

December 2015

Basis for Conclusions *Reporting on Audited Financial Reports— New and Revised Auditor Reporting Standards and Related Conforming Amendments*

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

Draft

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Basis for Conclusions Reporting on Audited Financial Reports—New and Revised Auditor Reporting Standards and Related Conforming Amendments has been developed by the Auditing and Assurance Standards Board (AUASB) to provide a background to, and rationale for, the development and approval of the Auditing Standards by the AUASB. The *Basis for Conclusions* relates to, but does not form part of the Australian Auditing Standards.

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Draft

BASIS FOR CONCLUSIONS

Reporting on Audited Financial Reports—New and Revised Auditor Reporting Standards and Related Conforming Amendments

1. This *Basis for Conclusions* is issued by the Auditing and Assurance Standards Board (AUASB). It provides a background to, and rationale for, the development and approval of changes to the Australian Auditing Standards by the AUASB.

This *Basis for Conclusions*:

- Relates to, but does not form part of the Australian Auditing Standards and is not a substitute for reading the Standards.
- Provides information on the more significant issues dealt with by the AUASB and does not include information on all decisions made in the development of the standards covered by the scope of this document.

Scope

2. This *Basis for Conclusions* applies to the following Australian Auditing Standards:

ASA	Name of Auditing Standard	Change
210	<i>Agreeing the Terms of Audit Engagements</i>	Conforming Amendments
220	<i>Quality Control for an Audit of a Financial Report and Other Historical Financial Information</i>	Conforming Amendments
230	<i>Audit Documentation</i>	Conforming Amendments
260	<i>Communicating with Those Charged with Governance</i>	Revised
450	<i>Evaluation of Misstatements Identified during the Audit</i>	Conforming Amendments
500	<i>Audit Evidence</i>	Conforming Amendments
510	<i>Initial Audit Engagements—Opening Balances</i>	Conforming Amendments
540	<i>Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures</i>	Conforming Amendments
560	<i>Subsequent Events</i>	Conforming Amendments
570	<i>Going Concern</i>	Revised
580	<i>Written Representations</i>	Conforming Amendments
600	<i>Special Considerations—Audits of a Group Financial Report (Including the Work of Component Auditors)</i>	Conforming Amendments
700	<i>Forming an Opinion and Reporting on a Financial Report</i>	Revised
701	<i>Communicating Key Audit Matters in the Independent Auditor’s Report</i>	New Standard

Basis for Conclusions Reporting on Audited Financial Reports—New and Revised Auditor Reporting Standards and Related Conforming Amendments

ASA	Name of Auditing Standard	Change
705	<i>Modifications to the Opinion in the Independent Auditor's Report</i>	Revised
706	<i>Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report</i>	Revised
710	<i>Comparative Information—Corresponding Figures and Comparative Financial Reports</i>	Conforming Amendments
720	<i>The Auditor's Responsibilities Relating to Other Information</i>	Revised
810	<i>Engagements to Report on Summary Financial Statements</i>	Conforming Amendments

Operative Date

3. The new and revised Australian Auditing Standards and related conforming amendments to other Australian Auditing Standards are operative for financial reporting periods ending on or after **15 December 2016**.

Background

4. While users of financial reports have signalled that the auditor's opinion on the financial report is valued, many have called for the auditor's report to be more informative – in particular, for auditors to provide more relevant information to users based on the audit that was performed. Accordingly, the IAASB set out to develop new and revised standards relating to auditor reporting, which are aimed at enhancing the informational value of the auditor's report.
5. The IAASB's project has resulted in the creation of one new International Standard on Auditing (ISA) – ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*; the revision of several existing auditing standards and related conforming amendments to several auditing standards.
6. The application date for the IAASB's enhancements to auditor reporting is for financial statement periods ending on or after 15 December 2016.

Expected Benefits

7. The auditor's report is the key deliverable addressing the output of the audit process. The IAASB intends for its new and revised Auditor Reporting standards to result in an auditor's report that increases the confidence in the audit and the financial statements, which is in the public interest.
8. The IAASB believes that in addition to the increased transparency and enhanced informational value of the auditor's report, changes to auditor reporting will also have the benefit of:
 - **Enhanced communications** between the auditor and investors as well as between auditors and those charged with governance;
 - **Increased attention** by management and those charged with governance (e.g., the audit committee) to the disclosures in the financial statements to which reference is made in the auditor's report; and
 - **Renewed focus of the auditor** on matters to be reported, which could indirectly result in an increase in professional scepticism.

Effect on the Financial Reporting Process

- The enhancements to the auditor’s report build upon the underlying concepts in a financial statements audit undertaken in accordance with International Standards on Auditing (ISAs) addressing how a risk-based audit is performed and what is required to be communicated with those charged with governance.
 - While auditor communications in the auditor’s report are expected to be entity-specific in order to be informative to users, it remains the responsibility of management, with the oversight of those charged with governance, to communicate relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework.
9. Further details can be found on the IAASB’s website: <http://www.ifac.org/auditing-assurance>
- At a Glance
<http://www2.ifac.org/system/files/publications/files/Audit-Reporting-At%20a%20Glance.pdf>
 - Basis for Conclusions
<http://www2.ifac.org/system/files/publications/files/Basis%20for%20Conclusions%20-%20Auditor%20Reporting%20-%20final.pdf>
 - Illustrative Key Audit Matters
<http://www2.ifac.org/system/files/publications/files/IAASB-Auditor-Reporting-Toolkit-Illustrative-Key-Audit-Matters.pdf>
 - Auditor Reporting on Going Concern
<http://www2.ifac.org/system/files/publications/files/Auditor-Reporting-Toolkit-Going-Concern.pdf>
 - ISA 700 (Revised)
http://www2.ifac.org/system/files/publications/files/ISA-700-Revised_8.pdf
 - ISA 701 (New)
http://www2.ifac.org/system/files/publications/files/ISA-701_2.pdf
 - ISA 705 (Revised)
http://www2.ifac.org/system/files/publications/files/ISA-705-Revised_0.pdf
 - ISA 706 (Revised)
http://www2.ifac.org/system/files/publications/files/ISA-706-Revised_0.pdf
 - ISA 570 (Revised)
<http://www2.ifac.org/system/files/publications/files/ISA-570-%28Revised%29.pdf>
 - ISA 260 (Revised)
http://www2.ifac.org/system/files/publications/files/ISA-260-Revised_1.pdf

- Consequential Conforming Amendments to ISAs

http://www2.ifac.org/system/files/publications/files/Conforming-Amendments-to-ISAs_1.pdf

AUASB

10. In accordance with its mandates under section 227 of the *Australian Securities and Investments Commission Act 2001* and the Financial Reporting Council's (FRC) *Strategic Direction*, the AUASB's policy is to adopt the IAASB's ISAs, unless there are compelling reasons not to do so; and to amend the ISAs only when there are compelling reasons to do so.
11. Compelling reasons fall broadly into two categories: legal and regulatory; and principles and practices considered appropriate in maintaining or improving audit quality in Australia. Compelling reasons are further guided by the AUASB's policy of harmonisation with the standards of the New Zealand Auditing and Assurance Standards Board (NZAuASB).
12. The AUASB's principles of convergence with the ISAs and harmonisation with the New Zealand auditing standards can be found on the AUASB's website:
http://www.auasb.gov.au/admin/file/content102/c3/Aug14_IAASB-NZAuASB_Principles_of_Convergence_and_Harmonisation.pdf
13. The AUASB has decided to adopt the new, revised and amended ISAs, relating to auditor reporting, into the Australian Auditing Standards that are made under section 336 of the *Corporations Act 2001* (the Act). Prior to implementation, the AUASB is required to consult with stakeholders and accordingly has issued Exposure Drafts **ED 01/15** and **ED 02/15** for public exposure and comment. All comments received from stakeholders are considered by the AUASB prior to finalisation of the proposed new, revised or amended standards.

Public Exposure

14. The IAASB enhancements to auditor reporting were accomplished through changes to the ISAs. The new and revised Australian standards, including the amendments described below, were published for public comment in two exposure drafts:
 - (a) ED 01/15: *Reporting on Audited Financial Reports—New and Revised Auditor Reporting Standards and Related Conforming Amendments* issued on 30 April 2015 and closed on 30 June 2015; and
 - (b) ED 02/15: *The Auditor's Responsibilities Relating to Other Information and Related Conforming Amendments* issued on 12 June 2015 and closed on 10 August 2015.

Amendments to the ISAs Prior to Public Exposure

15. The adoption of international standards and any changes to adopted standards are governed by the AUASB's policies regarding convergence with IAASB standards and harmonisation with the standards of the NZAuASB (see paragraphs 10 to 13). The policies and procedures incorporate "compelling reasons" tests which must be used to support changes to the international standards. Changes are made only when the AUASB is satisfied that there are persuasive reasons to do so.

AUASB Drafting Conventions

16. The changes to auditor reporting relate solely to Australian Auditing Standards issued under section 336 of the Act. Accordingly, the AUASB makes format and other editorial changes from the ISAs, such as spelling and terminology changes, to accord with Australian legislative requirements, particularly those relating to legislative instruments.

Other General Changes

17. The AUASB made other general changes from the ISAs which reflect ongoing policies and include:
- (a) Inclusion of illustrative example auditor's reports that comply with the Act;
 - (b) Replacement of requirements, guidance and references to international ethical requirements with requirements, guidance and references to relevant Australian ethical requirements; and
 - (c) Replacing references to international standards and international standard-setters with references to relevant Australian standards and standard-setters.

Other Specific Changes

18. In addition to the more general changes described above, the AUASB made further changes from the ISAs, and the pre-existing Auditing Standards, that addressed the following specific technical matters:
- (a) Non-retention of references in the Auditing Standards to requirements by other legislation or regulations, particularly those contained in the Act.
 - (b) Inclusion of a diagram linking going concern considerations, per the revised ISA, with the appropriate types of audit opinions. A long-standing addition to the standard on the basis it is helpful to practitioners. [ASA 570]
 - (c) Retention of the long-standing requirement for auditors to assess going concern for a period of approximately 12 months from the date of the auditor's report. This more onerous requirement replaces the ISA requirement that extends such an assessment to the next financial year-end. [ASA 570]
 - (d) Removal of reference(s) to the use of internal auditors to provide direct assistance to the external auditor. Direct assistance is prohibited under the Australian Auditing Standards. [ASA 610]
 - (e) Non-retention of the pre-existing requirement for the auditor to express an opinion on whether the financial report complies with IFRS. This requirement was considered redundant in view of changes to the Act which now requires the directors' declaration to include a statement on compliance with IFRS. [ASA 700]
 - (f) Removal of references in the ISAs to description of auditor responsibilities on the website of an appropriate authority. The AUASB had not intended establishing and maintaining auditor responsibilities on its website. [ASA 700]
 - (g) Replacement of the ISA requirement for the name of the engagement partner to be included in the auditor's report on the financial report of a listed company with a requirement for the name of the engagement partner to be included only when required by applicable law or regulation.
 - (h) The AUASB decided to not extend the application of key audit matters (KAM) beyond "listed entities". It was also decided to monitor the application of the standard and to formally revisit the question once the IAASB and AUASB post-implementation reviews were complete (expected to be during 2017/2018). [ASA 701]
 - (i) Non-retention of the pre-existing requirements in ASA 706 to include an Emphasis of Matter paragraph or an Other Matter paragraph if required to do so by other auditing standards. The AUASB considered these requirements as unnecessary duplications. [ASA 706]

- (j) The AUASB confirmed its consistency with IAASB policy that early adoption of the standards was permitted unless expressly prohibited, and that no such prohibition should be included in the Australian Auditing Standards.
- (k) The addition of a “decision-tree” for reporting on other information in the auditor’s report.

Major Issues raised by Stakeholders

19. The following summarises the major issues raised by stakeholders at roundtables and other outreach activities and by respondents to the Exposure Drafts; and how the AUASB has addressed them.

Website [ASA 700]

20. A majority percentage of stakeholders supported the ISA model of permitting the auditor responsibilities section of the auditor’s report to be located either in the body of the auditor’s report; in an appendix to the auditor’s report; or referred to when published on the website of an appropriate authority. The location will be at the auditor’s discretion. [ASA 700.40(c)]

AUASB Decision:

The AUASB agreed to reinstate the website option in ASA 700 on the basis that the original decision to remove the option was not based on technical argument, but on operational considerations. The AUASB reversed its previous decision and agreed to develop and maintain the appropriate auditor responsibilities information on its website. This decision results in ASA 700 conforming to ISA 700.

Inclusion of References to the Corporations Act 2001 (the “Act”) [All Standards]

21. A majority percentage of stakeholders did not support the removal of references in the Auditing Standards to requirements contained in the Act. Reasons given included:
- As Australian Auditing Standards are legally enforceable under the Act, it would be unreasonable to omit information related to application of associated legislative requirements (i.e. under the Auditing Standards).
 - The inclusion of references contributes to consistent application of the interrelated laws that apply to financial report audits.
 - There is no compelling reason for removing a long-standing protocol that did not give rise to problems/issues and was in fact considered helpful to the auditor.
 - Inclusion of specific Act references in the standard provide value as a useful reminder of its requirements, and practical guidance for the auditor in unusual situations.
 - Inclusion within the standards of references to requirements under the Act provides context to the requirement and important links to obligations under the Act.

AUASB Decision:

The AUASB agreed to reinstate the references to requirements contained in the Act. The points listed above provide the basis for the AUASB’s decision. The AUASB considers that the inclusion of references to the Act is in the public interest by providing appropriate context and an important link to the Act. Such amendment has the effect of increasing audit quality and therefore presents a compelling reason for reinstatement.

In addition, the AUASB noted that the IAASB’s protocols for amending ISAs while retaining conformity explicitly provides for national standard-setters to make changes due to national

legislation. In this case, the reinstatement of such *references* does not introduce additional requirements or lessen the auditor’s obligations under the standards, they merely reinforce requirements under the Act.

The reinstatement of references to the Act does not conflict with the AUASB’s policy of harmonisation with the standards of the NZAuASB.

Other References [All Standards]

22. Feedback from stakeholders on the removal of references to requirements contained in sources other than the Act revealed a general indifference to their inclusion in the standards.

AUASB Decision:

The AUASB concluded that such references did not meet the compelling reasons test and therefore their removal from the standards would not lessen the quality of the standards nor audit quality. The nature of, and relationship to, the Auditing Standards of such references was not perceived to be the same as those referring to requirements in the Act and accordingly such references were an unnecessary addition which should be removed. This removal was determined to be a new AUASB drafting policy for future amendments from the ISAs to the Australian Auditing Standards.

Name of Engagement Partner [ASA 700]

23. ISA 700 requires the name of the engagement partner to be included in the auditor’s report on the financial report of a listed entity. The ISA is silent on other circumstances. It is long-standing practice in Australia for the engagement partner’s name to be included in the auditor’s reports. However there are a number of audit engagements where there are no requirements on including the engagement partner’s name. The AUASB proposed a change to the standard that the name of the engagement partner is included when required to by law or regulation. This amendment covers the requirements of the Act and permits auditor discretion in cases where there are no legislative or regulatory requirements. The amendment does not lessen the requirements of the ISA.

The existing ASA 700 is silent on this matter.

A majority of stakeholders demonstrated a preference for the engagement partner’s name to be disclosed in *all* auditor’s reports. This view is consistent with existing practice in Australia.

AUASB Decision:

The AUASB concluded that an explicit requirement for the auditor’s name to be included in all auditor’s reports would, in some cases, be inconsistent with audit mandates. Accordingly, the AUASB concluded that the engagement partner’s name be included in the auditor’s report when required by law or regulation and that auditor discretion should exist in all other cases.

Key Audit Matters (KAM) [ASA 701]

24. The IAASB decided that the new standard ISA 701 should be applied to the audits of “listed entities” and that the auditor has discretion in other cases. The IAASB also decided that extending the mandatory application to other entities should be considered once the post-implementation review of the standard was completed (expected in 2017/2018).

The AUASB discussed the types of entities that might be considered “public interest” and agreed the concept of KAM disclosures in the auditor’s report about the matters of most significance to the audit was useful to all users of audited financial reports. However, the AUASB agreed to follow the same approach as the IAASB, and make no changes to the application of the standard at this time.

A significant majority of stakeholders agreed with the AUASB’s approach of not extending the application of ASA 701 at this time.

AUASB Decision:

The AUASB decided to adopt the same strategy as the IAASB, thereby conforming to the IAASB approach – i.e. mandating the use of ASA 701 for audits of listed entities and providing auditor discretion in all other entity cases. No changes from ISA 701 were made.

The AUASB intends to conduct its own post-implementation review of the implementation of the enhanced auditor reporting initiatives, as well as taking an active role in the IAASB’s post-implementation review. Part of the review will be to specifically identify and assess relevant criteria for the potential extension of the application of ASA 701.

Examples of Key Audit Matters [ASA 701]

25. The IAASB did *not* include any illustrative examples of key audit matters (KAM) within ISA 701. However, an IAASB staff paper was issued to provide illustrative KAM. Several stakeholders indicated that AUASB-produced examples would be beneficial to practitioners, especially in the transition period to the enhanced auditor reporting regime.

AUASB Decision:

The AUASB decided against developing and issuing illustrative examples of KAM. The main basis for this decision was the AUASB’s reluctance to potentially “lead” the content and style of KAM when the objective of the standard is clearly for auditors to provide information *specific to the audit of the particular entity*. The specific audit circumstances are all-important in reporting KAM. Furthermore, the AUASB did not want in any way to infer the type and style of wording to be used in reporting KAM, and thereby potentially contributing to “boilerplate” descriptions that would be perceived as of little informational value to users of the auditor’s report.

Going Concern Assessment Period [ASA 570]

26. The AUASB proposed retention of the existing auditor’s going concern assessment period to approximately 12 months from the date of the current auditor’s report. This is a long-standing requirement in Australia. A majority of stakeholders supported retention of this “relevant period” which is well understood by auditor’s and their clients and has not given rise to any previous practical issues. The relevant period clearly aligns the auditor’s assessment to the date of the auditor’s opinion.

AUASB Decision:

The AUASB considers the relevant period as an “ISA Plus” amendment – i.e. it is a stronger requirement than that in the equivalent ISA. To remove the requirement would, in the AUASB’s opinion, reduce the quality of the standard and consequently audit quality and would be contrary to the majority of stakeholders’ support for retention. Accordingly, the pre-existing relevant period assessment period is retained.

Going Concern Diagram [ASA 570]

27. The AUASB has decided to retain a diagram linking going concern considerations, per the revised ISA, with types of audit opinions. The revised long-standing addition to the standard was included as it was considered helpful to practitioners. This view was evident from the roundtables and other outreach activities and the views of AUASB members who were auditors. Stakeholders were not, in the exposure drafts, specifically asked to express a view on inclusion of the diagram, however, the open question on “any other matters of public interest” did not generate any comment either for or against.

AUASB Decision:

The AUASB decided to retain an updated version of the long-standing going concern diagram in an appendix to ASA 570 on the basis it provides useful summary guidance to auditors and adds value in the practical application of the standard.

Conclusion

28. In reaching its final conclusions, the AUASB considered:
- (a) All stakeholder feedback, including the more significant issues outlined above; and
 - (b) The consequential changes that the AUASB made to the ISAs in arriving at the final Australian equivalent Auditing Standards to be made under the Act.
29. The AUASB voted on 1 December 2015, to approve and issue:
- (a) Revisions to ASAs 260, 570, 700, 705, 706 and 720;
 - (b) New Auditing Standard ASA 701; and
 - (c) Conforming amendments to ASAs 210, 220, 230, 450, 500, 510, 540, 560, 580, 600, 710 and 810.

* * *

Appendix 1

(Ref: Para.)

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Appendix 2

(Ref: Para.)

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Appendix 3

(Ref: Para.)

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