

IAASB CAG Meeting Observation Memo

Hybrid/New York, March 7-8, 2023

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*Disclaimer: The observer applies his own judgment in identifying and communicating matters of public interest and due process at the meeting, and is responsible to the PIOB Technical Committee in doing so and in reporting on the observation. The views and opinions expressed in this Observation Memo are personal and belong solely to the observer and do not necessarily reflect or preclude the PIOB Board's position.*

Summary of key issues from the meeting:

The IAASB CAG meeting was held in a hybrid format, on March 7-8, 2023, at the IFAC offices, in New York, USA. Approximately half of the group was at the meeting in person with the rest joining by video conference. The meeting was chaired by the IAASB CAG Chair. The meeting ran very smoothly and allowed for the active participation of all attendees.

The agenda (public sessions) was as follows:

- B – GOING CONCERN
- C – ASSURANCE ON SUSTAINABILITY REPORTING
- D – FRAUD
- G – ISA FOR LCEs
- H – LISTED ENTITY AND PUBLIC INTEREST ENTITY (PIE)
- I – AUDIT EVIDENCE AND STRATEGY & WORK PLAN 2024-2027
- J – TECHNOLOGY

B - GOING CONCERN

Objective of the project: to revise ISA 570 (Revised), *Going Concern*, to promote consistent practice and behavior to address risks of going concern (GC), establish more robust evaluation of management's assessment of GC and strengthen communication and reporting of related GC matters. The IAASB plans to approve the exposure draft in March 2023 and will request input from the CAG on the proposed exposure draft (ED).

After the December 2022 meeting, the IAASB decided to delay the finalization of the GC project to ensure the best prioritization of its resources and to align it with the completion of the Fraud project. The IAASB expects now to finalize the project in June 2025.

### IAASB CAG Key Discussion Points

CAG members weighed in on the proposed exposure draft. The comments focused on improvements in the auditors' evaluation of management's assessment of going concern and communications with management and those charged with governance. In general, the CAG members were supportive of the ED.

### Public Interest Issues

I said that the ED should be welcomed and that it is in the public interest. Especially the requirements for a more robust evaluation of management's assessment of going concern and the transparency in the auditor's report. I suggested that users of financial information are interested in those situations where the conclusion is that the going concern assumption is appropriate, but that it was a "close call". Given that no changes have been made to the guidance in the ED, I recommended that the IAASB consider how to appropriately communicate users of the financial statements relevant and decision useful information in order to address the expectation gap.

## C - ASSURANCE ON SUSTAINABILITY REPORTING

Objective of the project: the IAASB is developing a standard for assurance on sustainability reporting with the aim to support the consistent performance of quality sustainability assurance engagements. The standard is expected to be suitable for all sustainability topics and disclosures, neutral from a reporting framework and assurance providers perspective.

The CAG was provided with an update and a report back including the objectives of the overarching standard, the PIF qualitative characteristics which are being considered for its development (i.e. scalability, timeliness, comprehensiveness, enforceability, implementability, relevance), how priority areas have been addressed (e.g. limited vs. reasonable assurance, relevance and reliability of information to be used as evidence, internal control system, qualitative and quantitative factors to consider for materiality, definitions, quality management, reporting).

### IAASB CAG Key Discussion Points

There was general support from the CAG as to the direction of the IAASB Task Force (TF) on this project. Some of the topics that were explored included limited assurance vs. reasonable assurance vs. agreed upon procedures. There was discussion as to how the project will address “greenwashing”. There was a discussion about the use of forward- looking information in sustainability disclosures and how that may affect the assurance providers’ work. There was discussion about the importance of internal controls over sustainability reporting and how that may impact the work of the assurance provider. The CAG had a good discussion about how to apply materiality in these types of engagements and that practical guidance will be important. The TF is proposing that assurance providers have a system of quality management that is akin to ISQM 1 or its equivalent. There was discussion as to how that will be applied. The TF is proposing that auditors be not required to report KAMs in sustainability reporting, though they are open to other points of view.

### Public Interest Issues

I recognized the impressive progress that the TF has made on this project. The approach that the TF has taken is consistent with the public interest including timeliness, being reporting framework agnostic and being assurance provider neutral. With respect to KAMs, I suggested that an ED could include questions for respondents about the use of KAMs in sustainability reporting and how that could be useful to users of this information. Finally, given that this is new territory for the IAASB, I suggested that they begin to think about the types of information they would like to gather from assurance providers after the final statement is issued. This will be useful to assurance providers in gathering implementation data for the IAASB to assess.

### D - FRAUD

Objective of the project: enhance and clarify the role and responsibilities of the auditor in relation to fraud in an audit of financial statements. Enhancement of ISA 240 and conforming and consequential amendments to other ISAs.

The Working Group presented a number of topics, including: professional skepticism, specific fraud-related procedures to journal entries, audit documentation, identifying and assessing the Risk of Material Misstatements (ROMMs), fraud and suspected fraud, transparency in the auditor’s report on fraud.

Examples of the TF’s proposals include:

- Professional skepticism: needed throughout the audit. Introduction of a requirement to perform additional audit procedures when fraud, suspected fraud or alleged fraud is identified. Additional procedures built on principles of

ISA 500 (e.g. not biased towards corroborative information or excluding contradictory information; consider all audit evidence obtained).

- Audit documentation: some enhancements (e.g. discussion among engagement team includes fraud risk factors identified), and some new proposals (e.g. fraud or suspected fraud identified, audit procedures performed, professional judgment made, conclusions reached).

When fraud or suspected fraud is identified, the TF had already proposed that the auditor evaluate whether the Risk of Material Misstatements (ROMMs) due to fraud is still appropriate; design and perform additional procedures to obtain additional audit evidence; determine whether control deficiencies exist; determine which additional responsibilities the auditor may have, due to law, regulations and ethical requirements (including NOCLAR in ISA 250); communicate with TCWG about fraud or suspected fraud; consider other implications for the audit (e.g. implications on the auditor's opinion on the financial statements, management's integrity, reliability, etc.).

Transparency options in the auditor's report were discussed in December 2022, with the IAASB concluding that the same filter as in ISA 701 (KAMs) should be used, applicable only to listed entities, and that fraud-related matters should be reported under the KAM section of the auditor's report. The IAASB also concluded that no communication is required in the auditor's report on significant deficiencies of internal controls that are relevant to the prevention and detection of fraud. In the TF's proposals, a specific sub-heading in KAMs should describe fraud-related KAMs, and a reference to the relevant disclosures in the financial statements should be provided, as well as how the ROMMs was addressed in the audit.

#### IAASB CAG Key Discussion Points

The CAG had a good discussion of the matters presented by the TF. There was discussion about the scalability of the fraud procedures for smaller audits. There was a request that the ED describe practical examples of "suspected fraud". There was support for the enhanced documentation requirements, but also a recognition that it is important to change auditor mindset and behaviors related to fraud and suspected fraud. There was discussion about the transparency of auditors reporting on fraud related matters and a question about what management might be expected to disclose. There was a reminder that the auditor needs to consider their knowledge of the company and its industry in designed and executing fraud procedures.

#### Public Interest Issues

I noted that this project is important to the public interest and has a potential for addressing the expectation gap between what auditors are doing in this area and what users expect auditors to be doing. I reminded the group about the importance of

considering external information, especially contradictory information, in identifying and assessing fraud risks. I also suggested that the TF consider providing guidance about how the auditor could assess internal control deficiencies, especially material weaknesses and significant deficiencies, and any related fraud risks associated with those deficiencies.

## H - LISTED ENTITY AND PUBLIC INTEREST ENTITY (PIE)

Objective of the project: This narrow scope project originated from the IESBA's project to review the definitions of Listed Entity and Public Interest Entities (PIE) in the Code of Ethics, with a key objective to achieve convergence between concepts in the Code and ISAs. The IESBA approved its final pronouncements in the Code in December 2021 (approved by the PIOB in April 2022).

The IAASB approved a project proposal to address PIE matters in its March 2022 meeting which is being developed in two phases or tracks:

- Track 1 (fast moving) addressing transparency of independence requirements applicable to PIEs (with a proposed effective date aligned with IESBA's PIE pronouncement of December 15, 2024) – The IAASB approved an exposure draft (ED) in June 2022 and will discuss feedback in March 2023, with a view to approve the final pronouncement in June 2023. The CAG received an overview of feedback received to the consultation and request comments on proposed direction.
- Track 2 addressing convergence of concepts between the Code and ISAs and other matters, to be finalized by June 2025. The CAG received an update on discussions at the December 2022 IAASB meeting.

### Track 1

The presentation shows an overview of comments received to the ED, with 38 responses, of which 2 from Monitoring Group (MG) members (IOSCO and IFIAR) and CEAOB. As usual, the majority of responses come from the profession (either Professional and Accounting Organizations or Firms).

Key matters discussed were:

- Disclosures in the auditor report (ISA 700 (Revised) and communications to those charged with governance (ISA 260 (Revised)) - There was overall support for the key proposals, that are: i) disclosure in the auditor's report, ii) conditional requirement to disclose in the auditor's report when the differential requirements require public disclosure, and iii) application material to communicate with those charged with governance the application of differential independence requirements. It is noted that both MG members (and CEAOB) preferred an unconditional requirement to disclose in the auditor report and that the revisions to ISA 260 (Revised) were made as requirements rather than application material.

- The TF proposes to keep the proposals unchanged, as it considers that there is enough support for the use of the auditor report and believes the conditional requirement is a proportionate approach. For the revisions to ISA 260 (Revised), the TF considers that the proposals under track 2, discussed in December, will eliminate the concern raised by the MG respondents (elevate to a requirement).
- Interim reviews - There were mixed views about revising ISRE 2400, but if a revision is considered, the majority supported following a similar approach to that of ISA 700 (Revised). In respect to ISRE 2410, IESBA considered the comments to the ED and agreed in February 2023 to retain the scope of the requirement applicable to both audits and reviews, and potentially include a question and answer in the staff Q&A document.
  - The TF proposes to address the revisions to ISRE 2400 (consistent with those proposed now for ISA 700 (Revised)) as part of Track 2. They also acknowledge that a revision to ISRE 2410 has been included as potential project for the next strategy period.

## Track 2

The TF shared the key conclusions agreed by IAASB in December 2022:

- Include in ISA 200 (Revised) and ISQM1 the “overarching objective”, guidelines for establishing “differential requirements” and the list of factors and examples used in evaluating the extent of public interest of an entity developed by IESBA.
- Expand the applicability of existing differential requirements to all PIEs in extant ISAs, with one exception. The TF identified and analyzed all instances where the ISAs or ISQMs provide differential requirements for listed entities and concluded that there would be sufficient basis to expand the differential requirements to all categories of PIEs, except for ISA 720 (Revised), that will be considered at a later stage.
- Adopt the definition of PIE (including application material for local standard setters) in ISQM 1 and ISA 200 (Revised) to ensure convergence of definitions used by IAASB standards and the IESBA Code. They also proposed to replace the definition of *Listed entity* in the Glossary with the definition of *Publicly traded entity* from the Code.

## IAASB CAG Key Discussion Points

The CAG had a good discussion on the topics presented. In general, there was support for including transparent communications with those charged with governance. Also, there was general support for the direction of Track 2 of the project.

## Public Interest Comments

With respect to Track 1, the proposals in the ED, and primarily the requirement to use the auditor's report as the mechanism to achieve the public disclosure required by the Code, are in the public interest. An unconditional requirement could achieve greater consistency across the globe, but we acknowledge the arguments supporting conditional disclosures.

With respect to Track 2, I noted that the description of the project is in the public interest and we look forward to seeing the detailed proposals. Regarding the extension of the existing differential requirements in the ISAs and ISQMs to all PIEs (and not limiting it only to listed or publicly traded entities), it is also in the public interest as it meets the heightened expectations on the audits of these type of entities, that require, among other, greater communication with TCWG and transparency with users of the audit report.

#### G - ISA for LCEs

Objective of the project: to develop a stand-alone ISA for audits of financial statements of LCEs. In response to the comments to the ED and feed-back gathered at the international conference in May 2022, the IAASB had previously discussed specific parts of the ISA for LCEs. The ED for Part 10 (Group Audits) was approved in December 2022 and is currently open for comments (due in May 2023). At the IAASB meeting in March, the TF will propose remaining parts revised/redrafted of the standard. The CAG was provided with an update and its input will be requested on specific areas.

The TF's presentation summarized the main changes occurred to the ISA for LCEs since the last CAG discussion. Among these: revisions in the Authority to prohibit the application of the standard in case of involvement of Component Auditors (CAs), except in limited circumstances (i.e. when physical presence of CAs is needed for specific group audits procedures); group specific qualitative characteristics in addition to LCEs characteristics; revisions related to the proportionality of the standard (e.g. in terms of documentation requirements); simplification and more clarity in the understanding of the entity's system of internal controls, combined identification and assessment of Risk of Material Misstatements (ROMMs). Based on the feed-back received, accounting estimates (which will be discussed at the March IAASB meeting), are now proposed to be included in the scope of the standard. The approach followed by the TF's proposals aims at reducing complexity of requirements, allowing the use of ISA for LCEs when the entity has a small number of "more complex" accounting estimates.

#### IAASB CAG Key Discussion Points

There was discussion about the level of documentation required by the LCE proposal. The proposal does not require an engagement letter that describes that the audit will be performed in accordance with the ISA for LCE. Some concern was expressed that this should be transparent with management and should be documented in working papers.

### Public Interest Comments

I expressed support for this project as it has the potential of driving consistency in the audit execution of LCEs and eliminate the fragmentation that currently exists in the audits of these entities. I also recommended that a final standard clarify that not all entities are auditable and provide guidance to auditors when the lack of controls or other factors may make an audit more difficult.

#### I - AUDIT EVIDENCE AND STRATEGY & WORK PLAN 2024-2027

The CAG received a report back on the Audit Evidence project and the Strategy & Work Plan.

Audit evidence: The IAASB approved the exposure draft in September 2022 and the ED is open for comments until April 2023.

Strategy and Work Plan 2024-2027: The IAASB revised the draft Consultation Paper (CP) on the IAASB's Strategy and Work Plan for 2024-2027 with feedback received in September and approved it in December for public consultation (open for comments until April 2023).

#### J - TECHNOLOGY

Objective of the project: to enable the IAASB to be prepared for technology disruption transforming audit and assurance and demonstrate how it can respond (with standard setting or non-authoritative guidance) to support audit and assurance quality.

The CAG was provided with an update on the activities undertaken by the Technology WG.

The Presentation to the CAG included the actions from the Digital Advisory Group, including identifying current standards which need to address and include technology; investigating opportunities to integrate technologies into the standards and how to make them more digital.



The presentation included a diagram on the level of maturity of different technologies used in Audit and Assurance, associated with the usage/impact at auditor's, entity's or both level (e.g. cybersecurity is in a growth stage, with a significant impact on both auditor's and entity's level).

Technology adoption in audit and assurance was described through three different factors: 1) person (e.g. skills and training, mindset, culture, budget and time pressure); 2) task (e.g. tools to complement professional judgment, automation replacing repetitive tasks); 3) environment (e.g. investment in technologies, audit firm innovation, perception of stakeholders about audit quality benefits of technology).

### IAASB CAG Key Discussion Points

The CAG had a good discussion about the survey results presented by the working group and was very intrigued by the proposed "thought experiments" that the Working Group would be performing over the coming months. It was noted that this project is likely to be evergreen, as new technologies are emerging. It was expressed that this is important to the future relevance of the effective auditing.

### Public Interest Issues

I acknowledged the importance of this project such that the IAASB is aware of the impact of new technologies on the development of data, the audit of that data and the consumption of the data.