



**Agenda Item 1D (clean)**

**Proposed Statement on Auditing Standards (SAS), *Emphasis-of-Matter Paragraphs and Other-Matter Paragraphs in the Independent Auditor's Report***

Requirements	Application Material
<b>Introduction</b>	
<b>Scope of this Proposed SAS</b>	Scope of This Proposed SAS (Ref: par. 4)
1. This proposed Statement on Auditing Standards (SAS) addresses additional communications in the auditor's report when the auditor considers it necessary to	
a. draw users' attention to a matter or matters presented or disclosed in the financial statements that are of such importance that they are fundamental to users' understanding of the financial statements (emphasis-of-matter paragraph); or	

<p>b. draw users' attention to any matter or matters other than those presented or disclosed in the financial statements that are relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report (other-matter paragraph).</p>	
<p>2. Proposed SAS, <i>Communicating Key Audit Matters in the Independent Auditor's Report</i>, establishes requirements and provides guidance when the auditor determines key audit matters and communicates them in the auditor's report. When the auditor includes a Key Audit Matters section in the auditor's report, this proposed SAS addresses the relationship between key audit matters and any additional communication in the auditor's report in accordance with this proposed SAS. (Ref: par. A1)</p>	<p><b>The Relationship between Emphasis of Matter Paragraphs and Key Audit Matters in the Auditor's Report</b> (Ref: par. 2, 81.a.b)</p> <p>A1. Key audit matters are defined in proposed SAS, <i>Communicating Key Audit Matters in the Independent Auditor's Report</i> as 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, which include significant findings from the audit of the financial statements of the current period.<sup>1</sup> Communicating key audit matters provides additional information to intended users of the financial statements to assist them in understanding those matters that, in the auditor's professional judgment, were of most significance in the audit and may also assist them in understanding the entity and areas of significant management judgment in the audited financial statements. When proposed SAS, <i>Communicating Key Audit Matters in the Independent Auditor's Report</i> applies, the use of emphasis-of-matter paragraphs is not a substitute for a description of individual key audit matters.</p>

<sup>1</sup> Proposed SAS, *Communication with Those Charged with Governance*, paragraph xx

<p>3. AU-C section 570, <i>The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern</i> and AU-C section 720, <i>Other Information in Documents Containing Audited Financial Statements</i> establish requirements and provide guidance about communication in the auditor's report relating to going concern and other information, respectively.</p>	
<p>4. Exhibit B, "List of AU-C Sections Containing Requirements for Emphasis-of-Matter Paragraphs," and exhibit C, "List of AU-C Sections Containing Requirements for Other-Matter Paragraphs," identify AU-C sections containing specific requirements for the auditor to include an emphasis-of-matter paragraph or other-matter paragraph, respectively, in the auditor's report. Accordingly, the requirements in this proposed SAS regarding the form of such paragraphs apply. (Ref: par. A2)</p>	<p>A2. The AU-C sections identified in exhibits B and C require the auditor to include an emphasis-of-matter paragraph or other-matter paragraph, respectively, in the auditor's report relating to certain matters. The nature of these matters is such that they are brought to the attention of users of the auditor's report in all instances rather than at the discretion of the auditor. The explanatory language provided by such required paragraphs achieves the same objective as an emphasis-of-matter or other-matter paragraph that is included based on the professional judgment of the auditor (that is, to provide additional communication to the users of the auditor's report). Therefore, the auditor follows the requirements in this section regarding the form of these required paragraphs.</p>
<p><b>Effective Date</b></p>	
<p>5. This proposed SAS is effective for audits of financial statements for periods ending on or after December 15, 20XX.</p>	
<p><b>Objective</b></p>	
<p>6. The objective of the auditor, having formed an opinion on the financial statements, is to draw users' attention, when in the auditor's judgment it is necessary to do so, by way of clear additional communication in the auditor's report, to</p>	

<p>a. a matter, although appropriately presented or disclosed in the financial statements, that is of such importance that it is fundamental to users' understanding of the financial statements or</p>	
<p>b. as appropriate, any other matter that is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.</p>	
<p><b>Definitions</b></p>	
<p>7. For purposes of generally accepted auditing standards (GAAS), the following terms have the meanings attributed as follows:</p>	
<p><b>Emphasis-of-matter paragraph.</b> A paragraph included in the auditor's report that is required by GAAS, or is included at the auditor's discretion, and that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's professional judgment, is of such importance that it is fundamental to users' understanding of the financial statements.</p>	
<p><b>Other-matter paragraph.</b> A paragraph included in the auditor's report that that is required by GAAS, or is included at the auditor's discretion, and that refers to a matter other than those presented or disclosed in the financial statements that, in the auditor's professional judgment, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.</p>	
<p><b>Requirements</b></p>	
<p><b>Emphasis-of-Matter Paragraphs in the Auditor's Report</b></p>	

<p>8. If the auditor considers it necessary to draw users’ attention to a matter appropriately presented or disclosed in the financial statements that, in the auditor’s professional judgment, is of such importance that it is fundamental to users’ understanding of the financial statements, the auditor should include an emphasis-of-matter paragraph in the auditor’s report, provided: (Ref: par. A3–A4)</p>	<p><b>Circumstances in Which an Emphasis of Matter Paragraph May Be Necessary</b> (Ref: par. 8)</p> <p>A3. Exhibit B identifies AU-C sections that contain specific requirements for the auditor to include emphasis-of-matter paragraphs in the auditor’s report in certain circumstances. These circumstances include:</p> <ul style="list-style-type: none"> <li>• When a financial reporting framework prescribed by law or regulation would be unacceptable but for the fact that it is prescribed by law or regulation.</li> </ul>
	<ul style="list-style-type: none"> <li>• To alert users that the financial statements are prepared in accordance with a special purpose framework.</li> </ul>
	<ul style="list-style-type: none"> <li>• When facts become known to the auditor after the date of the auditor’s report and the auditor provides a new or amended auditor’s report (such as subsequent events).<sup>2</sup></li> </ul>
	<p>A4. In addition to the required emphasis-of-matter paragraphs listed in exhibit B, the following are examples of circumstances when the auditor may consider it necessary to include an emphasis-of-matter paragraph:</p>
	<ul style="list-style-type: none"> <li>• An uncertainty relating to the future outcome of unusually important litigation or regulatory action.</li> </ul>

<sup>2</sup> AU-C 560, *Subsequent Events and Subsequently Discovered Facts*, paragraphs 12(b) and 16

Proposed SAS, EOM/OM (AU-C 706) – Clean  
ASB Meeting, July 17-20, 2017

	<ul style="list-style-type: none"> <li>• A significant subsequent event that occurs between the date of the financial statements and the date of the auditor’s report.<sup>3</sup></li> </ul>
	<ul style="list-style-type: none"> <li>• <del>Early application (where permitted) of a new accounting standard that has a material effect on the financial statements</del></li> <li>• A major catastrophe that has had, or continues to have, a significant effect on the entity’s financial position.</li> <li>• Significant transactions with related parties</li> </ul>
	<p>A5. Paragraph 8 requires that an emphasis-of-matter paragraph refer only to matters appropriately presented or disclosed in the financial statements. To include information in an emphasis-of-matter paragraph about a matter beyond what is presented or disclosed in the financial statements may raise questions about the appropriateness of such presentation or disclosure.</p>
<p>a. The auditor would not be required to modify the opinion in accordance with proposed SAS, <i>Modifications to the Opinion in the Independent Auditor’s Report</i> as a result of the matter; and</p>	
<p>b. When proposed SAS, <i>Communicating Key Audit Matters in the Independent Auditor’s Report</i> applies, the matter has not been determined to be a key audit matter to be communicated in the auditor’s report. (Ref: par. A1 )</p>	

<sup>3</sup> AU-C 560, paragraph 7

<p>9. When the auditor includes an emphasis-of-matter paragraph in the auditor’s report, the auditor should</p>	
<p>a. include the paragraph within a separate section of the auditor’s report with an appropriate heading that includes the term “Emphasis of Matter”;</p>	<p>A6. The auditor may add further context to the heading “Emphasis of Matter” (for example, “Emphasis of Matter – Subsequent Event”) to further describe the nature of the matter addressed by the emphasis-of-matter paragraph.</p>
<p>b. Include in the paragraph a clear reference to the matter being emphasized and to where relevant disclosures that fully describe the matter can be found in the financial statements. The paragraph should refer only to information presented or disclosed in the financial statements; and</p>	
	<p style="text-align: center;"><b>Including an Emphasis of Matter Paragraph in the Auditor’s Report</b> (Ref: par. 9)</p>
<p>c. indicate that the auditor’s opinion is not modified with respect to the matter emphasized. (Ref: par. A7–A8, A14–A15)</p>	<p>A7. The inclusion of an emphasis-of-matter paragraph in the auditor’s report does not affect the auditor’s opinion. An emphasis-of-matter paragraph is not a substitute for</p> <p style="margin-left: 40px;">a. a modified opinion in accordance with proposed SAS, <i>Modifications to the Independent Auditor’s Report</i>, when required by the circumstances of a specific audit engagement;</p>
	<p style="margin-left: 40px;">b. disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation; or</p>

	c. Reporting in accordance with AU-C section 570.
	A8. Paragraphs A14–A15 provide further guidance on the placement of emphasis-of-matter paragraphs in particular circumstances.
<b>Other Matter Paragraphs in the Auditor’s Report</b>	<b>Other-Matter Paragraphs in the Auditor’s Report</b> (Ref: par. 10–11)
	Circumstances in Which an Other-Matter Paragraph May Be Necessary
	Relevant to Users’ Understanding of the Audit
10. If the auditor considers it necessary to communicate a matter other than those that are presented or disclosed in the financial statements that, in the auditor’s professional judgment, is relevant to users’ understanding of the audit, the auditor’s responsibilities or the auditor’s report, the auditor should include an other-matter paragraph in the auditor’s report, provided that when proposed SAS, <i>Communicating Key Audit Matters in the Independent Auditor’s Report</i> applies, the matter has not been determined to be a key audit matter to be communicated in the auditor’s report. (Ref: par.A9–0)	
	A9. In the rare circumstance when the auditor is unable to withdraw from an engagement even though the possible effect of an inability to obtain sufficient appropriate audit evidence due to a limitation on the scope of the audit imposed by management is pervasive, <sup>4</sup> the auditor may consider it necessary to include an other-matter paragraph in the auditor’s report to explain why it is not possible for the auditor to withdraw from the engagement.

<sup>4</sup> See paragraph 13 of proposed SAS, Modifications to the Independent Auditor’s Report for a discussion of this circumstance.



Proposed SAS, EOM/OM (AU-C 706) – Clean  
ASB Meeting, July 17-20, 2017

	Relevant to Users' Understanding of the Auditor's Responsibilities or the Auditor's Report
	A10. Law, regulation or generally accepted practice may require or permit the auditor to elaborate on matters that provide further explanation of the auditor's responsibilities in the audit of the financial statements or of the auditor's report thereon. When the Other-Matter section includes more than one matter that, in the auditor's judgment, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report, it may be helpful to use different sub-headings for each matter.
	A11. An other-matter paragraph does not address circumstances when the auditor has other reporting responsibilities that are in addition to the auditor's responsibility under GAAS (see the "Other Reporting Responsibilities" section in proposed SAS, <i>Forming an Opinion and Reporting on Financial Statements</i> ), or when the auditor has been asked to perform and report on additional specified procedures, or to express an opinion on specific matters.

	<p><i>Reporting on More Than One Set of Financial Statements</i></p> <p>A12. An entity may prepare one set of financial statements in accordance with a general purpose framework (for example, accounting principles generally accepted in the United States of America) and another set of financial statements in accordance with another general purpose framework (for example, International Financial Reporting Standards promulgated by the International Accounting Standards Board), and engage the auditor to report on both sets of financial statements. If the auditor has determined that the frameworks are acceptable in the respective circumstances, the auditor may include an other-matter paragraph in the auditor’s report, referring to the fact that another set of financial statements has been prepared by the same entity in accordance with another general purpose framework and that the auditor has issued a report on those financial statements.</p>
<p>11. When the auditor includes an other-matter paragraph in the auditor’s report, the auditor should include the paragraph within a separate section with the heading “Other Matter,” or other appropriate heading. (Ref: par. A13–A15)</p>	<p><i>Including an Other-Matter Paragraph in the Auditor’s Report</i></p> <p>A13. The content of an other-matter paragraph reflects clearly that such other matter is not required to be presented and disclosed in the financial statements. An other-matter paragraph does not include information that the auditor is prohibited from providing by law, regulation or other professional standards (for example, ethical standards relating to confidentiality of information.) An other-matter paragraph also does not include information that is required to be provided by management.</p>
	<p><b>Placement of Emphasis-of-Matter Paragraphs and Other-Matter Paragraphs in the Auditor’s Report</b> (Ref: par. 9, 11)</p>

	<p>A14. The placement of an emphasis-of-matter paragraph or other-matter paragraph in the auditor’s report depends on the nature of the information to be communicated, and the auditor’s judgment as to the relative significance of such information to intended users compared to other elements required to be reported in accordance with proposed SAS, <i>Forming an Opinion and Reporting on Financial Statements</i>. For example:</p>
	<p><i>Emphasis of Matter Paragraphs</i></p> <ul style="list-style-type: none"> <li>• When a Key Audit Matters section is presented in the auditor’s report, an emphasis-of-matter paragraph may be presented either directly before or after the Key Audit Matters section, based on the auditor’s judgment as to the relative significance of the information included in the emphasis-of-matter paragraph. The auditor may also add further context to the heading “Emphasis of Matter”, such as “Emphasis of Matter – Subsequent Event”, to differentiate the emphasis-of-matter paragraph from the individual matters described in the Key Audit Matters section.</li> </ul>
	<p><i>Other Matter Paragraphs</i></p> <ul style="list-style-type: none"> <li>• When a Key Audit Matters section is presented in the auditor’s report and an other-matter paragraph is also considered necessary, the auditor may add further context to the heading “Other Matter”, such as “Other Matter – Scope of the Audit”, to differentiate the Other Matter paragraph from the individual matters described in the Key Audit Matters section.</li> </ul>

	<ul style="list-style-type: none"> <li>When an Other Matter paragraph is included to draw users' attention to a matter relating to other reporting responsibilities addressed in the auditor's report, the paragraph may be included in the Report on Other Legal and Regulatory Requirements section.</li> </ul>
	When relevant to all the auditor's responsibilities or users' understanding of the auditor's report, the other-matter paragraph may be included as a separate section following the "Report on the Audit of the Financial Statements" and the "Report on Other Legal and Regulatory Requirements."
	A15. Exhibit D is an illustration of the interaction between the Key Audit Matters section, an emphasis-of-matter paragraph and an other-matter paragraph when all are presented in the auditor's report. Illustration 2 in exhibit A includes an emphasis-of-matter paragraph in an auditor's report that contains a qualified opinion and for which key audit matters have not been communicated.
Communication With Those Charged With Governance	<b>Communication with Those Charged with Governance</b> (Ref. par. 12)
12. If the auditor expects to include an emphasis-of-matter or other-matter paragraph in the auditor's report, the auditor should communicate with those charged with governance regarding this expectation and the wording of this paragraph. (Ref: par. A16)	A16. The auditor's communication with those charged with governance required by paragraph 12 enables those charged with governance to be made aware of the nature of any specific matters that the auditor intends to highlight in the auditor's report, and provides them with an opportunity to obtain further clarification from the auditor when necessary. When the inclusion of an other-matter paragraph on a particular matter in the auditor's report recurs on each successive engagement, the auditor may determine that it is unnecessary to repeat the communication on each engagement.

**A18.**

**Exhibit B – List of AU-C Sections Containing Requirements for Emphasis-of-Matter Paragraphs**

**(Ref. par. 4)**

This exhibit identifies paragraphs in other AU-C sections that require the auditor to include an emphasis-of-matter paragraph in the auditor’s report in certain circumstances. The list is not a substitute for considering the requirements and related application and other explanatory material in AU-C sections.

- Paragraph .16c of AU-C section 560, *Subsequent Events and Subsequently Discovered Facts*
- Paragraphs .15–.16 of AU-C section 570, *The Auditor’s Consideration of an Entity’s Ability to Continue as a Going Concern*
- Paragraphs .08–.09 and .11–.13 of AU-C section 708, *Consistency of Financial Statements*
- Paragraphs .19 and .21 of AU-C section 800, *Special Considerations—Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks*

**A19.**

**Exhibit C – List of ISAs AU-C Sections Containing Requirements for Other-Matter Paragraphs**

**(Ref. par. 4)**

This exhibit identifies paragraphs in other AU-C sections that require the auditor to include an other-matter paragraph in the auditor’s report in certain circumstances. The list is not a substitute for considering the requirements and related application and other explanatory material in AU-C sections.

- Paragraph .16c of section 560, *Subsequent Events and Subsequently Discovered Facts*
- Paragraphs .55-.56 and .58-.59 of proposed SAS, *Forming an Opinion and Reporting on Financial Statements*

- Paragraph .12 of section 720, Other Information in Documents Containing Audited Financial Statements
- Paragraph .09 of section 725, Supplementary Information in Relation to the Financial Statements as a Whole
- Paragraph .07 of section 730, Required Supplementary Information
- Paragraph .20 of section 800, Special Considerations—Audits of Financial Statements Prepared in Accordance With Special Purpose Frameworks
- Paragraph .13 of section 806, Reporting on Compliance With Aspects of Contractual Agreements or Regulatory Requirements in Connection With Audited Financial Statements
- Paragraph .07 of section 905, Alert That Restricts the Use of the Auditor’s Written Communication