

# AUDITING STANDARDS BOARD (ASB)

## Meeting Highlights

July 17-20, 2017

Denver, CO

### MEETING ATTENDANCE

#### ASB Members

Mike Santay, *Chair*

Gerry Boaz

Jay Brodish

Dora Burzenski

Joseph Cascio

Larry Gill

Steve Glover

Gaylen Hansen

Tracy Harding

Dan Hevia

Ilene Kassman

Alan Long

Rich Miller

Dan Montgomery

Steven Morrison

Rick Reisig

Catherine Schweigel

Jere Shawver

Chad Singletary (7/17; 7/20 by phone)

#### Observers and Guests

Denny Ard, *Dixon Hughes (7/18-19 only)*

Sally Ann Bailey, *Deloitte & Touche LLP*

Adam Barrow, *EY LLP*

Jim Dalkin, *GAO*

Karin French (by phone, 7/19)

Bridget Gyofri, *KPMG LLP*

David Haller, *RSM LLP*

Audra Harrington, *PWC LLP (by phone)*

Kathy Healy, *PwC LLP*

Jan Herringer, *BDO*

Susan Jones, *KPMG LLP*

Nigyar Mamedova, *NASBA*

Laura Schuetze, *Grant Thornton (by phone)*

Sara Lord, *RSM LLP*

David Steimel, *EKS&H, LLP (7/17-7/18)*

Mark Wells, *Thompson Reuters*

#### AICPA Staff

Mike Austin, *PCPS Technical Issues Committee*

Amanda Black (by phone)

Linda Delahanty, *Audit & Attest Standards*

Mike Glynn, *A&A Standards*

Ahava Goldman, *A&A Standards*

Hiram Hasty, *A&A Standards*

Kristy Illuzzi, *PCPS Technical Issues Committee*

Teighlor March, *Assistant General Counsel*

Andy Mrakovic, *A&A Standards*

Judith Sherinsky, *A&A Standards*

### Chair's Report

The ASB approved the highlights of its May 2017 meeting. Mr. Santay reported on the recent meeting of the AITF.

The ASB discussed changes to its Operating Policies, including adding an option to abstain and the need for outreach to users of the auditor's report. Revised Operating Policies will be circulated through email for approval.

## **1. Auditor Reporting**

The ASB voted unanimously to ballot for issuance as exposure drafts the following proposed auditor reporting standards:

- Proposed SAS *Forming an Opinion and Reporting on Financial Statements*, to supersede AU-C section 700 of the same title
- Proposed SAS *Modifications to the Opinion in the Independent Auditor's Report*, to supersede AU-C section 705 of the same title
- Proposed SAS *Emphasis-of-Matter Paragraphs and Other-Matter Paragraphs in the Independent Auditor's Report*, to supersede AU-C section 706 of the same title
- Proposed SAS *Communicating Key Audit Matters in the Independent Auditor's Report*, which will create new AU-C section 701 of the same title
- Proposed amendments to various AU-C sections, including AU-C section 260, *The Auditor's Communication With Those Charged With Governance* and SAS No. 132, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*

Mr. Montgomery, chair of the Auditor Reporting Task Force, led the ASB in a discussion of the proposed auditor reporting standards and related documents. The ASB provided the task force with the following feedback:

(Note: paragraph references relate to the July 2017 ASB meeting agenda materials)

### **General Feedback:**

- Include the proposed changes to AU-C section 260, *The Auditor's Communication With Those Charged with Governance* as part of the amendments section of the exposure draft rather than as a separate proposed SAS, and revise all references to that proposed SAS accordingly.
- Remove all changes related to the ASB's disclosures project (See agenda item 3), for purposes of the Auditor Reporting ballot draft, because the ASB will vote to ballot for exposure those changes as part of a teleconference call in September 2017. The paragraphs affected by this change (to remove the disclosures related content) include the following:
  - Proposed SAS *Forming an Opinion and Reporting on Financial Statements*, paragraph 9, 13, 14, 42, A9-A14, and A58-A59

- Proposed SAS *Modifications to the Opinion in the Independent Auditor's Report*, paragraph 23, A3-A4, A7-A8
- Incorporate the disclosures project amendments into the Auditor Reporting exposure draft for the September call, because of the inter-relationship among the amendments, and issue the exposure draft of proposed SAS *The Auditor's Responsibilities Relating to Other Information Included in Annual Reports* (see agenda item 2) at the same time as the exposure draft of the suite of Auditor Reporting standards. Those exposure drafts are expected to be issued in the fall of 2017.
- Include a provisional effective date of no earlier than for audits of financial statements for periods ending on or after June 15, 2019. Because of the relationship among the proposed standards, early implementation would not be permitted.

**Agenda Item 1A - Proposed SAS *Forming an Opinion and Reporting on Financial Statements***

- Paragraph 26(c) — to clarify that the relevant ethical requirements relate to those that are relevant to the audit by revising the requirement to state that the Basis for Opinion section should include a statement that the auditor is independent of the entity, and has fulfilled the auditor's other ethical responsibilities, in accordance with the relevant ethical requirements relating to the audit.
- Paragraph 36(b)(ii) — revise requirement to only remove those words no longer needed.
- Paragraph A2 – revise to clarify that the list of AU-C sections is not all inclusive and add other AU-C sections that contain reporting requirements, such as AU-C 570, AU-C 725, and proposed SAS *The Auditor's Responsibilities Relating to Other Information in Annual Reports*.
- Paragraph A24 — add a footnote to reference to paragraph .A18 of AU-C section 200.
- Paragraph A27 — clarify that the identification of the title for each statement that the financial statements comprise may be achieved by referencing the table of contents in a document when the document is bound with or accompanying the financial statements and auditor's report thereon.
- Paragraph A28 — change “other than” to “in addition to” to better reflect the intent of the sentence. Replace “other information” with “information other than the financial statements and the auditor's report thereon”
- Paragraph A31 — remove the first sentence because the ASB does not believe it is necessary
- Paragraph A38 — add “or Government Auditing Standards as promulgated by the Comptroller General of the United States” to include government considerations
- Paragraph A43 — clarify that a reference to oversight responsibilities is not needed when “all of the individuals” responsible for oversight of the financial reporting process are “also” responsible for the preparation of the financial statements.

- Add a new application material paragraph for the requirement in paragraph 45 to explain that an audit being conducted in accordance with the standards of the PCAOB would include the relevant requirements in the PCAOB standards regarding the determination and reporting of critical audit matters and that this would not affect the requirement for the auditor to state in the auditor's report that the audit was conducted in accordance with GAAS as required by paragraph 45 of the proposed SAS. (Note: The final standards and amendments relating to the new PCAOB reporting model are subject to approval by the Securities and Exchange Commission.)

**Agenda Item 1B - Proposed SAS *Communicating Key Audit Matters in the Independent Auditor's Report***

- Paragraph 1 — clarify that the proposed SAS addresses the auditor's responsibility when the auditor is engaged to communicate key audit matters in the auditor's report.
- Paragraph 3(c) — add "amendment to" before AU-C section 570
- Paragraph 4 — clarify that the proposed SAS applies when the auditor is engaged to communicate key audit matters in the auditor's report
- Paragraph 14 — change "modified" to "qualified"
- Paragraph A1 – remove the last sentence
- Add new application material for paragraph 4 to clarify that the proposed SAS does not require the communication of key audit matters in the auditor's report. However, the auditor may be engaged to communicate key audit matters or may be required by law, regulation, or contractual agreement to do so.
- Paragraph A7 — remove entire paragraph because it is not necessary
- Paragraph A8 — revised to better explain how the auditor determines key audit matters
- Paragraph A9 — add a new first sentence to explain that from the matters that required significant auditor attention, the auditor then determines those matters that, in the auditor's judgment, were of most significance in the audit of the financial statements of the current period, and are therefore are the key audit matters
- Paragraph A14 — change "various" to "certain" and move the examples relating to related party transactions and limitation on the group audit under AU-C section 260 content because these are areas in which there may be potential difficulties.
- Paragraph A23 — revise paragraph to clarify that accounting estimates are often areas of significant auditor attention and may be identified as significant risks
- Paragraph A35 — removed the example
- Paragraph A36 — revise the paragraph to clarify that although the auditor seek seeks to avoid providing original information about the entity, it may be necessary for the auditor to do so, and when the auditor determines it is necessary to do so management may elect to expand or supplement the entity's disclosures rather than have the auditor provide original information in the auditor's report

- Paragraph A51 — change “defense contractor” to “government contractor”
- Paragraph A58 — change “adequate” to “robust”

**Agenda Item 1C - Proposed SAS *Modifications to the Opinion in the Independent Auditor’s Report***

- Paragraph 12 — add “if appropriate” before “determine whether it is possible to perform alternative procedures to obtain sufficient appropriate audit evidence” because it may not always be appropriate to perform alternative procedures
- Paragraph 30 — change “issues an adverse opinion” to “expresses an adverse opinion” and add “when the auditor disclaims an opinion on the financial statements, the auditor’s report should not include an Other Information section in accordance with proposed SAS, *The Auditor’s Responsibilities Relating to Other Information Included in Annual Reports.*”
- Paragraph A9 — move as application material for paragraph 22
- Paragraph A13 — remove “for an associated entity”
- Paragraph A16 — remove “even if the auditor has obtained sufficient appropriate audit evidence about each of the individual uncertainties”
- Paragraph A17 — add “or elected” after “appointed” in the second sentence to address governmental situations
- Paragraph A29 — remove “or segment information”
- Paragraph A36 —
  - change “has expressed an adverse opinion” to “expresses an adverse opinion”
  - change “not relevant to the users because” to “overshadow the fact that”
  - add “Similarly, it would not be appropriate for the auditor to make any statements about the auditor’s consideration of the consistency of other information in an annual report with the financial statements.”
  - add to end of the last sentence “and also prohibits the inclusion of an Other Information section in the auditor’s report when the auditor disclaims an opinion on the financial statements.”

**Agenda Item 1D - Proposed SAS *Emphasis-of-Matter Paragraphs and Other-Matter Paragraphs in the Independent Auditor’s Report***

- Paragraph 2 — revise to clarify that this proposed SAS also addresses the relationship between key audit matters and any additional communication in the auditor’s report
- Add new application material for paragraph 3 to explain when an emphasis-of-matter paragraph may be included in the auditor’s report relating to going concern considerations in accordance with AU-C section 570

- Paragraph 8 — change “and” to “or”
- Paragraph A3 — remove paragraph A3 because it is repetitive with paragraph A2
- Paragraph A7(c) — to clarify that an EOM is not a substitute for reporting in a separate section in the auditor’s report in accordance with proposed amendments to AU-C section 570
- Paragraph A9 — removed “In the rare circumstances” in the first sentence because it is not needed
- Exhibit B — remove bullet relating to paragraphs .15-.16 of AU-C section 570 because there is no required emphasis-of-matter paragraph for going concern but rather a new required section in the auditor’s report.
- Exhibit C — remove bullet relating to paragraph .12 of AU-C section 720 because there is no required other-matter paragraph in AU-C section 720 but rather a separate section in the auditor’s report, when applicable.

**Agenda Item 1E (changed to proposed amendments) AU-C section 260 *The Auditor’s Communication With Those Charged With Governance***

- Paragraph 3 — include “law or regulation or other” before “external requirements” in the penultimate sentence
- Paragraph A21 (4<sup>th</sup> bullet) — add “The auditor may wish to focus more broadly on the factors considered by the auditor when determining materiality for purposes of the audit, rather than specific thresholds or amounts.”
- Paragraph A22 (5<sup>th</sup> bullet) — conform to proposed SAS *The Auditor’s Responsibilities Relating to Other Information Included in Annual Reports*
- Paragraph A30 — remove “for the auditor”
- Paragraph A50 (3<sup>rd</sup> bullet) – align the bullet with ISA wording

**Agenda Item 1F — Proposed Amendments**

The ASB provided the task force with suggested changes to certain of the amendments, including the following:

- **AU-C section 210**

- Paragraph A25 – revise to say the following:

*Although there is no requirement to communicate key audit matters in the auditor’s report, the engagement letter may acknowledge that management has requested the auditor to communicate key audit matters in the auditor’s report. If the terms of the audit engagement initially acknowledge that key audit matters will be communicated, but it is later decided that this will not be done, the engagement letter may need to be modified accordingly. If the auditor is requested to communicate key audit matters in the auditor’s report after the*

*engagement letter is signed, the auditor may acknowledge this agreement in a new engagement letter or as an addendum to the originally signed letter.*

- Revise the example in the illustrative engagement letter relating to going concern to say the following as it relates to the auditor's responsibilities:

*Conclude, based on the audit evidence obtained, whether there are conditions or events, considered in the aggregate, that raise substantial doubt about ABC Company's ability to continue as a going concern for a reasonable period of time and conclude on the appropriateness of management's use of the going concern basis of accounting, when relevant, in the preparation of the financial statements.*

## **Illustrative Reports**

The ASB provided the task force with suggested edits to the illustrative reports. The task force was asked to go through the illustrative reports for consistency and to align the report wording with the changes made to the proposed SASs.

### **2. Other Information**

The ASB voted unanimously to ballot for exposure proposed SAS *The Auditor's Responsibilities Relating to Other Information Included in Annual Reports*. If approved as a final standard, the standard will supersede AU-C section 720, *Other Information Included in Documents Containing Audited Financial Statements*.

The ASB reviewed the draft and the proposed wrap material and directed that

- The proposed standard include a requirement that the auditor is to take appropriate action if the auditor becomes aware that the entity did not provide the auditor with the final version of the documents that were determined to comprise part of the annual report prior to the issuance of those documents to third parties. Application guidance would then be provided as to examples of such appropriate action.
- The proposed effective date of the proposed standard be consistent with the proposed effective date of the proposed auditor's reporting suite of standards. The proposed provisional effective date suggested by the ASB was for audits of financial statements for periods ending on or after June 15, 2019. It is anticipated that early implementation will not be permitted.
- The proposed wrap material include a specific request for comment regarding potential difficulties in operationalizing the proposed standard. Specifically, whether respondents believe that there may be issues due to treatment of inconsistencies and material misstatements of fact as simply misstatements of the other information. Further, respondents should be asked whether consideration of omitted or obscured information will enhance audit quality.
- The comment period on the exposure draft should be 90 days from issuance.

### 3. Convergence/Disclosures

The ASB discussed proposed amendments to various AU-C sections to converge with the IAASB's ISA *Addressing Disclosures in the Audit of Financial Statements—Revised ISAs and Related Conforming Amendments*, which was issued in July 2015. The amendments are intended to focus auditors' attention on disclosures throughout the financial statement audit.

The ASB discussed the fact that the amendments, particularly to ISA/AU-C section 315, may necessitate changes in some firms' methodologies and changes to textbooks, especially with regard to assertions. It was noted that paragraph A127 of AU-C section 315 provides flexibility in addressing assertions.

The ASB directed that the following changes be made:

- ISA/AU-C 300
  - Par. A12b/A14b – add “are addressed” in lead-in to make explicit.
  - Same par.: 1<sup>st</sup> bullet: change “a change in the the required identification of segments and reporting of segment information arising from a significant business combination” to “disclosures about discontinued operations or a significant business combination”
- ISA/AU-C 315
  - Par 26/27 – change “or to “and”
  - Par A30/A30 – delete “, and whether adequate disclosure of such issues in the financial statements has been made” and inserted “and disclosed” after “accounted for”, to be more concise
  - Appendix C, consider whether to insert “, including disclosures” after “financial statements” in the introductory sentence.
- ISA/AU-C 320
  - Par. A10/A12, last bullet, change “segments” to “discontinued operations”
- ISA/AU-C 330
  - Par. 24/26 – reverse proposed change.
  - Par. A52/A57 – retain the text deleted in the ISA, as an example.
  - Par. A59/A72 - Change “appropriate presentation, *arrangement* and content of the financial statements” to “appropriate presentation, *structure* and content of the financial statements” to be consistent with GAAS wording.
- ISA/AU-C 450:
  - Par. A13a/A19a – remove reference to specific industry from each example in bullets
  - Par. A13b/A19b – change “persistent” to “recurring” to be consistent with GAAS wording.
- ISA/AU-C 700
  - A3/A4 – Second sub-bullet to last bullet- Consider what disclosures are intended to help users understand the risks of material misstatement.
  - A4b/A8b – Revise to clarify long sentence.

#### 4. Quality Control

Ms. Karin French, Chair of the IAASB Quality Control Task Force, presented an update on the IAASB Quality Control project and proposed changes to the IAASB's standards relating to Quality Control (ISQC 1 and ISA 220). Proposed changes include incorporating a "Quality Management Process (QMP)", which will require firms to identify their firm's quality objectives, risks to those quality objectives, and responses to those risks.

Comments made by the ASB included the following:

- How will Peer Review evaluate the quality objectives, risks and responses? Peer reviewers tend to be prescriptive. There is subjectivity in Yellow Book about independence and how threats are evaluated and safeguards implemented. A lot of Peer Review interpretations address the subjectivity. The ASB will need to work with the Peer Review Board to help peer reviewers interpret the standards.
- Challenges in the proposed approach include how firms will measure and document governance principles and determining how often firms have to do the quality risk assessment.
- The proposed approach is similar to the COSO approach of inventorying risks, assessing risks and designing responses. How is the documentation of that scalable to small firms? Ms. French noted that the task force is still developing documentation requirements, and will be presenting those to the IAASB in September.
- Scalability:
  - How will the proposed standard be scalable for the largest firms, small firms, sole practitioners? Application material will address; one suggestion is an accompanying document with the ED that shows examples of how to operationalize the standard.
  - Concern was expressed that the smallest firms have ad hoc processes that are nonetheless effective, but don't fit well into flowcharts shown and may not fit into this standard.
  - Input of smaller firms is necessary.
- Root cause analysis was advocated for by regulators and oversight groups but articulating how far to go with it is a challenge.
- Similarities exist with the AICPA's Enhancing Audit Quality. The IAASB QC task force was provided with the EAQ materials. A liaison between the IAASB QCTF, ASB QCTF, and Peer Review may be helpful.
- Regarding EQCR, the ASB encouraged the IAASB to strengthen the requirements so that the right person is the reviewer, and it be done on appropriate stages (which may be only at the end for smaller engagements). The ASB also encouraged the IAASB to maintain flexibility about what significant judgments and documentations are reviewed, to avoid the unintended consequence of having firms reduce the number of engagements subject to the EQCR, and expand guidance on which engagements should be addressed.

## **5. Estimates**

Ms. Ilene Kassman provided a summary of the ASB comment letter drafted by the Estimates Task Force in response to the IAASB's Exposure Draft: *Proposed International Standard on Auditing (ISA) 540 (Revised), Auditing Accounting Estimates and Related Disclosures (ED 540)*. Ms. Kassman explained that although the Estimates Task Force is supportive of the IAASB amending ISA 540 to address existing practice issues, the proposed ISA 540 requires significant changes in order to better address issues such as 1) connectivity of ISA 540 with other ISAs, 2) clarity of the requirements in the ED, and 3) work effort and scope of the ED. In addition, she noted that the comment letter urges the IAASB to work with the PCAOB in order to achieve closer convergence with its respective proposed standards.

## **6. Selected Procedures**

The ASB reviewed a draft of the proposed wrap document to be issued as part of the exposure draft of the proposed SSAE *Selected Procedures* and provided feedback to the Task Force.

Mr. Santay advised the ASB that, while the project will continue to be a joint project with the Accounting and Review Services Committee, it was determined that the most effective and efficient manner in which to keep the project moving forward was to have the ARSC vote to expose the proposed standard for public comment. The ASB and ARSC will jointly consider comment letters received on the exposure draft. The ASB members will be provided with the materials for the August 2017 ARSC meeting when those materials are sent to the ARSC members, and were asked to provide feedback on those materials.

Mr. Santay advised that while the ASB is not considering the draft standard at this time, the proposed standard will incorporate elements from AT-C section 105 that may ultimately be included in a revised AT-C section 105. Those elements are included in the proposed standard to provide potential respondents with all of the requirements that would apply to a selected procedures engagement.

The ASB members provided feedback on the draft wrap document, including the addition of material further describing how the proposed service differs from an agreed-upon procedures engagement, and a question for respondents about the existence of circumstances in which the service should not be permitted.

## **IAASB Update**

Mr. Hasty presented an update on IAASB activities. Mr. Hasty and Mr. Santay represented the ASB at the May 2017 National Standards Setter meeting. A focus of the meeting continues to be the scalability of the ISAs. The issue has been primarily driven by the Nordic Federation's standards for audits of small entities.

Mr. Hasty noted that the June IAASB meeting was primarily focused to discussing issues related to the proposed changes to ISQC1. In addition to ISQC1, the IAASB discussed updates on Emerging Reporting Issues, Data Analytics, and Group Audits. Mr. Hasty also noted that the chairman of the IAASB reported at the meeting that oversight bodies of the IFAC standard setting boards are contemplating reforms and are expected to issue an exposure draft on these reforms during the summer of 2017.

Mr. Hasty stated that the IASTF (International Auditing Standards Task Force) will be meeting on September 14 and October 13. The objective of the Task Force is to give feedback to the IAASB representatives and provide the IAASB with feedback from stakeholders.

### **Convergence Matters**

The ASB welcomed Mr. Marvin Strait, past chair of the AICPA Board of Directors. Mr. Strait expressed his appreciation for the work of the ASB. Mr. Strait and the ASB discussed the ASB's convergence project and exposure process.