (Ref: <del>Para</del><u>Par.</u> A2423–A2524)</p>	<p>The Effect on the Audit of Significant Events or Transactions that Occurred during the Period (Ref: <del>Para</del><u>par.</u> 8(c))</p> <p><del>A23. A25.</del>—Events or transactions that had a significant effect on the financial statements or the audit may be areas of significant auditor attention and may be identified as significant risks. For example, the auditor may have had extensive discussions with management and those charged with governance at various stages throughout the audit about the effect on the financial statements of significant transactions with related parties or significant transactions that are outside the normal course of business for the entity or that otherwise appear to be unusual.<sup>2817</sup> Management may have made difficult or complex judgments in relation to recognition, measurement, presentation or disclosure of such transactions, which may have had a significant effect on the auditor’s overall strategy.</p>		
	<p><del>A24. A26.</del>—Significant economic, accounting, regulatory, industry, or other developments that affected management’s assumptions or judgments may also affect the auditor’s overall approach to the audit and result in a matter requiring significant auditor attention.</p>		
<p><del>9. 10.</del>—The auditor <del>shall</del><u>should</u> determine which of the matters determined in accordance with paragraph 8 were of most significance in the audit of the financial statements</p>	<p><i>Matters of Most Significance</i> (Ref: Para. 9)</p> <p><del>7.——Matters that required significant auditor attention also may have resulted in significant interaction with those charged with governance. The nature and extent of communication about such</del></p>	<p>.12 In determining whether a matter involved especially challenging, subjective, or complex auditor judgment, the auditor should take into</p>	

<sup>2817</sup> See paragraphs ~~16(a)xx~~, ~~16(c)xx~~ and ~~A22,xx~~, and ~~Appendix 2, Exhibit X~~, of ~~ISA 260 (Revised)~~, proposed AU-C 260.

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
<p>of the current period and therefore are the key audit matters. (Ref: <del>Parapar.</del> <a href="#">A87</a>–<a href="#">A10,9</a>, <a href="#">A2625</a>–A29)</p>	<p><del>matters with those charged with governance often provides an indication of which matters are of most significance in the audit. For example, the auditor may have had more in-depth, frequent or robust interactions with those charged with governance on more difficult and complex matters, such as the application of significant accounting policies that were the subject of significant auditor or management judgment.</del></p>	<p>account, alone or in combination, the following factors, as well as other factors specific to the audit:</p> <p>a. The auditor's assessment of the risks of material misstatement, including significant risks;</p> <p>b. The degree of auditor subjectivity in determining or applying audit procedures to address the matter or in evaluating the results of those procedures;</p> <p>c. The nature and extent of audit effort required to address the matter, including the extent of specialized skill or knowledge needed or the nature of consultations outside the engagement team regarding the matter;</p> <p>d. The degree of auditor judgment related to areas in the financial statements that</p>	

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
		<p>involved the application of significant judgment or estimation by management, including estimates with significant measurement uncertainty;</p> <p>e. The nature and timing of significant unusual transactions and the extent of audit effort and judgment related to these transactions; and</p> <p>f. The nature of audit evidence obtained regarding the matter.</p> <p>Note: It is expected that, in most audits, the auditor would determine that at least one matter involved especially challenging, subjective, or complex auditor judgment.</p>	
	<p><del><a href="#">A25. Matters of Most Significance (Ref: Para. 9)</a></del><a href="#">The concept of matters of most significance is applicable in the context of the entity and the audit that was performed. As such, the intent is for</a></p>		

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p><a href="#">the auditor to identify matters specific to the audit and to make a judgment about their importance relative to other matters in the audit.</a></p> <p><del>A26. A28.</del> Matters that required significant auditor attention also may have resulted in significant interaction with those charged with governance. The nature and extent of communication about such matters with those charged with governance often provides an indication of which matters are of most significance in the audit. For example, the auditor may have had more in-depth, frequent or robust interactions with those charged with governance on more difficult and complex matters, such as the application of significant accounting policies that were the subject of significant auditor or management judgment.</p>		
	<p><del>A27. A29.</del>—Other considerations that may be relevant to determining the relative significance of a matter communicated with those charged with governance and whether such a matter is a key audit matter include:</p> <ul style="list-style-type: none"> <li>• The importance of the matter to intended users’ understanding of the financial statements as a whole, in particular, its materiality to the financial statements.</li> <li>• The nature of the underlying accounting policy relating to the matter or the complexity or subjectivity involved in management’s selection of an appropriate policy compared to other entities within its industry.</li> <li>• The nature and materiality, quantitatively or qualitatively, of corrected and accumulated uncorrected</li> </ul>		

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p>misstatements due to fraud or error related to the matter, if any.</p> <ul style="list-style-type: none"> <li>• The nature and extent of audit effort needed to address the matter, including: <ul style="list-style-type: none"> <li>○ The extent of specialized skill or knowledge needed to apply audit procedures to address the matter or evaluate the results of those procedures, if any.</li> <li>○ The nature of consultations outside the engagement team regarding the matter.</li> </ul> </li> <li>• The nature and severity of difficulties in applying audit procedures, evaluating the results of those procedures, and obtaining relevant and reliable evidence on which to base the auditor’s opinion, in particular as the auditor’s judgments become more subjective.</li> <li>• The severity of any control deficiencies identified relevant to the matter.</li> <li>• Whether the matter involved a number of separate, but related, auditing considerations. For example, long-term contracts may involve significant auditor attention with respect to revenue recognition, litigation or other contingencies, and may have an effect on other accounting estimates</li> </ul>		
	<p><del>A28. A30.</del> Determining which, and how many, of those matters that required significant auditor attention were of most</p>		

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p>significance in the audit of the financial statements of the current period is a matter of professional judgment. The number of key audit matters to be included in the auditor’s report may be affected by the size and complexity of the entity, the nature of its business and environment, and the facts and circumstances of the audit engagement. In general, the greater the number of matters initially determined to be key audit matters, the more the auditor may need to reconsider whether each of these matters meets the definition of a key audit matter. Lengthy lists of key audit matters may be contrary to the notion of such matters being those of most significance in the audit.</p> <p><a href="#">A29. Paragraph 15 addresses the form and content of the key audit matters section of the auditor’s report when the auditor determines that there are no key audit matters to be communicated.</a></p>		
<b>Communicating Key Audit Matters</b>	<b>Communicating Key Audit Matters</b>	<i>Communication of Critical Audit Matters</i>	
<p><a href="#">10.</a> <del>11.</del>—The auditor <del>shall</del><a href="#">should</a> describe each key audit matter, using an appropriate subheading, in a separate section of the auditor’s report under the heading “Key Audit</p>		<p>.13 The auditor must communicate in the auditor’s report critical audit matters<sup><a href="#">2918</a></sup> relating to the audit of the current period’s financial</p>	

<sup>2918</sup> Fn228 Critical audit matters are not a substitute for required explanatory language (paragraphs) described in paragraph .18. If a matter that meets the definition of a critical audit matter also requires an explanatory paragraph, such as a matter related to going concern, the auditor may include the information required under paragraph .14 in the explanatory paragraph with a ~~crossreference~~[cross-reference](#) in the critical audit matters section of the auditor’s report to the explanatory paragraph. Alternatively, the auditor may include the explanatory paragraph and critical audit matter communication separately in the auditor’s report and add a cross-reference between the two sections.

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
<p>Matters,” unless the circumstances in paragraphs 13 or 14 apply. The introductory language in this section of the auditor’s report <del>shall</del><u>should</u> state that:</p>		<p>statements or state that the auditor determined that there are no critical audit matters.  Note: When the current period’s financial statements are presented on a comparative basis with those of one or more prior periods, the auditor may communicate critical audit matters relating to a prior period when (1) the prior period’s financial statements are made public for the first time, such as in an initial public offering, or (2) issuing an auditor’s report on the prior period’s financial statements because the previously issued auditor’s report could no longer be relied upon.</p> <p><u>(A11 in ISA)</u>  <i>Language Preceding Critical Audit Matters in the Auditor’s Report</i></p> <p>.15 The following language, including the section title “Critical Audit Matters,” should precede critical audit matters</p>	

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
		communicated in the auditor's report:	
<p>(a) Key audit matters are those matters that <u>were communicated with those charged with governance and</u>, in the auditor's professional judgment, were of most significance in the audit of the financial statements [of the current period]; and</p> <p>(b) These matters were addressed in the context of the audit of the financial statements as a whole, and in forming the auditor's opinion thereon, and the auditor does not provide a separate opinion on these matters. (Ref: <del>Para</del><u>Par.</u> A30–A32)</p>	<p><i>Separate Key Audit Matters Section in the Auditor's Report</i> (Ref: Para. 10)</p> <p><del>A30. A31.</del>Placing the separate Key Audit Matters section in close proximity to the <del>auditor's opinion</del><u>Opinion and Basis for Opinion sections</u> may give prominence to such information—<del>and acknowledge the perceived value of engagement-specific information to intended users.</del></p>	<p>Critical Audit Matters</p> <p>The critical audit matters communicated below are matters arising from the current period audit that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. Critical audit matters do not alter in any way our opinion on the financial statements, taken as a whole, and we do not provide separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.</p> <p>Note: If the auditor communicates critical audit matters for prior periods, the</p>	

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
		language preceding the critical audit matters should be modified to indicate the periods to which the critical audit matters relate.	
	<a href="#">A31.</a> <del>A32.</del> —The order of presentation of individual matters within the Key Audit Matters section is a matter of professional judgment. For example, such information may be organized in order of relative importance, based on the auditor’s judgment, or may correspond to the manner in which matters are disclosed in the financial statements. The requirement in paragraph 10 to include subheadings is intended to further differentiate the matters.		
	<a href="#">A32.</a> <del>A33.</del> —When comparative financial information is presented, the introductory language of the Key Audit Matters section is tailored to draw attention to the fact that the key audit matters described relate to only the audit of the financial statements of the current period, and may include reference to the specific period covered by those financial statements ( <del>e.g. for example</del> , “for the year ended December 31, 20X1”).		
<i>Key Audit Matters Not a Substitute for Expressing a Modified Opinion</i>			
<a href="#">11.</a> <del>12.</del> —The auditor <del>shall</del> <a href="#">should</a> not communicate a matter in the Key Audit Matters section of the auditor’s		11. ... Critical audit matters are not a substitute for the auditor's departure from an unqualified	

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
report when the auditor would be required to modify the opinion in accordance with <del>ISA</del> <a href="#">proposed AU-C 705 (Revised)</a> as a result of the matter. (Ref: <del>Parapar.</del> A4)		opinion (i.e., a qualified opinion, adverse opinion, or disclaimer of opinion on the financial statements as described in AS 3105).	
<i>Descriptions of Individual Key Audit Matters</i>			
<del>12.</del> <del>13.</del> —The description of each key audit matter in the Key Audit Matters section of the auditor’s report <del>shall</del> <a href="#">should</a> include a reference to the related disclosure(s), if any, in the financial statements and <del>shall</del> <a href="#">should</a> address: (Ref: <del>Parapar.</del> A33–A40 <del>39</del> )	<i>Descriptions of Individual Key Audit Matters</i> (Ref: <del>Parapar.</del> 12) <del>A33. A34.</del> —The adequacy of the description of a key audit matter is a matter of professional judgment. The description of a key audit matter is intended to <del>provide a succinct and balanced explanation to enable intended</del> users to understand why the matter was one of most significance in the audit and how the matter was addressed in the audit. Limiting the use of highly technical auditing terms also helps to enable intended users who do not have a reasonable knowledge of auditing to understand the basis for the auditor’s focus on particular matters during the audit. <del>The nature and extent of information provided by the auditor is intended to be balanced in the context of the responsibilities of the respective parties (i.e., for the auditor to provide useful information in a concise and understandable form, while not inappropriately being the provider of original information about the entity).</del>	.14 For each critical audit matter communicated in the auditor's report the auditor must: a. Identify the critical audit matter;  d. Refer to the relevant financial statement accounts and disclosures that relate to the critical audit matter.	
	<del>A34. A35.</del> — <a href="#">It is important for the auditor to seek to avoid inappropriately providing original information about the entity when describing a key audit matter.</a> Original information is any		

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p>information about the entity that has not <del>otherwise been made publicly available by the entity (e.g., has not been included</del><u>been disclosed</u> in the financial statements or <del>other information available at the date of the auditor's report, or addressed in other oral or written communications by management or those charged with governance, such as a preliminary announcement of financial information or investor briefings)</del><u>is not otherwise publicly available</u>. Such information is the responsibility of the entity's management and those charged with governance. <u>The description of a key audit matter is not usually of itself original information about the entity, as it describes the matter in the context of the audit.</u></p>		
	<p><del>A36. It is appropriate for the auditor to seek to avoid the description of a key audit matter inappropriately providing original information about the entity. The description of a key audit matter is not usually of itself original information about the entity, as it describes the matter in the context of the audit. However, the auditor may consider it necessary to include additional information to explain why the matter was considered to be one of most significance in the audit and therefore determined to be a key audit matter, and how the matter was addressed in the audit, provided that disclosure of such information is not precluded by law or regulation. When such information is determined to be necessary by the auditor, the auditor may encourage management or those charged with governance to disclose additional information, rather than the auditor providing original information in the auditor's report.</del></p>		

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p><a href="#">A35.</a> <del>A37.</del> Management or those charged with governance may decide to include new or enhanced disclosures in the financial statements or elsewhere in the annual report relating to a key audit matter in light of the fact that the matter will be communicated in the auditor’s report. Such new or enhanced disclosures, for example, may be included to provide more robust information about the sensitivity of key assumptions used in accounting estimates or the entity’s rationale for a particular accounting practice or policy when acceptable alternatives exist under the applicable financial reporting framework. <u><a href="#">Additional disclosures by management also may be helpful when the auditor considers it necessary to include additional information to explain why a matter was determined to be a key audit matter, and how the matter was addressed in the audit.</a></u></p>		
	<p><a href="#">A36.</a> <del>A38.</del> Although the auditor’s opinion on the financial statements does not extend to the other information addressed by <del>ISA-720<sup>30</sup></del> <u><a href="#">AU-C 720, Other Information in Documents Containing Audited Financial Statements</a></u> the auditor may consider this information, as well as other publicly available communications by the entity or other credible sources, in formulating the description of a key audit matter.</p>		
	<p><a href="#">A37.</a> <del>A39.</del> Audit documentation prepared during the audit can also be useful to the auditor in formulating the description of a key audit matter. For example, written communications, or the auditor’s documentation of oral communications, with those charged with governance and other audit documentation provides a useful basis for the auditor’s communication in the auditor’s</p>		

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p>report. This is because audit documentation in accordance with <del>ISA</del><a href="#">proposed AU-C</a> 230 is intended to address the significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions, and serves as a record of the nature, timing and extent of the audit procedures performed, the results of those procedures, and the audit evidence obtained. Such documentation may assist the auditor in developing a description of key audit matters that explains the significance of the matter and also in applying the requirement in paragraph 17.</p>		
	<p>Reference to Where the Matter Is Disclosed in the Financial Statements (Ref: Para. 12)</p> <p><del>A38. A40.</del> Paragraphs 12(a)-(b) requires the description of each key audit matter to address why the auditor considered the matter to be one of most significance in the audit and how the matter was addressed in the audit. Accordingly, the description of key audit matters is not a mere reiteration of what is disclosed in the financial statements. However, a reference to any related disclosures enables intended users to further understand how management has addressed the matter in preparing the financial statements.</p>		
	<p><del>A39. A41.</del> In addition to referring to related disclosure(s), the auditor may draw attention to key aspects of them. The extent of disclosure by management about specific aspects or factors in relation to how a particular matter is affecting the financial statements of the current period may help the auditor in pinpointing particular aspects of how the matter was addressed in</p>		

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	the audit such that intended users can understand why the matter is a key audit matter. For example:		
	<ul style="list-style-type: none"> <li>When an entity includes robust disclosure about accounting estimates, the auditor may draw attention to the disclosure of key assumptions, the disclosure of the range of possible outcomes, and other qualitative and quantitative disclosures relating to key sources of estimation uncertainty or critical accounting estimates, as part of addressing why the matter was one of most significance in the audit and how the matter was addressed in the audit.</li> </ul>		
	<ul style="list-style-type: none"> <li>When the auditor concludes in accordance with <del>ISA</del><a href="#">AU-C 570 (Revised)</a> <del>that no material uncertainty exists relating to events or conditions that may cast significant doubt on that substantial doubt about</del> the entity's ability to continue as a going concern <del>for a reasonable period of time has been alleviated by management's plans</del>, the auditor may nevertheless determine that one or more matters relating to this conclusion arising from the auditor's work effort under <del>ISA</del><a href="#">AU-C 570 (Revised)</a> are key audit matters. In such circumstances, the auditor's description of such key audit matters in the auditor's report could include aspects of the identified events or conditions disclosed in the financial statements, such as substantial operating losses, available borrowing facilities and possible debt</li> </ul>		Task force to consider GC wording

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	refinancing, or non-compliance with loan agreements, and related mitigating factors. <sup>3419</sup>		
(a) Why the matter was considered to be one of most significance in the audit and therefore determined to be a key audit matter; and (Ref: <del>Para</del> <u>Par.</u> <del>A4140–A4442</del> )	Why the Auditor Considered the Matter to Be One of Most Significance in the Audit (Ref: <del>Para</del> <u>par.</u> 12(a))  <del>A40. A42.</del> The description of a key audit matter in the auditor’s report is intended to provide insight as to why the matter was determined to be a key audit matter. Accordingly, the requirements in paragraphs 8–9 and the application material in paragraphs <del>A4110–A2827</del> related to determining key audit matters may also be helpful for the auditor in considering how such matters are to be communicated in the auditor’s report. For example, explaining the factors that led the auditor to conclude that a particular matter required significant auditor attention and was of most significance in the audit is likely to be of interest to intended users.	b. Describe the principal considerations that led the auditor to determine that the matter is a critical audit matter;	
	<del>A43. The relevance of the information for intended users is a consideration for the auditor in determining what to include in the description of a key audit matter. This may include whether the description would enable a better understanding of the audit and the auditor’s judgments.</del>		
	<del>A41. A44.</del> Relating a matter directly to the specific circumstances of the entity may also help to minimize the potential that such		

<sup>34</sup>—See paragraph A3 of ISA 570 (Revised).

<sup>19</sup> See paragraph XX of proposed AU-C 570.

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p>descriptions become overly standardized and less useful over time. For example, certain matters may be determined as key audit matters in a particular industry across a number of entities due to the circumstances of the industry or the underlying complexity in financial reporting. In describing why the auditor considered the matter to be one of most significance, it may be useful for the auditor to highlight aspects specific to the entity (e.g., circumstances that affected the underlying judgments made in the financial statements of the current period) in order to make the description more relevant for intended users. This also may be important in describing a key audit matter that recurs over periods.</p>		
	<p><del>A42. A45.</del>—The description may also make reference to the principal considerations that led the auditor, in the circumstances of the audit, to determine the matter to be one of most significance, for example:</p>		
	<ul style="list-style-type: none"> <li>• Economic conditions that affected the auditor’s ability to obtain audit evidence, for example illiquid markets for certain financial instruments.</li> </ul>		
	<ul style="list-style-type: none"> <li>• New or emerging accounting policies, for example entity-specific or industry-specific matters on which the engagement team consulted <del>within the firm.</del></li> </ul>		
	<ul style="list-style-type: none"> <li>• Changes in the entity’s strategy or business model that had a material effect on the financial statements.</li> </ul>		

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
<p>(b) How the matter was addressed in the audit. (Ref: <del>Parapar.</del> <del>A4543</del>–<del>A5048</del>)</p>	<p>How the Matter Was Addressed in the Audit (Ref: <del>Parapar.</del> 12(b)) <del>A43. A46.</del>The amount of detail to be provided in the auditor’s report to describe how a key audit matter was addressed in the audit is a matter of professional judgment. In accordance with paragraph <del>4312</del>(b), the auditor may describe:</p> <ul style="list-style-type: none"> <li>• Aspects of the auditor’s response or approach that were most relevant to the matter or specific to the assessed risk of material misstatement;</li> <li>• A brief overview of procedures performed;</li> <li>• An indication of the outcome of the auditor’s procedures; or</li> <li>• Key observations with respect to the matter,</li> </ul> <p>or some combination of these elements.</p> <p>Law or regulation <del>or national auditing standards</del> may prescribe a specific form or content for the description of a key audit matter, or may specify the inclusion of one or more of these elements.</p>	<p>c. Describe how the critical audit matter was addressed in the audit; and</p>	
		<p>Note 1: Language that could be viewed as disclaiming, qualifying, restricting, or minimizing the auditor’s responsibility for the critical audit matters or the auditor’s opinion on the financial</p>	

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
		<p>statements is not appropriate and may not be used. The language used to communicate a critical audit matter should not imply that the auditor is providing a separate opinion on the critical audit matter or on the accounts or disclosures to which they relate.</p> <p>Note 2: When describing critical audit matters in the auditor's report the auditor is not expected to provide information about the company that has not been made publicly available by the company unless such information is necessary to describe the principal considerations that led the auditor to determine that a matter is a critical audit matter or how the matter was addressed in the audit.</p>	
	<p><del>A44. A47.</del>—In order for intended users to understand the significance of a key audit matter in the context of the audit of the financial statements as a whole, as well as the relationship between key audit matters and other elements of the auditor's</p>		

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p>report, including the auditor’s opinion, care may be necessary so that language used in the description of a key audit matter:</p> <ul style="list-style-type: none"> <li>• Does not imply that the matter has not been appropriately resolved by the auditor in forming the opinion on the financial statements.</li> <li>• Relates the matter directly to the specific circumstances of the entity, while avoiding generic or standardized language.</li> <li>• Takes into account how the matter is addressed in the related disclosure(s) in the financial statements, if any.</li> <li>• Does not contain or imply discrete opinions on separate elements of the financial statements.</li> </ul>		
	<p><del>A45. A48.</del> Describing aspects of the auditor’s response or approach to a matter, in particular when the audit approach required significant tailoring to the facts and circumstances of the entity, may assist intended users in understanding unusual circumstances and significant auditor judgment required to address the risk of material misstatement. In addition, the audit approach in a particular period may have been influenced by entity-specific circumstances, economic conditions, or industry developments. It may also be useful for the auditor to make reference to the nature and extent of communications with those charged with governance about the matter.</p>		

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p><del>A46. A49.</del> For example, in describing the auditor’s approach to an accounting estimate that has been identified as having high estimation uncertainty, such as the valuation of complex financial instruments, the auditor may wish to highlight that the auditor employed or engaged an auditor’s expert. Such a reference to the use of an auditor’s expert does not reduce the auditor’s responsibility for the opinion on the financial statements and is therefore not inconsistent with paragraphs 14–15 of <del>ISA</del><a href="#">AU-C 620</a> <i>Using the Work of an Auditor’s</i> <del>620.</del><sup>32</sup> <i>Specialist</i>.</p>		
	<p><del>A47. A50.</del> There may be challenges in describing the auditor’s procedures, particularly in complex, judgmental areas of the audit. In particular, it may be difficult to summarize the procedures performed in a succinct way that adequately communicates the nature and extent of the auditor’s response to the assessed risk of material misstatement, and the significant auditor judgments involved. Nonetheless, the auditor may consider it necessary to describe certain procedures <u>that were</u> performed to <del>communicate</del><u>explain</u> how the matter was addressed in the audit. Such description may typically be at a high level <u>(i.e., those procedures that are most relevant to the unique facts and circumstances of the entity and the current-period audit)</u>, rather than <del>include</del> a detailed description of <u>all</u> procedures <u>performed regarding the matter</u>.</p>		

<sup>32</sup>—ISA 620, *Using the Work of an Auditor’s Expert*

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p><del>A48. A51.</del>As noted in paragraph <del>A45, 43.</del> the auditor may also provide an indication of the outcome of the auditor’s response in the description of the key audit matter in the auditor’s report. However, if this is done, care is needed to avoid the auditor giving the impression that the description is conveying a separate opinion on an individual key audit matter or that in any way may call into question the auditor’s opinion on the financial statements as a whole.</p>		
<p><i>Circumstances in Which a Matter Determined to Be a Key Audit Matter Is Not Communicated in the Auditor’s Report</i></p>	<p><i>Circumstances in Which a Matter Determined to Be a Key Audit Matter Is Not Communicated in the Auditor’s Report</i> (Ref: <del>Parapar.</del> 13)</p>		<p>PCAOB does not have requirement for sensitivity</p>
<p><del>13. 14.</del>The auditor <del>shall</del><u>should</u> describe each key audit matter in the auditor’s report unless: (Ref: <del>Para. A52–A55</del>)</p>			
<p>(a) Law or regulation precludes <del>public</del> disclosure about the matter; or (Ref: <del>Parapar.</del> <u>A5149</u>)</p>	<p><del>A49. A52. A52.</del>Law or regulation may preclude <del>public</del> disclosure by either management or the auditor about a specific matter determined to be a key audit matter. <del>For example, law or regulation may specifically prohibit any public communication that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act (e.g., matters that are or appear to be related to money laundering).</del></p>		
<p>(b) In extremely rare circumstances, the auditor</p>	<p><del>A50. A53.</del>As indicated by paragraph 13(b), it will be extremely rare for a matter determined to be a key audit matter not to be</p>		

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
<p>determines that the matter should not be communicated in the auditor’s report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication. This <del>shall</del><u>should</u> not apply if <del>the entity has publicly disclosed</del> information about the matter <u>is available outside the entity</u>.  (Ref. par. A50–A53)</p>	<p>communicated in the auditor’s report. This is because there is presumed to be a public interest benefit in providing greater transparency about the audit for intended users. Accordingly, the judgment not to communicate a key audit matter is appropriate only in cases when the adverse consequences to the entity or the public as a result of such communication are viewed as so significant that they would reasonably be expected to outweigh the public interest benefits of communicating about the matter.</p>		
	<p><del>A51. A54.</del>–The determination not to communicate a key audit matter takes into account the facts and circumstances related to the matter. Communication with management and those charged with governance helps the auditor understand management’s views about the significance of the adverse consequences that may arise as a result of communicating about a matter. In particular, communication with management and those charged with governance helps to inform the auditor’s judgment in determining whether to communicate the matter by:</p>		

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<ul style="list-style-type: none"> <li>Assisting the auditor in understanding why the matter has not been publicly disclosed by the entity (e.g. for example, if law, regulation or certain financial reporting frameworks permit delayed disclosure or non-disclosure of the matter) and management's views as to the adverse consequences, if any, of disclosure. Management may draw attention to certain aspects in law or regulation or other authoritative sources that may be relevant to the consideration of adverse consequences (e.g. for example, such aspects may include harm to the entity's commercial negotiations or competitive position). However, management's views about the adverse consequences alone do not alleviate the need for the auditor to determine whether the adverse consequences would reasonably be expected to outweigh the public interest benefits of communication in accordance with paragraph 13(b).</li> </ul>		
	<ul style="list-style-type: none"> <li>Highlighting whether there have been any communications with applicable regulatory, enforcement or supervisory authorities in relation to the matter, in particular whether such discussions would appear to support management's assertion as to why public disclosure about the matter is not appropriate.</li> </ul>		

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<ul style="list-style-type: none"> <li>Enabling the auditor, <del>where</del><u>when</u> appropriate, to encourage management and those charged with governance to <del>make public disclosure of</del><u>disclose</u> relevant information about the matter. In particular, this may be possible if the concerns of management and those charged with governance about communicating are limited to specific aspects relating to the matter, such that certain information about the matter may be less sensitive and could be communicated.</li> </ul> <p>The auditor also may consider it necessary to obtain a written representation from management as to why <del>public</del>-disclosure about the matter is not appropriate, including management’s view about the significance of the adverse consequences that may arise as a result of such communication.</p>		
	<p><u>A52.</u> <del>A55.</del> It may also be necessary for the auditor to consider the implications of communicating about a matter determined to be a key audit matter in light of relevant ethical requirements. In addition, the auditor may be required by law or regulation to communicate with applicable regulatory, enforcement or supervisory authorities in relation to the matter, regardless of whether the matter is communicated in the auditor’s report. Such communication may also be useful to inform the auditor’s consideration of the adverse consequences that may arise from communicating about the matter.</p>		

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p><del>A53. A56.</del>—The issues considered by the auditor regarding a decision to not communicate a matter are complex and involve significant auditor judgment. Accordingly, the auditor may consider it appropriate to obtain legal advice.</p>		
<p><i>Interaction between Descriptions of Key Audit Matters and Other Elements Required to Be Included in the Auditor’s Report</i></p>			
<p><del>14.</del> <del>15.</del>—A matter giving rise to a modified opinion in accordance with <del>ISA 705 (Revised), or a material uncertainty related to events or conditions that may cast significant doubt on the</del><u>AU-C 705, or when substantial doubt exists about an</u> entity’s ability to continue as a going concern <u>for a reasonable period of time</u> in accordance with <del>ISA 570 (Revised), AU-C 570,</del> are by their nature key audit matters. However, in such circumstances, these matters <del>shall</del><u>should</u> not be described in the Key Audit Matters section of the auditor’s report and the requirements in paragraphs 12–13 do not apply. Rather, the auditor <del>shall</del><u>should</u>:</p>		<p>Fn 228 Critical audit matters are not a substitute for required explanatory language (paragraphs) described in paragraph .18. If a matter that meets the definition of a critical audit matter also requires an explanatory paragraph, such as a matter related to going concern, the auditor may include the information required under paragraph .14 in the explanatory paragraph with a crossreference in the critical audit matters section of the auditor’s report to the explanatory paragraph. Alternatively, the auditor may</p>	<p>GC – need to work on wording?</p>

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
		include the explanatory paragraph and critical audit matter communication separately in the auditor's report and add a cross-reference between the two sections	
(a) Report on these matter(s) in accordance with the applicable <del>ISA(s)</del> <a href="#">AU-C sections</a> ; and			
(b) Include a reference to the Basis for Qualified ( <del>Adverse</del> ) Opinion or the <del>Material Uncertainty Related to</del> Going Concern section(s) in the Key Audit Matters section. (Ref: <del>Parapar.</del> <a href="#">A5–A6</a> )			GC – pending outcome of reporting and title of section.
<i>Form and Content of the Key Audit Matters Section in Other Circumstances</i>	<i>Form and Content of the Key Audit Matters Section in Other Circumstances</i> (Ref: <del>Parapar.</del> <a href="#">15</a> )		
<del>15.</del> <del>16.</del> If the auditor determines, depending on the facts and circumstances of the entity and the audit, that there are no key audit matters to communicate or that the only key audit matters communicated are those matters addressed by paragraph 14, the auditor <del>shall</del> <a href="#">should</a>	<del>A54.</del> <del>A57.</del> The requirement in paragraph <del>16</del> <a href="#">15</a> applies in three circumstances: <ul style="list-style-type: none"><li>• <del>(i)</del>—The auditor determines in accordance with paragraph <del>10</del><a href="#">9</a> that there are no key audit matters <del>(see paragraph 0).</del> <a href="#">This may be the case because</a></li></ul>	16 In situations in which the auditor determines that there are no critical audit matters, the auditor should include the following language, including the section title "Critical Audit Matters," in the auditor's report:  Critical Audit Matters	

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
<p>include a statement to this effect in a separate section of the auditor’s report under the heading “Key Audit Matters.” (Ref: <del>Para. A56</del> <u>par. A54</u>)</p>	<p><u>there were no matters that required significant auditor attention.</u></p> <ul style="list-style-type: none"> <li>• <del>(ii)</del>—The auditor determines in accordance with paragraph 13 that a key audit matter will not be communicated in the auditor’s report and no other matters have been determined to be key audit matters.</li> <li>• <del>(iii)</del>—The only matters determined to be key audit matters are those communicated in accordance with paragraph 14.</li> </ul>	<p>Critical audit matters are matters arising from the current period audit that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. We determined that there are no critical audit matters.</p>	

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p><del>A55.</del> <del>A58.</del>—The following illustrates the presentation in the auditor’s report if the auditor has determined there are no key audit matters to communicate:</p> <p><b>Key Audit Matters</b></p> <p>[Except for the matter described in the <i>Basis for Qualified (Adverse) Opinion</i> section or <i>Material Uncertainty Related to Going Concern</i> section,] We have determined that there are no [other] key audit matters to communicate in our report.</p>		
	<p><del>A59. The determination of key audit matters involves making a judgment about the relative importance of matters that required significant auditor attention. Therefore, it may be rare that the auditor of a complete set of general purpose financial statements of a listed entity would not determine at least one key audit matter from the matters communicated with those charged with governance to be communicated in the auditor’s report. However, in certain limited circumstances (e.g., for a listed entity that has very limited operations), the auditor may determine that there are no key audit matters in accordance with paragraph 10 because there are no matters that required significant auditor attention.</del></p>		
<p>Communication with Those Charged with Governance</p>	<p>Communication with Those Charged with Governance (Ref: <del>Parapar.</del> <a href="#">1716</a>)</p>		

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
<p><del>16.</del> <del>17.</del>—The auditor <del>shall</del><u>should</u> communicate with those charged with governance:</p>			
<p>(a) Those matters the auditor has determined to be the key audit matters; or</p>			
<p>(b) If applicable, depending on the facts and circumstances of the entity and the audit, the auditor’s determination that there are no key audit matters to communicate in the auditor’s report. (Ref: <del>Para</del><u>par.</u> <del>A5856</del>–<del>A6459</del>)</p>	<p><del>A56. A60. ISA-260 (Revised) requires the auditor to communicate with those charged with governance on a timely basis.</del><sup>33</sup>—The appropriate timing for communications <u>with those charged with governance</u> about key audit matters will vary with the circumstances of the engagement. However, the auditor may communicate preliminary views about key audit matters when discussing the planned scope and timing of the audit, and may further discuss such matters when communicating about audit findings. Doing so may help to alleviate the practical challenges of attempting to have a robust two-way dialogue about key audit matters at the time the financial statements are being finalized for issuance.</p>		

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p><a href="#">A57</a>. <del>A61</del>—Communication with those charged with governance enables them to be made aware of the key audit matters that the auditor intends to communicate in the auditor’s report, and provides them with an opportunity to obtain further clarification where necessary. The auditor may consider it useful to provide those charged with governance with a draft of the auditor’s report to facilitate this discussion. Communication with those charged with governance recognizes their important role in overseeing the financial reporting process, and provides the opportunity for those charged with governance to understand the basis for the auditor’s decisions in relation to key audit matters and how these matters will be described in the auditor’s report. It also enables those charged with governance to consider whether new or enhanced disclosures may be useful in light of the fact that these matters will be communicated in the auditor’s report.</p>		
	<p><a href="#">A58</a>. <del>A62</del>—The communication with those charged with governance required by paragraph <del>47</del><a href="#">16</a>(a) also addresses the extremely rare circumstances in which a matter determined to be a key audit matter is not communicated in the auditor’s report (see paragraphs <del>44</del><a href="#">13</a> and <del>A54</del><a href="#">51</a>).</p>		

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	<p><del>A59. A63.</del>The requirement in paragraph <del>47</del><u>16</u>(b) to communicate with those charged with governance when the auditor has determined there are no key audit matters to communicate in the auditor’s report may provide an opportunity for the auditor to have further discussion with others who are familiar with the audit and the significant matters that may have arisen (including the engagement quality control reviewer, where one has been appointed). These discussions may cause the auditor to re-evaluate the auditor’s determination that there are no key audit matters.</p>		
<b>Documentation</b>	<b>Documentation</b> (Ref: <del>Para</del> <u>par.</u> <del>48</del> <u>17</u> )	<i>Documentation of Critical Audit Matters</i>	
<p><del>17. 18.</del>The auditor <del>shall</del><u>should</u> include in the audit documentation:<sup>3420</sup> (Ref: <del>Para</del><u>Par.</u> <del>A62</del><u>60</u>)</p>	<p><del>A60. A64.</del>Paragraph 8 of <del>ISA</del><u>AU-C</u> 230 requires the auditor to prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand, among other things, significant professional judgments. In the context of key audit matters, these professional judgments include the determination, from the matters communicated with those charged with governance, of the matters that required significant auditor attention, as well as whether or not each of those matters is a key audit matter. The auditor’s judgments in this regard are likely to be supported by the documentation of the auditor’s communications with those charged with governance and the audit documentation relating to each individual matter (see paragraph <del>A39</del><u>37</u>), as well as certain</p>	<p>.17 The auditor must document the basis for the auditor’s determination whether each matter that both:</p>	

<sup>3420</sup> ISA 230, *Audit Documentation*, paragraphs 8–11 and A6

Proposed Wording for AU-C 701†	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
	<p>other audit documentation of the significant matters arising during the audit (<del>e.g., for example,</del> a completion memorandum). However, this <del>ISA</del><a href="#">proposed SAS</a> does not require the auditor to document why other matters communicated with those charged with governance were not matters that required significant auditor attention.</p>		
<p>(a) The matters that required significant auditor attention as determined in accordance with paragraph 8, and the rationale for the auditor’s determination as to whether or not each of these matters is a key audit matter in accordance with paragraph 9;</p>		<p>a. Was communicated or required to be communicated to the audit committee; and</p> <p>b. Relates to accounts or disclosures that are material to the financial statements involved especially challenging, subjective, or complex auditor judgment.<sup><del>35</del>21</sup></p>	
<p>(b) <del>Where</del><a href="#">When</a> applicable, the rationale for the auditor’s determination that there are no key audit matters to communicate in the auditor’s report or that the only key audit matters to communicate are</p>			

<sup>35</sup> ~~Consistent with the requirements of AS 1215, the audit documentation should be in sufficient detail to enable an experienced auditor, having no previous connection with the engagement, to understand the determinations made to comply with the provisions of this standard.~~

<sup>21</sup> [Consistent with the requirements of AS 1215, the audit documentation should be in sufficient detail to enable an experienced auditor, having no previous connection with the engagement, to understand the determinations made to comply with the provisions of this standard.](#)

Proposed Wording for AU-C 701††	Proposed Wording for AU-C 701† (Application Material)	PCAOB Reproposal	Comments
those matters addressed by paragraph 14; and			
(c) <del>Where</del> <u>When</u> applicable, the rationale for the auditor's determination not to communicate in the auditor's report a matter determined to be a key audit matter.			
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	Count

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Moved to	7
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