

ASA 260
(October 2009)

Explanatory Statement

ASA 260 Communication with Those Charged with Governance

Issued by the **Auditing and Assurance Standards Board**



Australian Government

Auditing and Assurance Standards Board

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For approval

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**Reasons for Issuing Auditing Standard ASA 260
*Communication with Those Charged with Governance***

The Auditing and Assurance Standards Board (AUASB) issues Auditing Standard ASA 260 *Communication with Those Charged with Governance* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is an independent statutory board of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001* (the Act), the AUASB may make Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislative Instruments Act 2003*.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required to have regard to any programme initiated by the International Auditing and Assurance Standards Board (IAASB) for the revision and enhancement of the International Standards on Auditing (ISAs) and to make appropriate consequential amendments to the Australian Auditing Standards. The IAASB has undertaken a programme to redraft, and in some cases, revise, in “clarity” format, the entire suite of ISAs. Accordingly, the AUASB has decided to revise and redraft the Australian Auditing Standards using the equivalent redrafted ISAs.

The Auditing Standard conforms with ISA 260 *Communication with Those Charged with Governance*.

Operative Date

ASA 260 *Communication with Those Charged with Governance* is operative for financial reporting periods commencing on or after 1 January 2010.

Purpose of Auditing Standard ASA 260 *Communication with Those Charged with Governance*

The purpose of the Auditing Standard is to establish requirements and to provide application and other explanatory material to auditors regarding their responsibility to communicate with those charged with governance in an audit of a financial report.

Main Features

The Auditing Standard:

- (a) applies irrespective of an entity's governance structure or size;
- (b) provides an overarching framework, including key processes for the auditor's communication with those charged with governance;
- (c) distinguishes between 'management' and 'those charged with governance';
- (d) identifies specific matters to be communicated by the auditor to those charged with governance;
- (e) allows the auditor to communicate other matters, as required by law or regulation;
- (f) promotes two-way communication between the auditor and those charged with governance; and
- (g) establishes documentation requirements.

Preamble and Overall Objectives

ASA 260 is to be read in conjunction with ASA 101 *Preamble to Australian Auditing Standards*, which sets out the intentions of the AUASB on how the Australian Auditing Standards, operative for financial reporting periods commencing on or after 1 January 2010, are to be understood, interpreted and applied. ASA 260 is to be read also in conjunction with ASA 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*.

Process of making Australian Auditing Standards

The AUASB's Strategic Direction, *inter alia*, provides that the AUASB develop Australian Auditing Standards that:

- have a clear public interest focus and are of the highest quality;
- use the International Standards on Auditing (ISAs) of the International Auditing and Assurance Standards Board (IAASB) as the underlying standards;
- conform with the Australian regulatory environment; and
- are capable of enforcement.

In implementing the FRC's Strategic Direction, the AUASB has undertaken a process of revision and redrafting of the Australian Auditing Standards that has:

- updated the form, layout and content of the Australian Auditing Standards;
- addressed the legal enforceability of mandatory obligations;
- maintained clarity of the auditor's obligations;
- incorporated appropriate references to Australian laws and regulations;
- clearly identified, by use of the prefix "Aus", AUASB additions to paragraphs in the requirements or the application and other explanatory material; and
- included other amendments as necessary.

Consultation Process prior to issuing the Auditing Standard

The AUASB has consulted publicly as part of its due process in developing the Auditing Standard. Exposure Draft ED 06/08 *Proposed Auditing Standard: Communication with Those Charged with Governance* (Re-issuance of ASA 260), was issued on 31 July 2008 with a 30 day comment period.

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As an integral part of its consultation with the public, the AUASB sought comments on specific questions including:

- the completeness and accuracy of references in the Auditing Standard to relevant laws and regulations;
- the significant costs, if any, and benefits, of compliance with any additional requirements under the Auditing Standard; and
- whether or not there exist any matters of public interest affecting the issuance of the Auditing Standard.

Submissions were received by the AUASB and these were considered as part of the development and finalisation of the Auditing Standard.

Regulatory Impact Statement

A *Regulatory Impact Statement* (RIS) has been prepared in connection with the redrafting of Australian Auditing Standards in “clarity” format, including *ASA 260 Communication with Those Charged with Governance*.

The RIS has considered both the expected benefits and expected costs of the introduction of clarified auditing standards, including comments provided by stakeholders during the redrafting process. It concluded that the expected benefits to users of audit services, users of audit reports, auditors and the Australian economy in general, are, on balance, likely to outweigh expected costs.

Main Differences from *ASA 260 Communication of Audit Matters with Those Charged with Governance* (April 2006)

The main differences between the Auditing Standard and the Auditing Standard that it supersedes, *ASA 260 Communication of Audit Matters with Those Charged with Governance* (April 2006) are:

1. Auditing Standard ASA 260 is written in “clarity” format using the equivalent International Standard on Auditing (ISA 260 *Communication with Those Charged with Governance*) as the underlying Auditing Standard. Consequently, the format, layout, and paragraph numbering styles are different from the extant Auditing Standard.

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2. The following requirements included in the Auditing Standard are in part, or full, additional to the extant Auditing Standard:
- (a) In some cases, all of those charged with governance are involved in managing the entity, for example, a small business where a single owner manages the entity and no one else has a governance role. In these cases, if matters required by this Auditing Standard are communicated with person(s) with management responsibilities, and those person(s) also have governance responsibilities, the matters need not be communicated again with those same person(s) in their governance role. These matters are noted in paragraph 16(c) of this Auditing Standard. The auditor shall nonetheless be satisfied that communication with person(s) with management responsibilities adequately informs all of those with whom the auditor would otherwise communicate in their governance capacity. (Ref: Para. 13)
 - (b) The auditor shall communicate with those charged with governance the responsibilities of the auditor in relation to the financial report audit, including that:
 - (i) The auditor is responsible for forming and expressing an opinion on the financial report that has been prepared by management with the oversight of those charged with governance; and
 - (ii) The audit of the financial report does not relieve management or those charged with governance of their responsibilities). (Ref: Para. 14)
 - (c) The auditor shall communicate with those charged with governance:
 - (i) The auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial report disclosures. When applicable, the auditor shall explain to those charged with governance why the auditor considers a significant accounting practice, that is acceptable under the applicable financial reporting framework, not to be most appropriate to the particular circumstances of the entity;

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- (ii) Significant difficulties, if any, encountered during the audit;
 - (iii) Unless all of those charged with governance are involved in managing the entity:
 - Significant matters, if any, arising from the audit that were discussed, or subject to correspondence with management; and
 - Written representations the auditor is requesting; and
 - (iv) Other matters, if any, arising from the audit that, in the auditor's professional judgement, are significant to the oversight of the financial reporting process. (Ref: Para. 16)
- (d) The auditor shall evaluate whether the two-way communication between the auditor and those charged with governance has been adequate for the purpose of the audit. If it has not, the auditor shall evaluate the effect, if any, on the auditor's assessment of the risks of material misstatement and ability to obtain sufficient appropriate audit evidence, and shall take appropriate action. (Ref: Para. 22)
- (e) Where matters required by this Auditing Standard to be communicated are communicated orally, the auditor shall include them in the audit documentation, and when and to whom they were communicated. Where matters have been communicated in writing, the auditor shall retain a copy of the communication as part of the audit documentation. (Ref: Para. 23)
3. The following requirement included in the extant Auditing Standard ASA 260 is included as a requirement in Auditing Standard ASA 450 *Evaluation of Misstatements Identified during the Audit*:
- (a) The auditor shall inform those charged with governance of those uncorrected misstatements aggregated by the auditor during the audit that were determined by management to be immaterial, both individually and in the aggregate, to the financial report taken as a whole. (Extant Ref: Para. 17)

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4. Certain guidance material in the extant Auditing Standard has been elevated to requirements.
5. To improve clarity, certain requirements and guidance in the extant Auditing Standard have been re-written, however, the equivalent meanings have been retained.
6. Application and other explanatory material, linked to the additional requirements listed at 2. above is also included in the Auditing Standard.

For approval