

Heads Up

In This Issue:

- Background
- Proposed Changes to the Auditor's Reporting Model
- Proposed Auditor Responsibilities Regarding Other Information and Related Reporting
- Application to Audits of Broker-Dealers and Emerging Growth Companies
- Next Steps and Request for Public Comment
- Appendix A — Comparison of the PCAOB's Proposed CAMs and the IAASB's Proposed KAMs
- Appendix B — Example of an Auditor's Unqualified Report
- Appendix C — Illustration of the Proposed Process for Determining and Reporting CAMs

The PCAOB's proposal represents the most significant expansion of tailored information provided about a financial statement audit by auditors to the user community in the profession's history.

PCAOB Proposes Changes to the Auditor's Reporting Model and the Auditor's Responsibilities Regarding Other Information

by Megan Zietsman, Deloitte & Touche LLP, and Jennifer Burns, Ashley Pruitt, and Brent Simer, Deloitte LLP

On August 13, 2013, the PCAOB issued [Release 2013-005](#),¹ which proposes two new auditing standards on the auditor's reporting model and on the auditor's responsibilities for other information included in annual reports filed with the SEC. The release also proposes conforming changes to certain PCAOB standards.

While retaining the current "pass/fail" approach to the audit report, the PCAOB's proposal represents the most significant expansion of tailored information provided about a financial statement audit by auditors to the user community in the profession's history. The Board is proposing the revisions in response to concerns expressed in feedback by U.S. and global audit standard-setting constituents, including investor groups, that the current auditor's report contains little or no information specific to a particular audit. Investors also indicated that they would benefit from the auditor's unique and relevant insights.

The proposed changes are intended to (1) increase the informational value, usefulness, and relevance of the auditor's report and (2) expand the auditor's responsibilities (and related procedures) for information outside the financial statements. The significant proposed changes include:

- The addition in the auditor's report of a new section in which critical audit matters (CAMs) specific to an audit would be communicated.
- Enhanced language in the auditor's report about the auditor's responsibilities, and new statements in the report intended to communicate more information about the audit and the auditor, including disclosures about auditor independence and tenure.
- An expansion of the auditor's responsibilities for other information in the annual report, and disclosure about this responsibility in the auditor's report, along with a statement about the results of the new required evaluation of that other information.

In a [news release](#) announcing the proposed standards, Martin Baumann, PCAOB chief auditor and director of professional standards at the PCAOB, stated the following:

The goal of these proposed standards and amendments is to significantly improve the current auditor reporting model by requiring the auditor to communicate specific information about each audit based on audit procedures performed.

¹ PCAOB Release No. 2013-005, *Proposed Auditing Standards — The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion; The Auditor's Responsibilities Regarding Other Information in Certain Documents Containing Audited Financial Statements and the Related Auditor's Report; and Related Amendments to PCAOB Standards*.

The PCAOB has conducted research and has performed outreach activities over the last three years to “better understand the nature of improvements that could be made to make the auditor’s report more informative.”

The release indicates that the proposed standards and amendments would be effective for audits of financial statements for fiscal years beginning on or after December 15, 2015; however, this date depends on the timing of approval by the PCAOB and SEC of any final standard and related amendments. We encourage all financial statement stakeholders, including audit committees, company management, investor groups, and others, to study the release and submit comments to the PCAOB. See the [Next Steps and Request for Public Comment](#) section below for information on how to submit comments.

This *Heads Up* provides an overview of the two auditing standards proposed in the release.

Background

As discussed in the release, the PCAOB has conducted research and has performed outreach activities over the last three years to “better understand the nature of improvements that could be made to make the auditor’s report more informative.” The PCAOB and its staff have spoken with investors, auditors, financial statement preparers, audit committees, other regulators and standard setters, and the PCAOB’s Investor Advisory Group and Standing Advisory Group. Outreach activities have also included the PCAOB’s issuance of a [concept release](#)² on June 21, 2011, to obtain public comment on potential changes to the content and form of the auditor’s report. The concept release presented various alternatives, and the PCAOB received a substantial volume of comment letters from a variety of constituents. (See Deloitte’s [June 28, 2011](#), and [November 2, 2011](#), *Heads Up* newsletters for summaries of the concept release and constituent responses, respectively.) In addition, on September 15, 2011, the PCAOB conducted a public roundtable to obtain additional insights on the alternatives presented in the concept release from a diverse group, including investors, financial statement preparers, audit committee members, and auditors.

Editor’s Note: The concept release outlined the following four alternative means of giving financial statement users additional information in the auditor’s report: (1) inclusion of an auditor’s discussion and analysis, (2) required and expanded emphasis paragraphs, (3) auditor assurance on other information outside the financial statements, and (4) clarification of certain language in the standard auditor’s report. Although the proposed standards do not adopt wholesale any of the alternatives presented in the PCAOB’s concept release, they do contain certain of their elements.

At the PCAOB’s August 13, 2013, open meeting to consider proposing the new standards (the “PCAOB’s open meeting”), Mr. Baumann indicated that the staff chose not to propose the alternatives in their entirety for a variety of reasons, including that they would be “costly to implement, could result in delays of financial reporting, would fundamentally change the auditor’s role from an attest role to that of a financial analyst, and could interfere with the role of the audit committee.”³

The release further explains that in developing the proposed standards, the Board considered the following:

- Information currently communicated in the auditor’s report.
- Potential benefits and costs related to the Board’s proposed approach.
- Additional alternative approaches.
- Developments in similar projects by other standard setters (see below).
- Relevant academic research.

² PCAOB Release No. 2011-003, *Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements and Related Amendments to PCAOB Standards*.

³ See [pages 21–27](#) of the release for a discussion of the Board’s consideration of the alternatives described in the concept release.

CAMs (as determined by the auditor) would be communicated in a newly created section of the auditor's report.

In addition to efforts by the PCAOB in the United States to improve the auditor's reporting model, several international and non-U.S. standard setters and regulators have been working on projects to modify the auditor's report. In July 2013, the International Auditing and Assurance Standards Board (IAASB) issued an [exposure draft](#)⁴ on changes to the form and content of the auditor's report for audits conducted under standards of the IAASB. [Appendix A](#) of this *Heads Up* compares various aspects of the PCAOB's release and the IAASB's exposure draft. In developing its proposed standards, the PCAOB also considered the European Commission's [legislative proposal](#) and subsequent European parliamentary [draft report](#) related to audits of public interest entities as well as the Financial Reporting Council's recently adopted revision of its [auditing standard on the auditor's report](#).

Proposed Changes to the Auditor's Reporting Model

The [proposed auditor reporting standard](#) in the release would expand the language in the auditor's report by requiring the auditor to provide specific insight into the audit of a company's financial statements. Under the release, three significant changes would be made to the existing auditor's report:

- CAMs (as determined by the auditor) would be communicated in a newly created section of the report.
- New elements would be added related to auditor independence, auditor tenure, and the auditor's responsibility for, and the results of, the auditor's evaluation of other information outside the financial statements.
- The standardized language would be enhanced to include statements about the auditor's responsibility for fraud and the notes to the financial statements.

[Appendix B](#) of this *Heads Up* contains an example of an auditor's unqualified report and highlights the proposed changes necessary for compliance with the proposed standard.

Overview of CAMs

The proposal defines CAMs as those matters addressed during the audit of the financial statements that:

- "[I]nvolved the most difficult, subjective, or complex auditor judgments";
- "[P]osed the most difficulty to the auditor in obtaining sufficient appropriate evidence"; or
- "[P]osed the most difficulty to the auditor in forming the opinion on the financial statements."

The proposal states that the word "most" is "not intended to imply that only one matter under each criteria would qualify as a critical audit matter."

IAASB Comparison: The IAASB's auditor reporting proposal contains a similar requirement but uses the term key audit matters (KAMs) to describe the matters that auditors of financial statements of listed entities would be required to communicate in a new section of their report. KAMs are defined in the IAASB's proposal 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." KAMs are selected from matters communicated with those charged with governance. See [Appendix A](#) of this *Heads Up* for additional discussion.

⁴ IAASB Exposure Draft, *Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing*.

Specific language would be required in the report if the auditor determines that no CAMs exist, although such determination would be rare.

The Auditor's Determination of CAMs

According to the proposal, CAMs ordinarily are matters of such importance that they are included in the matters required to be:

- Documented in the engagement completion document under AS 3,⁵ which summarizes the significant issues and findings from the audit;
- Reviewed by the engagement quality reviewer under AS 7;⁶
- Communicated to the audit committee under AS 16⁷ or other PCAOB standards; or
- Any combination of the three.

Further, the proposal lists factors that the auditor should take into account when determining whether a matter is a CAM (see [Appendix C](#) of this *Heads Up* for an illustration of the proposed process for determining CAMs).

Reporting of CAMs

Under the proposal, the information to be communicated as CAMs would be based on (1) information known to the auditor and (2) procedures that are already performed as part of the audit, and are related to the audit, of the **current-period** financial statements.⁸ CAMs would be included in the auditor's report in a separate section titled "Critical Audit Matters," which would follow the "Opinion on the Financial Statements" section. According to the proposal, for each CAM communicated in the auditor's report, the auditor must:

- Identify the [CAM];
- Describe the considerations that led the auditor to determine that the matter is a [CAM]; and
- Refer to the relevant financial statement accounts and disclosures that relate to the [CAM], when applicable.

The proposal requires the auditor to include specific language⁹ in the report if the auditor determines that no CAMs exist.

Documentation of CAMs

In accordance with AS 3, the auditor must document the determination of CAMs. The proposal states that the audit documentation must "contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to understand the basis for the auditor's determination that (1) each reported matter was a [CAM] and (2) non-reported audit matters addressed in the audit that would appear to meet the definition of a [CAM] were not [CAMs]."

If a matter has been included in the engagement completion document, reviewed by the engagement quality reviewer, or communicated to the audit committee and, after considering the factors mentioned above, the auditor determines that the matter does not meet the definition of a CAM, the auditor should document the basis for determining that the matter is not a CAM.

⁵ PCAOB Auditing Standard No. 3, *Audit Documentation*.

⁶ PCAOB Auditing Standard No. 7, *Engagement Quality Review*.

⁷ PCAOB Auditing Standard No. 16, *Communications With Audit Committees*.

⁸ The proposal states, "When the current period financial statements are presented on a comparative basis with those of one or more prior periods, the auditor should consider communicating critical audit matters relating to the prior periods 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."

⁹ See [pages A1-9 and A1-10](#) of the proposal for the specific language required in the auditor's report when there are no CAMs.

Under the proposal, the auditor would be required to disclose the year the auditor began serving consecutively as the company's auditor.

Amendments to Basic Elements of the Auditor's Report

The release indicates that commenters on the PCAOB's concept release noted that modifications to the language used in the auditor's report could "improve financial statement users' understanding of the nature of an audit, the auditor's responsibilities, and the purpose of the auditor's report." The Board has therefore proposed certain clarifications to existing language in the report to include statements about (1) auditor independence; (2) auditor tenure; (3) the auditor's responsibilities related to fraud and the financial statement footnotes; and (4) the auditor's responsibilities for, and the results of the auditor's evaluation of, other information. See discussion below. See also [Appendix B](#) of this *Heads Up* for an example of an auditor's report that includes these proposed changes.

Auditor Independence

The proposed changes related to auditor independence in the auditor's report would require the auditor to include a statement that the auditor is both:

- A "public accounting firm registered with the PCAOB."
- "[R]equired to be independent with respect to the company in accordance with the United States federal securities laws and the applicable rules and regulations of the SEC and the PCAOB."

Editor's Note: In the current auditor's report, the only reference to auditor independence is in the title of the report, which is "Report of Independent Registered Public Accounting Firm."

Audit Tenure

Under the proposal, the auditor would be required to disclose the year the auditor began serving consecutively as the company's auditor. The release indicates that the "intent of the proposed requirement is to disclose the duration of the auditor's relationship with the company" and that investors and other financial users have expressed interest in knowing the auditor's tenure.

Additional Standardized Language

The proposal requires the auditor to include the phrase "**whether due to error or fraud**" in the statement describing the auditor's responsibilities under PCAOB standards to obtain reasonable assurance about whether the financial statements are free of material misstatement. The discussion of the auditor's procedures would also include a statement that the audit includes performing procedures to assess the risks of material misstatement and performing procedures to respond to those risks. Further, in identifying the financial statements included as part of the audit, the auditor would refer to the "related notes" of the financial statements.

Proposed Auditor Responsibilities Regarding Other Information and Related Reporting

The [proposed other information standard](#) in the release would expand the auditor's responsibilities related to other information contained in the annual report by expanding the definition of other information and by increasing the auditor's required procedures related to such information. The proposal would also create related auditor reporting requirements.

Proposed Definition of Other Information

Under the proposal, other information includes:

- Information (other than the audited financial statements and the related auditor's report) "in a company's annual report that is filed with the SEC under the Securities Exchange Act of 1934 ("Exchange Act") and contains that company's audited financial statements and the related auditor's report."
- Information incorporated by reference in the annual report that is available to the auditor before the issuance of the auditor's report.
- Information incorporated by reference from the company's definitive proxy statement filed within 120 days after the end of the fiscal year covered by the Form 10-K.

Editor's Note: The proposal's description of other information differs substantively from the description of other information in PCAOB AU Section 550,¹⁰ which outlines current requirements related to the auditor's responsibility for other information. AU Section 550 applies only "to other information contained in (1) annual reports to holders of securities or beneficial interests, annual reports of organizations for charitable or philanthropic purposes distributed to the public, and annual reports filed with regulatory authorities under the Exchange Act or (2) other documents to which the auditor, at the client's request, devotes attention." The current standard does not apply to information incorporated by reference into an annual report. In addition, AU Section 550 states that the auditor's current responsibility "does not extend beyond the financial information identified in [the audit] report, and the auditor has no obligation to perform any procedures to corroborate other information contained in a document."

Like AU Section 550, the proposed standard would not apply when the financial statements and the auditor's report appear in a registration statement filed under the Securities Act of 1933.

The proposal's description of other information differs substantively from the description of other information in PCAOB AU Section 550.

Auditor Objectives and Audit Procedures Related to Other Information

The proposal states that the objectives and procedures of the auditor related to other information are as follows:

- a. To evaluate whether the other information contains (1) a material inconsistency with amounts or information, or the manner of their presentation, in the audited financial statements ("material inconsistency"); (2) a material misstatement of fact; or (3) both and, if so, to respond appropriately; and
- b. When issuing an auditor's report, to communicate in the auditor's report the auditor's responsibilities for other information and whether, based on relevant audit evidence obtained and conclusions reached during the audit, the other information contains a material inconsistency, a material misstatement of fact, or both. [Footnote omitted]

Further, under the proposal, the auditor is required "to **read** the other information and, based on relevant audit evidence obtained and conclusions reached during the audit, **evaluate**" (emphasis added) the following:

- a. Consistency of amounts in the other information, and the manner of their presentation, that are intended to be the same as, or to provide greater detail about, the amounts in the financial statements, with the amounts in the financial statements and relevant audit evidence;
- b. Consistency of any qualitative statement in the other information, and the manner of its presentation, that is intended to represent or provide greater detail about information in the financial statements, with the financial statements and relevant audit evidence;
- c. Other information not directly related to the financial statements as compared to relevant audit evidence obtained and conclusions reached during the audit; and

¹⁰ PCAOB AU Section 550, *Other Information in Documents Containing Audited Financial Statements*.

- d. Amounts in the other information that are calculated using amounts in (1) the other information; (2) the financial statements; or (3) relevant audit evidence, by recalculating the amounts for mathematical accuracy.

If, on the basis of performing this evaluation, the auditor identifies a potential material inconsistency, a potential material misstatement of fact, or both, the auditor would be required to discuss the matter with management and request that management revise the other information.

The proposal outlines additional audit procedures for situations in which management fails to make appropriate revisions, including timely communication with the audit committee and, if applicable, determining the auditor's responsibilities under Section 10A of the Exchange Act and considering whether to withdraw from the engagement. Finally, the proposal notes that if the auditor determines that there is a potential misstatement in the audited financial statements as a result of the required evaluation of the other information, the auditor should refer to:

- AS 14¹¹ and AU Section 508,¹² "if the auditor's report on the financial statements has not been issued"; or
- AU Section 561¹³ "if the auditor's report on the financial statements has been issued."

Editor's Note: The proposal's auditor performance provisions significantly add to the auditor's responsibilities for other information by introducing required audit procedures to support the auditor's conclusion about the auditor's evaluation of other information. Specifically, under AU Section 550, the auditor is required to "**read**" and "**consider**" other information, whereas under the proposal, the auditor is required to "**read**" and "**evaluate**" the other information on the basis of relevant audit evidence obtained and conclusions reached during the audit. The release acknowledges that some of the information that the auditor would be required to read and evaluate may not be directly related to the audited financial statements (e.g., nonfinancial data or information related to the company's operations). The auditor's evaluation of such information would be based on relevant audit evidence obtained and conclusions reached during the audit, but the auditor "would not be required to perform procedures to obtain additional audit evidence regarding other information not directly related to the financial statements that was not required to be obtained during the audit."

Under the proposal, the auditor would be required to describe the results of the evaluation of other information in the auditor's report.

Reporting in the Auditor's Report

Under the proposal, the auditor would be required to include a separate section, "The Auditor's Responsibilities Regarding Other Information," in the auditor's report. This section would contain the following:

- a. A statement that . . . the auditor evaluated whether the other information contains a material inconsistency with the financial statements, a material misstatement of fact, or both;
- b. Identification of the annual report that contains the other information, and the audited financial statements and the auditor's report, by referring to the SEC Exchange Act form type and the period end date of the financial statements;
- c. A statement that the auditor's evaluation of the other information was based on relevant audit evidence obtained and conclusions reached during the audit;
- d. A statement that the auditor did not audit the other information and does not express an opinion on the other information; and
- e. A statement that, based on the evaluation, the auditor:
 - (1) Has not identified a material inconsistency or a material misstatement of fact in the other information; or [Footnote omitted]

¹¹ PCAOB Auditing Standard No. 14, *Evaluating Audit Results*.

¹² PCAOB AU Section 508, *Departures From Unqualified Opinions and Other Reporting Circumstances* (new proposed title).

¹³ PCAOB Auditing Standard No. 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report*.

- (2) Has identified a material inconsistency, a material misstatement of fact, or both in the other information that has not been appropriately revised and a description of the material inconsistency, the material misstatement of fact, or both.

The Board has requested feedback and corresponding data related to efficiency, competition, and capital formation and any benefits and costs associated with the proposals.

Application to Audits of Broker-Dealers and Emerging Growth Companies

On July 30, 2013, the SEC issued a [final rule](#) that amended Rule 17a-5 under the Exchange Act to require that audits of brokers' and dealers' financial statements be performed in accordance with the standards of the PCAOB. The rule is effective for audits with fiscal years ending on or after June 1, 2014. The Board is seeking comments on issues specific to broker-dealers and on whether the proposed standards and amendments in the release are appropriate for audits of brokers-dealers. It is also seeking responses to questions on applying the proposed standards to audits of emerging growth companies (EGCs). The JOBS¹⁴ Act requires the SEC to perform a specific economic analysis when considering whether PCAOB rules, including auditing standards, should apply to audits of EGCs.¹⁵ (For more information on EGCs, see Deloitte's April 2, 2012 (updated May 8, 2012), [Heads Up](#).) The Board has requested feedback and corresponding data related to efficiency, competition, and capital formation and any benefits and costs associated with the proposals.

Next Steps and Request for Public Comment

During the PCAOB's open meeting, the Board emphasized the importance of the comment process and the careful consideration by the Board and staff of comments received. In the release, the Board notes that it is considering holding a public roundtable in 2014 to discuss the proposed standards and comments received.

Considerations for Comment

Appendixes 5, 6, and 7 of the release contain questions that apply to various sections of the proposed standards. We encourage all interested parties to study the release, including the questions for commenters, and submit feedback to the PCAOB. Comments should be sent to the Office of the Secretary, PCAOB, 1666 K Street, N.W., Washington, D.C. 20006-2803. Comments also may be submitted by e-mail to comments@pcaobus.org or through the Board's Web site at www.pcaobus.org. All comments should refer to PCAOB Rulemaking Docket Matter No. 034 in the subject or reference line and should be received by the Board no later than 5:00 p.m. (EST) on December 11, 2013.

¹⁴ Jumpstart Our Business Startups.

¹⁵ As defined in Section 3(a)(80) of the Exchange Act.

Appendix A — Comparison of the PCAOB’s Proposed CAMs and the IAASB’s Proposed KAMs

The table below compares various aspects of the PCAOB’s proposed CAMs and the IAASB’s proposed KAMs.

	PCAOB’s Proposed Critical Auditing Matters ¹⁶	IAASB’s Proposed Key Audit Matters ¹⁷
Definition	Those matters addressed during the audit that: <ul style="list-style-type: none"> Involved the most difficult, subjective, or complex auditor judgments; Posed the most difficulty to the auditor in obtaining sufficient appropriate evidence; or Posed the most difficulty to the auditor in forming the opinion on the financial statements. 	Those matters that, in the auditor’s professional judgment, were of most significance in the audit of the financial statements of the current period.
Period covered	Current-period financial statements. ¹⁸	Current-period financial statements.
Determination of CAMs / KAMs	<p>CAMs ordinarily are matters of such importance that they are included in the matters required to be:</p> <ul style="list-style-type: none"> Documented in the engagement completion document, which summarizes the significant issues and findings from the audit; Reviewed by the engagement quality reviewer; Communicated to the audit committee; or Any combination of the three. <p>Factors to be considered are:</p> <ul style="list-style-type: none"> The degree of subjectivity involved in determining or applying audit procedures to address the matter or in evaluating the results of those procedures. The nature and extent of audit effort required to address the matter. The nature and amount of available relevant and reliable evidence regarding the matter or the degree of difficulty in obtaining such evidence. The severity of control deficiencies identified relevant to the matter, if any. The degree to which the results of audit procedures to address the matter resulted in changes in the auditor’s risk assessments, including risks that were not identified previously, or required changes to planned audit procedures, if any. The nature and significance, quantitatively or qualitatively, of corrected and accumulated uncorrected misstatements related to the matter, if any. 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. The nature of consultations outside the engagement team regarding the matter, if any. Other factors specific to the audit. 	<p>The auditor’s decision-making process in determining KAMs is designed to select a smaller number of matters, from the matters communicated to those charged with governance (TCWG). Matters of most significance may include:</p> <ul style="list-style-type: none"> Areas identified as significant risks in accordance with ISA 315 (Revised)¹⁹ or involving significant auditor judgment; Areas in which the auditor encountered significant difficulty during the audit including sufficient appropriate audit evidence; or Circumstances that required significant modification of the auditors planned approach to the audit. <p>Factors to be considered are:</p> <ul style="list-style-type: none"> The nature and extent of discussion with management, TCWG, and engagement quality control reviews. The effect on the overall strategy and ability to obtain sufficient and appropriate audit evidence. The level of effort and allocation of resources. The difficulty of judgments or high estimation uncertainty. Matters involving consultation. Areas involving significant unusual transactions, related parties, internal control deficiencies. The involvement of specialists. Whether disclosure would enhance users’ understanding of the audit. Prior-year KAMs. The industry in which the entity operates and recent significant economic, accounting, regulatory or other developments.

¹⁶ The text in this column is derived from the PCAOB’s proposed auditor reporting standard.

¹⁷ The text in this column is derived from the “Requirements” and “Application and Other Explanatory Material” sections of Proposed International Standard on Auditing 701, *Communicating Key Audit Matters in the Independent Auditor’s Reporting*.

¹⁸ See footnote 8.

¹⁹ International Standard on Auditing 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and its Environment*.

	PCAOB's Proposed CAMs	IAASB's Proposed KAMs
Reporting of CAMs / KAMs	<p>CAMs are communicated in a separate section of the auditor's report titled "Critical Audit Matters," which follows the "Opinion on the Financial Statements" section and any explanatory paragraphs.</p> <p>The description of each CAM in the auditor's report shall:</p> <ul style="list-style-type: none"> • Identify the CAM. • Describe the considerations that led the auditor to determine that the matter is a CAM. • Refer to the relevant financial statement accounts and disclosures that relate to the CAM, when applicable. 	<p>KAMs are communicated in a separate section of the auditor's report titled "Key Audit Matters."</p> <p>The description of each KAM in the auditor's report shall include:</p> <ul style="list-style-type: none"> • An appropriate subheading. • An explanation to enable users of the financial statements to understand why the matter is considered to be one of most significance in the audit and to the extent necessary, its effect on the audit.
Reporting when no CAMs / KAMs exist	<p>In circumstances in which the auditor has determined that CAMs do not exist, the proposed auditor reporting standard requires specific language to be included in the auditor's report including a statement that "we determined that there are no [CAMs]."</p>	<p>If the auditor determines that there are no KAMs to communicate in the auditor's report, the auditor shall:</p> <ul style="list-style-type: none"> • Discuss this conclusion with the engagement quality control reviewer, for those engagements where one has been appointed; • Communicate this conclusion with TCWG; and • Explain in the auditor's report that this section of the auditor's report is intended to describe the matters communicated with TCWG that the auditor has determined, in the auditor's professional judgment, were of most significance in the audit of the financial statements and the auditor has determined that there are no matters to report.
Audit documentation	<p>In accordance with AS 3, the auditor must document the determination of CAMs. The audit documentation must contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to understand the basis for the auditor's determination that (1) each reported matter was a CAM and (2) non-reported audit matters addressed in the audit that would appear to meet the definition of a CAM were not CAMs.</p> <p>If a matter has been included in the engagement completion document, reviewed by the engagement quality reviewer, or communicated to the audit committee and, after considering the factors mentioned above, the matter does not meet the definition of a CAM, the auditor would document the basis for determining that the matter is not a CAM.</p>	<p>The auditor shall document the matters that will be communicated as KAMs, and the judgments made in reaching this determination in accordance with ISA 230.²⁰ This includes, where applicable, the rationale for the auditor's determination that there are no KAMs to communicate in the auditor's report.</p> <p>Audit documentation in accordance with ISA 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. It 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.</p> <p>Professional judgments related to the matters determined to be KAMs are likely to be supported by the documentation of the auditor's communications with TCWG and the audit documentation related to each individual KAM as well as certain other audit documentation of significant matters arising during the audit. The documentation of the significant professional judgments made in determining the KAMs draws upon this documentation. Such documentation also may provide an indication that other matters communicated with TCWG are not KAMs.</p>

²⁰ International Standard on Auditing 230, *Audit Documentation*.

Appendix B — Example of an Auditor’s Unqualified Report

Below is an example of an auditor’s unqualified report, as reprinted (and annotated) from Appendix B the proposed auditor reporting standard. Proposed changes from the illustrative report in AU Section 508 are underlined.

Report of Independent Registered Public Accounting Firm

To the shareholders and board of directors of X Company

[Introduction]

We have audited the accompanying balance sheets of X Company (the “Company”) as of December 31, 20X2 and 20X1, the related statements of operations, stockholders’ equity, and cash flows, for each of the three years in the period ended December 31, 20X2, and the related notes (collectively referred to as the “financial statements”). These financial statements are the responsibility of the Company’s management.

We are a public accounting firm registered with the Public Company Accounting Oversight Board (“PCAOB”) (United States) and are required to be independent with respect to the Company in accordance with the United States federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission (“SEC”) and the PCAOB. We or our predecessor firms have served as the Company’s auditor consecutively since [year].

Auditor
Independence

Auditor Tenure

[Basis of Opinion]

Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures include examining, on a test basis, appropriate evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Additional
Standardized
Language

[Opinion on the Financial Statements^[21]]

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of [a] December 31, 20X2 and 20X1, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 20X2, in conformity with [the applicable financial reporting framework].

Critical Audit Matters

The standards of the PCAOB require that we communicate in our report critical audit matters relating to the audit of the current period’s financial statements or state that we determined that there are no critical audit matters. Critical audit matters are those matters addressed during the audit that (1) involved our most difficult, subjective, or complex judgments; (2) posed the most difficulty to us in obtaining sufficient appropriate evidence; or (3) posed the most difficulty to us in forming our opinion on the financial statements. The critical audit matters communicated below do not alter in any way our opinion on the financial statements, taken as a whole.

Critical Audit
Matters

[Include critical audit matters]

The Auditor’s Responsibilities Regarding Other Information

In addition to auditing the Company’s financial statements in accordance with the standards of the PCAOB, we evaluated whether the other information, included in the annual report on [SEC Exchange Act form type] filed with the SEC that contains both the December 31, 20X2 financial statements and our audit report on those financial statements, contains a material inconsistency with the financial statements, a material misstatement of fact, or both. Our evaluation was based on relevant audit evidence obtained and conclusions reached during the audit. We did not audit the other information and do not express an opinion on the other information. Based on our evaluation, we have not identified a material inconsistency or a material misstatement of fact in the other information.^[22]

Other Information

[Signature]

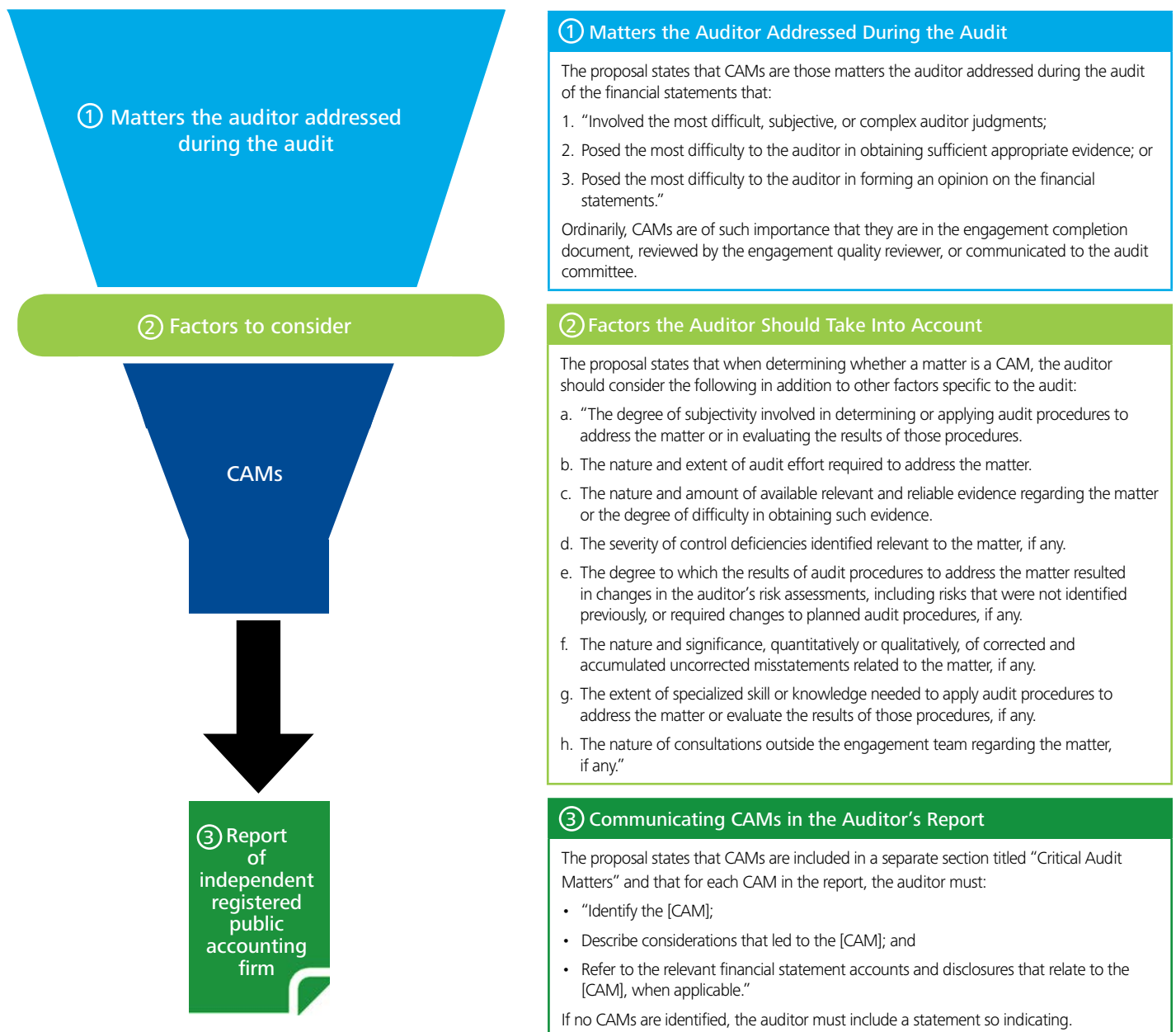
[City and State or Country]

[Date]

²¹ An “emphasis of matter” explanatory paragraph may also be included in the auditor’s report and would be placed before the “Critical Audit Matters” section. See pages A1-10–A-12 of the proposed auditor reporting standard.

²² When the auditor has identified a material inconsistency, this sentence should be replaced with the following: “Based on our evaluation, we identified [a material inconsistency, a material misstatement of fact, or both] in the other information that has not been appropriately revised.” In addition, the auditor would provide a description of the material inconsistency, material misstatement of fact, or both.

Appendix C — Illustration of the Proposed Process for Determining and Reporting CAMs



Subscriptions

If you wish to receive *Heads Up* and other accounting publications issued by Deloitte's Accounting Standards and Communications Group, please [register](http://www.deloitte.com/us/subscriptions) at www.deloitte.com/us/subscriptions.

Dbriefs for Financial Executives

We invite you to participate in *Dbriefs*, Deloitte's webcast series that delivers practical strategies you need to stay on top of important issues. Gain access to valuable ideas and critical information from webcasts in the "Financial Executives" series on the following topics:

- Business strategy & tax.
- Financial reporting for taxes.
- Technology.
- Driving enterprise value.
- Governance and risk.
- Transactions & business events.
- Financial reporting.
- Sustainability.

Dbriefs also provides a convenient and flexible way to earn CPE credit — right at your desk. [Subscribe](#) to *Dbriefs* to receive notifications about future webcasts at www.deloitte.com/us/dbriefs.

Registration is available for this upcoming *Dbriefs* webcast. Use the link below to register:

- [EITF Roundup: Highlights From the September Meeting](#) (September 18, 2 p.m. (EDT)).

Technical Library: The Deloitte Accounting Research Tool

Deloitte makes available, on a subscription basis, access to its online library of accounting and financial disclosure literature. Called Technical Library: The Deloitte Accounting Research Tool, the library includes material from the FASB, the EITF, the AICPA, the PCAOB, the IASB, and the SEC, in addition to Deloitte's own accounting and SEC manuals and other interpretive accounting and SEC guidance.

Updated every business day, Technical Library has an intuitive design and navigation system that, together with its powerful search features, enable users to quickly locate information anytime, from any computer. Technical Library subscribers also receive *Technically Speaking*, the weekly publication that highlights recent additions to the library.

In addition, Technical Library subscribers have access to *Deloitte Accounting Journal* entries, which briefly summarize the newest developments in accounting standard setting.

For more information, including subscription details and an online demonstration, visit www.deloitte.com/us/techlibrary.

Heads Up is prepared by the National Office Accounting Standards and Communications Group of Deloitte as developments warrant. This publication contains general information only and Deloitte is not, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional advisor.

Deloitte shall not be responsible for any loss sustained by any person who relies on this publication.

As used in this document, "Deloitte" means Deloitte & Touche LLP, a subsidiary of Deloitte LLP. Please see www.deloitte.com/us/about for a detailed description of the legal structure of Deloitte LLP and its subsidiaries. Certain services may not be available to attest clients under the rules and regulations of public accounting.