

Summary of Clarified Auditing Reporting Standards



The AICPA's Auditing Standards Board (ASB) has redrafted all of the auditing sections in *Codification of Statements on Auditing Standards* (contained in *AICPA Professional Standards*). The overall goal of this landmark, multiyear project of the ASB is to make the standards easier to read, understand, and implement and to converge them with the International Standards on Auditing (ISAs). Although the purpose of redrafting the auditing standards is for clarity and convergence and not to create additional requirements, auditors will need to make some adjustments to their audit procedures as a result of this project. New requirements may affect interim testing and other fieldwork and some mandate changes to the report.

This brief provides a summary of the clarified reporting standards. AU-C section 700, *Forming an Opinion and Reporting on Financial Statements*; AU-C section 705, *Modifications to the Opinion in the Independent Auditor's Report*; and AU-C section 706, *Emphasis-of-Matter Paragraphs and Other-Matter Paragraphs in the Independent Auditor's Report* (AICPA, *Professional Standards*), include auditor report changes describing management's responsibility, the use of headings, and the introduction of the two new terms: *emphasis-of-matter* and *other-matter paragraphs*, which replace the term *explanatory paragraph*.

Under the clarified reporting standards, the auditor considers AU-C section 700 when the auditor is forming an opinion and issuing an auditor's report in connection with an audit of financial statements. AU-C sections 705 and 706 address how the form and content of the auditor's report are affected when the auditor expresses a modified opinion (qualified, adverse, or disclaimer of opinion) or includes an emphasis-of-matter or other-matter paragraph in the auditor's report. AU-C section 800, *Special Considerations—Audits of Financial Statements Prepared in Accordance With Special Purpose Frameworks*, and AU-C section 805, *Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts, or Items of a Financial Statement* (AICPA, *Professional Standards*), provide special considerations in the application of generally accepted auditing standards (GAAS) (including AU-C sections 700, 705, and 706) when financial statements are prepared in accordance with a special purpose framework or when there is an audit of a single financial statement or of a specific element, account, or item of a financial statement. AU-C section 810, *Engagements to Report on Summary Financial Statements* (AICPA, *Professional Standards*), addresses the auditor's responsibilities when undertaking an engagement to report on summary financial statements derived from financial statements audited by that same auditor.

AU-C Section 700

AU-C section 700 addresses the auditor's responsibility to form an opinion on the financial statements as a whole. Paragraphs .13–.18 provide the requirements for what an auditor should do in order to form that opinion and therefore it forms a base from which the other reporting standards will build upon. AU-C section 700 also addresses the form and content of the auditor's report issued as a result of an audit of financial

statements and is written in the context of a complete set of general purpose financial statements, prepared in accordance with a fair presentation framework. Paragraphs .19–.21 of AU-C section 700 discuss the form of opinion and when the auditor should modify the opinion in accordance with AU-C section 705. AU-C section 700 specifically addresses situations when the auditor would be expressing an unmodified opinion on the financial statements and establishes the basic form of the auditor’s report. AU-C section 700 also includes requirements and application material related to auditing and reporting on comparative financial statements.

AU-C Section 705

AU-C section 705 addresses the auditor’s responsibility to issue an appropriate report in circumstances when, in forming an opinion in accordance with AU-C section 700, the auditor concludes that a modification to the auditor’s opinion on the financial statements is necessary. AU-C section 705 defines a modified report to include a qualified or adverse opinion or a disclaimer of opinion. Paragraphs .07–.16 of AU-C section 705 provide the auditor with requirements for determining the type of modification to the auditor’s opinion.

AU-C section 705 addresses the issuance of a qualified, adverse, or disclaimer of opinion using the auditor’s judgment about the materiality of the matters giving rise to the modification and the pervasiveness of their effects or possible effects on the financial statements.

Nature of Matter Giving Rise to the Modification	Auditor’s Judgment About the Pervasiveness of the Effects or Possible Effects on the Financial Statements	
	Material but Not Pervasive	Material and Pervasive
Financial statements are materially misstated	Qualified opinion	Adverse opinion
Inability to obtain sufficient appropriate audit evidence	Qualified opinion	Disclaimer of opinion

AU-C Section 706

AU-C section 706 addresses circumstances when the auditor considers it necessary or is required to include additional communications in the auditor’s report that are not modifications to the auditor’s opinion.

AU-C section 706 describes an emphasis-of-matter paragraph as a paragraph included in the auditor’s report that is required by GAAS or is included at the auditor’s discretion. An emphasis-of-matter paragraph refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor’s professional judgment, is of such importance that it is fundamental to users’ understanding of the financial statements. An other-matter paragraph is a paragraph included in the auditor’s report, that is required by GAAS, or is included at the auditor’s discretion, and that refers to a matter other than those presented or disclosed in the financial statements that, in the auditor’s professional judgment, is relevant to users’ understanding of the audit, the auditor’s responsibilities, or the auditor’s report.

The number and nature of emphasis-of-matter and other-matter paragraphs included in the auditor’s report is not expected to change from current practice.

Special Purpose Frameworks

AU-C section 800 addresses special considerations in the application of AU-C sections to an audit of financial statements prepared in accordance with a special purpose framework. AU-C section 800, along with AU-C section 805 and AU-C section 806, *Reporting on Compliance With Aspects of Contractual Agreements or Regulatory Requirements in Connection With Audited Financial Statements*, superseded AU section 623 *Special Reports* (AICPA, *Professional Standards*). The reporting elements in AU-C sections 800, 805, and 806 all build upon AU-C sections 700, 705, and 706.

Terminology Changes

The ASB has made various changes to the language from superseded AU section 508, *Reports on Audited Financial Statements* (AICPA, *Professional Standards*), to harmonize with the language used in the ISAs. The following table lists some of those changes:

<i>Superseded Term</i>	<i>Clarified Term</i>
Standard report	Term not used because we refer to the opinion and not the report
Clean opinion / unqualified opinion	Unmodified opinion
Explanatory paragraph	Emphasis-of-matter paragraph or other-matter paragraph (as applicable)
Explanatory language	Additional communication

Note: Superseded guidance allows a matter to be emphasized before or after the opinion paragraph. AU-C section 706 requires both the emphasis-of-matter and other-matter paragraphs to always follow the opinion paragraph (with the emphasis-of-matter paragraph placed before the other-matter paragraph).

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