

Insights: PCAOB Auditor's Report — Critical Audit Matters

PCAOB Auditing Standard 3101, *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion*, requires the auditor to identify and describe critical audit matters (CAMs).

What is a CAM?

A CAM is any matter arising from the audit of the financial statements that was communicated or required to be communicated to the audit committee and that: (1) relates to accounts or disclosures that are material to the financial statements and (2) involved especially challenging, subjective, or complex auditor judgment.

The PCAOB "expects that, **in most audits** to which the requirements to communicate critical audit matters applies, the auditor will determine that at least **one** matter involved especially challenging, subjective, or complex auditor judgment."

Effective date for the communication of CAMs* will be phased in as follows:

- Audits of large, accelerated filers — Fiscal years ending on or after **June 30, 2019**.
- Audits of all other companies — Fiscal years ending on or after **December 15, 2020**.

*Communication of CAMs is not required for audits of (1) brokers and dealers reporting under the Securities Exchange Act of 1934 Rule 17a-5; (2) investment companies registered under the Investment Company Act of 1940, other than business development companies; (3) employee stock purchase, savings, and similar plans; and (4) emerging growth companies as defined in Section 3(a)(80) of the Securities Exchange Act of 1934.

Expected benefits

Increased confidence in financial statements

Enhanced communication about the audit directly from the auditor

More informative and relevant auditor's report

Enhanced discussions between auditors and audit committees

Improved quality of financial reporting

Considerations for audit committees and management

- What matters could be CAMs?
- How will management and audit committees engage with the auditor as CAMs are identified and the auditor's descriptions of the CAMs are developed and finalized?
- How will the timing of auditor communications with management and the audit committee accommodate the discussion of CAMs?
- How do the auditor's statements regarding CAMs compare to management's disclosures regarding the same matters?

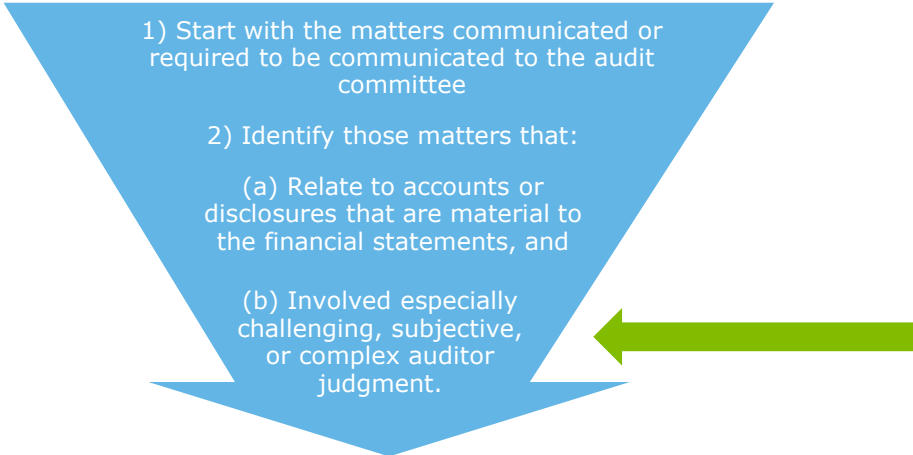
Challenges and opportunities

Describing CAMs in a succinct and understandable manner

Early engagement between the auditor and the audit committee regarding CAMs

Additional time likely needed to finalize the auditor's report (depending on complexity of matters that are CAMs)

Steps the Auditor Takes to Identify CAMs:

- 1) Start with the matters communicated or required to be communicated to the audit committee
 - 2) Identify those matters that:
 - (a) Relate to accounts or disclosures that are material to the financial statements, and
 - (b) Involved especially challenging, subjective, or complex auditor judgment.
- 

For each CAM identified, the following must be communicated in the auditor's report:

- Identify the CAM,
- Describe the principal considerations that led to the auditor's determination that the matter is a CAM,
- Describe how the CAM was addressed in the audit, and
- Refer to the relevant financial statement accounts or disclosures that relate to the CAM

Factors to be taken into account when determining whether a matter involved especially challenging, subjective, or complex auditor judgment:

- a. The auditor's assessment of the risks of material misstatement, including significant risks;
- b. The degree of auditor judgment related to areas in the financial statements that involved the application of significant judgment or estimation by management, including estimates with significant measurement uncertainty;
- c. The nature and timing of significant unusual transactions and the extent of audit effort and judgment related to these transactions;
- d. The degree of auditor subjectivity in applying audit procedures to address the matter or in evaluating the results of those procedures;
- e. The nature and extent of audit effort required to address the matter, including the extent of specialized skill or knowledge needed or the nature of consultations outside the engagement team regarding the matter;
- f. The nature of audit evidence obtained regarding the matter.
- g. Other factors specific to the audit.

CAM Dry Runs

Wesley Bricker, SEC Chief Accountant, has stated that "dry runs can help auditors and audit committees plan for meaningful information specific to the audit to be included in the audit report." (See *Remarks before the AICPA National Conference on Banks & Saving Institutions*, September 17, 2018)

Objectives of a dry run are to perform the following one year in advance of the standard taking effect:

- Identify CAMs
- Draft CAMs
- Discuss CAMs with company management and the audit committee.

About Deloitte

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as "Deloitte Global") does not provide services to clients. In the United States, Deloitte refers to one or more of the US member firms of DTTL, their related entities that operate using the "Deloitte" name in the United States and their respective affiliates. Certain services may not be available to attest clients under the rules and regulations of public accounting. Please see www.deloitte.com/about to learn more about our global network of member firms.

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.