



May 15, 2018

Mr. Mike Glynn  
Audit and Attest Standards  
American Institute of Certified Public Accountants  
1211 Avenue of the Americas  
New York, NY 10036-8775

**RE: Proposed Statement on Auditing Standards, *The Auditor's Responsibilities Relating to Other Information Included in Annual Reports***

Dear Mr. Glynn:

We appreciate the opportunity to comment on the Proposed Statement on Auditing Standards, *The Auditor's Responsibilities Relating to Other Information Included in Annual Reports* (the "proposed SAS").

We acknowledge the Auditing Standards Board's (ASB) strategic objective to converge its standards with those of the International Auditing and Assurance Standards Board (IAASB), while avoiding unnecessary differences between the ASB's standards and those of the Public Company Accounting Oversight Board (PCAOB). However, before making changes to existing AU-C sections to converge with new or revised International Standards on Auditing (ISAs), the ASB should ensure it has considered the basis for decisions made in developing existing ASB standards, the comparable PCAOB standard, and the potential implications given the US regulatory and legal environment.

While we support the ASB's goal of narrowing the gap between the auditor's role and responsibilities under the applicable standards and the expectations of audit report users, we have significant concerns with the approach in the proposed SAS and do not support the ASB moving forward with it as currently drafted. It is important to base the ASB's standard on what auditors can reasonably be expected to achieve regarding "other information" reported by the company within the overall context of the audit of the financial statements. As the linkage between other information and information in the audited financial statements becomes less direct, the auditor's ability to identify potential "misstatements of the other information" is reduced. In addition, proposing a new requirement for the auditor to report on other information in the auditor's report risks exacerbating the expectations gap that currently exists.

We also believe alignment between the standards for public and private companies in the US remains appropriate. Moving ahead with the proposed SAS as currently drafted would be a significant departure from the current PCAOB standard, AS 2710.<sup>1</sup> While the PCAOB proposed revisions to AS 2710 in 2013, based on the nature of the comments received, the PCAOB is "reevaluating whether there is a need to revise the standards in this area."<sup>2</sup>

Our response to the PCAOB's 2013 proposal, and the feedback from the profession,<sup>3</sup> expressed significant concern about the potential implications of the expanded auditor responsibilities and the proposed form of reporting in the US legal environment. We believe those concerns are equally relevant to the ASB's

<sup>1</sup> PCAOB AS 2710, *Other Information in Documents Containing Audited Financial Statements*

<sup>2</sup> PCAOB Standard Setting Update, Office of the Chief Auditor, at p. 6-7 (March 21, 2018).

<sup>3</sup> See PwC and CAQ response letters to PCAOB Release No. 2013-005.



proposed SAS. The ASB should consider whether it would be more effective to wait for the resolution of these significant concerns in the standard for public company audits before moving ahead with the proposed SAS.

If the ASB believes it is necessary to move forward in the near term, we believe revisions to the proposed SAS could be made to achieve the intended outcomes while helping to reduce unintended consequences. We urge the ASB to carefully consider the feedback it receives on the exposure draft and revise the proposed SAS accordingly.

Our detailed responses to the questions posed in the exposure draft are included in Appendix 1. Appendix 2 includes suggested revisions to the proposed SAS we believe would be necessary to respond to our concerns. The following summarizes our more significant concerns with the proposed SAS.

*New definition of a “misstatement of the other information”*

We do not support the proposed change from “material inconsistency” and “material misstatement of fact” to a broader concept of a “[material] misstatement of the other information.” We believe the incorporation of new terminology (and changes to the related performance requirements) will cause practical challenges and potentially increase confusion about the auditor’s responsibilities for other information that is not directly related to, or derived from, the financial statements (referred to hereafter as “nonfinancial other information”).

We are fundamentally concerned with the new definition of a “misstatement of the other information,” which expands the auditor’s role to require consideration of whether nonfinancial other information is incorrectly stated or otherwise misleading (including because it omits or obscures information necessary for a proper understanding of the matter). Paragraph A12 of the proposed SAS appropriately explains “the auditor is not responsible for searching for omitted information or for the completeness of the other information.” We believe an auditor performing a financial statement audit pursuant to ASB standards often will not have a sufficient basis for determining whether nonfinancial other information is incorrectly stated or otherwise misleading. Given the diverse types of nonfinancial other information that may be addressed in the other information, (1) there are often no standards or framework against which to assess the presentation of such information, including its completeness, and (2) the auditor may not have the expertise to assess the validity of statements made in relation to matters unrelated to the audit of the financial statements. The PCAOB explicitly acknowledges these limitations in AS 2710 with respect to nonfinancial other information.<sup>4</sup>

To overcome these practical challenges, we suggest the ASB retain the terminology from AU-C section 720 and PCAOB AS 2710 rather than aligning with the ISA terminology. The distinction between a “material inconsistency” when dealing with other information that is related to the financial statements and a “material misstatement of fact” related to nonfinancial other information is understood in practice today, and using different terms acknowledges the difference in the auditor’s responsibility with regard to each category of information. Since the intent is to strengthen the auditor’s work effort in relation to the two

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<sup>4</sup> Paragraph .05 of PCAOB AS 2710 acknowledges the following in relation to a material misstatement of fact: “... the auditor should consider that he may not have the expertise to assess the validity of the statement, that there may be no standards by which to assess its presentation, and that there may be valid differences of judgment or opinion. If the auditor concludes he has a valid basis for concern he should propose that the client consult with some other party whose advice might be useful to the client, such as the client’s legal counsel.”



types of other information, this should be accomplished by changing the performance requirements instead of changing the terminology.

#### *Knowledge obtained in the audit*

We have concerns with the proposed changes to the objectives in paragraph 11 and the requirement in paragraph 15b in relation to explicitly considering whether there is a material inconsistency between the other information and “the knowledge obtained in the audit in the context of audit evidence obtained and conclusions reached in the audit.” The auditor can bring the knowledge obtained as part of the audit to bear when reading and considering the other information and considering whether there is a material misstatement of fact - but there are limits to what is practically achievable and reasonable to expect. While we understand these changes are intended to result in an “intelligent read” of the other information, they will result in a number of practical challenges. We believe further clarification would be needed regarding the following to help auditors consistently apply the requirement:

- The auditor’s procedures, including risk assessment procedures, are designed to enable the auditor to obtain audit evidence that is sufficient and appropriate to provide a basis for the auditor’s opinion on the financial statements as a whole, not to obtain audit evidence regarding other information. Paragraph 3 of the proposed SAS notes appropriately that the auditor is not required to obtain audit evidence beyond that required to form an opinion on the financial statements. However, we are concerned reference to the knowledge obtained in the audit seems to include *all* information gathered during an audit, not just the information subject to audit procedures or information necessary to conduct the audit. For example, paragraph A36 of the proposed SAS refers to matters arising from the auditor’s risk assessment, and paragraphs A35 and A37 give specific examples of other matters, including those that are prospective in nature. Many procedures performed during the course of an audit involve formal and informal interactions with company personnel who provide context necessary to understand, for example, which types and pieces of information are relevant to the financial statements. Information learned during this process that does not appear relevant to the financial statements may not be perceived as noteworthy and/or may not be documented in the auditor’s workpapers. For this reason, it will be challenging—particularly with respect to information received by the auditor significantly prior to its receipt of the draft annual report—for the auditor to determine whether he or she has obtained information during the course of the audit relevant to other information in a company’s annual report.
- We believe the proposed SAS could be viewed as requiring the auditor to make an explicit determination about whether any knowledge obtained during the audit related to the financial and nonfinancial matters described in the other information. It is unclear what procedures the auditor may need to perform in order to determine whether a material inconsistency or material misstatement of fact exists if the information in the audit file does not agree to the other information.
- The further the other information is removed from being related to the audited financial statements, the greater the likelihood that it is unrealistic and impracticable for an auditor to be able to determine that a *misstatement* of the other information exists, even based on the knowledge obtained in the audit. However, because the proposed SAS nevertheless requires the auditor to make such a determination despite limited information and expertise, auditors may be inappropriately held responsible for any subsequently detected omission in that information.



- If the auditor does not identify a material misstatement within the nonfinancial other information, it would not be reasonably possible to determine whether the auditor (1) did not obtain the knowledge that would have enabled them to identify the material misstatement, or (2) obtained the information but did not document such knowledge in the workpapers. In the first instance, it may not have been necessary for the auditor to obtain information about the particular matter if it was not relevant to the audit. Similarly, in the second instance, it may not have been necessary for the auditor to document the information if it was not relevant to the audit. We are therefore concerned that the proposed SAS could drive unnecessary documentation if it is not clear where the boundaries are in relation to considering knowledge obtained in the audit and how audit documentation is to be used.

### *Reporting*

We understand the ASB's intent to provide greater transparency in the auditor's report about the nature of the auditor's responsibilities through this proposed SAS and other changes as part of the wider Auditor Reporting project. However, we believe the reporting on other information as proposed is ambiguous and susceptible to a wide array of interpretation by users. Practical challenges also arise because what constitutes an annual report differs among companies, and companies frequently do not finalize their annual reports until well after the auditor's report has been issued. We note the proposed language in the auditor's report would only be included when some or all of the other information has been received as of the date of the auditor's report – which means the desired transparency may often not be achieved.

We do not believe providing an affirmative statement or conclusion with respect to the other information is appropriate in light of: (1) the limited procedures required by the proposed SAS and (2) the practical limitations on the auditor's ability to review the other information (e.g., the auditor lacks subject-matter expertise to assess nonfinancial other information; the auditor may not be able to review other information received late in the reporting cycle). Describing the auditor's effort with regard to other information in a separate section of the auditor's report, in our view, could give this information undue prominence and suggest a greater level of assurance regarding other information than the auditor can provide. We are also concerned with the placement of the section immediately following the Basis for Opinion in the illustrative reports.

We considered the alternative of including a description of the auditor's responsibilities relating to other information in the auditor's report instead of stating a conclusion at a point in time. We thought this might help mitigate the practical challenges relating to delayed receipt of other information, while still providing relevant information about what would occur if the auditor were to become aware of a material inconsistency with the audited financial statements, a material misstatement of fact in the other information, or both. In pursuing this alternative, we found it difficult to summarize the work effort in the auditor's report in a way that did not imply a greater degree of effort than is required by the proposed SAS. We also noted potential practical challenges of requiring a standardized description in the auditor's report if the other information had not been received as of the date of that report. For example, management could ultimately decide not to issue other information, and the required language provided in the auditor's report describe responsibilities that had not been performed.

The potential benefit of providing transparency about the auditor's responsibilities relating to other information is recognized when there is a consistent framework and requirements for annual reporting, including specified timing (e.g., the Form 10-K for public companies). Absent this, articulating



requirements for reporting in a way that not only provides useful information but can be consistently implemented across companies becomes quite challenging.

We recommend the ASB reconsider whether enhanced reporting is necessary in this area. We believe today's requirement for the auditor to include an Other Matter paragraph when a material inconsistency is identified and the other information has not been corrected remains appropriate. This requirement could also be extended to circumstances in which a material misstatement of fact is identified and the other information has not been corrected.

*Cost/benefit considerations*

The explanatory memorandum to the exposure draft states the proposed SAS will "benefit users of audited financial statements and other information ... by increasing the value of the audit, without changing its scope..." We believe the proposed SAS will result in a significant increase in audit effort, particularly with respect to nonfinancial other information, with a corresponding significant increase in costs that, in our view, will exceed the benefits. It is unclear whether there is demand from users of private company financial statements for this additional effort and we are concerned with the practical challenges of the proposed SAS. We believe the changes we propose in Appendix 2 would better align the costs of implementing the proposed SAS with the benefits.

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We appreciate the opportunity to express our views and would be pleased to discuss our comments or answer any questions you may have. Please contact Jay D. Brodish, Jr. at (973) 236-4043 regarding our submission.

Sincerely,

A handwritten signature in cursive script that reads "PricewaterhouseCoopers LLP".

PricewaterhouseCoopers LLP



## Appendix 1

### **Specific Request for Comment 1 – Scope of documents required to be subjected to the auditor’s procedures**

There is already significant variability in terms of the types of documents that a company may issue that may or may not meet the definition of an annual report. We agree it is helpful to propose a more robust definition of an annual report and incremental guidance in the proposed SAS. However, we do not support expanding the auditor’s responsibilities beyond documents containing the audited financial statements to documents that accompany the audited financial statements or incorporate them by reference. For example, we think it would be impracticable to require the auditor to perform procedures in accordance with the proposed SAS if the auditor’s report accompanies a report on debt covenants.

We believe the material in paragraph A4 of the proposed SAS should be included in the scope section of the proposed SAS rather than the application material.

In addition, the proposed SAS should highlight that both AU-C sections 925<sup>5</sup> and 945<sup>6</sup> establish responsibilities for reading certain documents other than annual reports. However, it is unclear how the reporting requirements included in the proposed SAS might apply to these documents. We believe it will be necessary to make conforming amendments to these standards to clarify whether the proposed SAS would be applicable.

See paragraphs 9, 10 and 14 in Appendix 2 for our suggested edits to the proposed SAS.

### **Specific Request for Comment 2 – Determining which documents constitute the entity’s annual report**

We understand the rationale behind the proposed requirement in paragraph 13, and support actions to promote an upfront understanding of what constitutes an annual report for the engagement based on its nature and purpose, as well as when it will be made available to the auditors. However, the reporting requirements applicable to private companies vary greatly, and thus management may not always be aware whether an annual report will be produced (e.g., whether those charged with governance intend to do so). Similarly, the scope and contents of annual reports can vary greatly, and thus management may not be in a position to confirm the documents that will encompass the annual report during the early stages of the audit. Such determinations may occur significantly after the date of the auditor’s report. In these circumstances, management may be unable or unwilling to provide written representations regarding the potential issuance of an annual report or its contents at the time the auditor is engaged to audit the financial statements. Accordingly, we are not convinced the level of specificity in paragraph 13 is needed, as it may not be scalable to all entities.

We believe a focus on inquiry – of both management and those charged with governance – would be more appropriate, with written acknowledgment focusing on the need for the annual report to be provided to the auditor prior to its issuance. Application material similar to paragraphs A17-A19, A22 and A26 may be helpful to address matters related to the expected timing and nature of information to be included in the annual report in the engagement letter or other written communication. Doing so could ensure

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<sup>5</sup> AU-C section 925, *Filings with the U.S. Securities and Exchange Commission Under the Securities Act of 1933*

<sup>6</sup> AU-C section 945, *Auditor Involvement with Exempt Offering Documents*



management is aware of the auditor’s obligations in accordance with the proposed SAS and agrees to provide the other information to the auditor on a timely basis before it is issued.

We believe it is necessary to reconsider certain application material to ensure the proposed SAS is clear as to the types of information that may be included in an annual report (paragraphs A5-A11), as well as to be explicit about what documents do not constitute an annual report. Finally, we believe it would be helpful to clarify guidance in paragraphs A8 and A23 of the proposed SAS to explain how electronic availability may influence the auditor’s work effort.

See paragraphs 15-16 in Appendix 2 for our suggested edits to the proposed SAS.

**Specific Request for Comment 3 – Work effort, proposed definitions and guidance in relation to the auditor’s consideration of omitted or obscured information**

*Proposed definitions*

As highlighted in our cover note, we do not support the proposed change from “material inconsistency” and “material misstatement of fact” to a broader concept of a “[material] misstatement of the other information” for a number of reasons.

We are concerned that there is no framework against which the auditor can consider the other information (in particular, nonfinancial other information) to evaluate whether the other information is misleading, particularly in light of the auditor’s lack of subject-matter expertise regarding certain nonfinancial other information. The guidance in paragraph A49, which supports the requirement in paragraph 17, does not adequately explain how the auditor can conclude whether or not a material misstatement exists sufficient to support a conclusion in the auditor’s report.

Further, the exposure draft references that “in many cases there may be no applicable framework that includes a discussion of the concept of materiality as it applies to the other information.” Under the existing standards, materiality is developed in the context of the financial statements as a whole (AU-C 320.10). The definition of materiality included within AU-C 320.10 encompasses the financial statements, but not the other information included within an annual report. Decisions related to the materiality of other information are often subjective judgments made by management (with the recommendation of counsel), as well as other stakeholders with whom we have no contact.

Moving towards a focus on “knowledge obtained in the audit,” coupled with new reporting on the other information in the auditor’s report, could increase the expectations gap and mislead users as to the auditor’s responsibilities. In many cases, the auditor would not have been required to obtain knowledge in the audit about certain matters that are discussed in the other information - which is why we believe the more narrow concept of a “material misstatement of fact” remains appropriate.

We also note the concept of materiality with respect to other information is not well-defined. The ASB should clarify whether the intent is for auditors to use the materiality calculated for the financial statements, or if the ASB intends for the auditor to establish a separate materiality level for purposes of assessing the other information in accordance with the proposed standard.

See paragraph 14 of Appendix 2 for our suggested edits to the proposed SAS.



### *Omitted information*

We are concerned with the intent articulated in *Specific Request for Comment 3* that the auditor will be expected to challenge statements “included in (or omitted from) the other information that are inconsistent with the audited financial statements or the auditor’s knowledge obtained as part of the audit.” While paragraph A12 of the proposed SAS explains “the auditor is not responsible for searching for omitted information or for the completeness of the other information,” it is unclear how the auditor determines if there is nonfinancial information that has been omitted that would make the other information misleading. We do not find the remaining guidance in paragraphs A12-A13 that addresses whether information omits or obscures a proper understanding of the matters disclosed to be helpful. We believe these concepts will be difficult to apply in practice, particularly in relation to nonfinancial information or matters in the annual report the auditor would not reasonably be expected to know based on the audit.

### *Work effort*

We believe it is important for the ASB to differentiate the expected effort an auditor would need to apply to (1) other information directly related to or derived from the financial statements and (2) nonfinancial other information. We are particularly concerned with the new requirement in paragraph 16 that would require the auditor to remain alert for indications that other information not related to the financial statements or the auditor’s knowledge obtained in the audit appears to be misstated. There is potentially a wide variety of such nonfinancial and non-audit-related other information, and we think it will be difficult for auditors to understand what is intended by the phrase “appears to be materially misstated.”

Our suggested edits in paragraphs 15-21 of Appendix 2 are intended to address these concerns, while at the same time exploring how the auditor’s work effort could be enhanced, as follows:

- Grounding the proposed SAS in the extant terminology of material inconsistency and material misstatement of fact, with the latter concept relating to nonfinancial other information.
- Requiring the auditor to perform procedures on other information directly related to the audited financial statements, with a focus on selected amounts or other items that are intended to be the same as, to summarize, or to provide greater detail about amounts or other items in the financial statements (incorporating elements of paragraphs A30-A32).
- Explaining that the auditor’s consideration of a material inconsistency relates to whether such information, or the manner of its presentation, is materially inconsistent with information, or the manner of its presentation, appearing in the audited financial statements (incorporating elements of paragraphs A33-A34).
- Explaining that the auditor would recalculate the amounts in other information when the formula is described in the annual report, the formula is generally understood, or the recalculation can be performed without referring to a formula.
- Reframing the concept in the proposed SAS that the auditor should “remain alert” for indications that other information not related to the financial statements or the auditor’s knowledge obtained during the audit appears to be materially misstated. We believe the extant concept of a material misstatement of fact could be retained, by promoting the concept that the auditor should remain



alert for indications that the other information not directly related to the financial statement contains a material misstatement of fact. In this instance, we believe the auditor would be making this consideration based on the auditor’s knowledge gained in the course of conducting the audit, as done in practice today. Appropriate guidance to explain how the auditor can leverage the knowledge gained in the audit could be developed to support this new requirement (e.g., guidance as to the extent that procedures performed in the audit to support the auditor’s opinion may provide relevant information in relation to considering material misstatements of fact (incorporating elements of par. A40-A44)). However, the proposed SAS should also emphasize the auditor may not have the expertise to assess the validity of certain statements in the other information in a manner similar to AS 2710.

- Removing requirements and guidance that set out an expectation for the auditor to consider omitted or obscured information, in the absence of a framework for annual reports for private companies.
- Suggesting explicit potential actions when the auditor determines either the other information needs to be corrected or the financial statements are materially misstated. Notwithstanding these suggestions, we remain concerned with placing incremental responsibility on the auditor to “seek to have the uncorrected material misstatement appropriately brought to the attention of anyone in receipt of the financial statements and the auditor’s report.” This approach is incremental to existing obligations to consider this circumstance in the context of AU-C section 560.

See paragraphs 18-24 in Appendix 2 for our suggested edits to the proposed SAS.

#### **Specific Request for Comment 4 – Guidance for group auditors**

We expect the group auditor to read the other information in its entirety, even in the limited situations when responsibility for the audit is divided. We believe this is consistent with practice today. In such circumstances, we would expect the group auditor to request the other auditor to read the other information and perform the procedures included in the proposed SAS to the extent matters in the other information relate to the part of the audit performed by the other auditor. We believe the guidance in paragraph A38 could explain this.

However, we are concerned that the need for this guidance results from the practical challenges of introducing both a requirement to consider knowledge obtained in the audit, as well as an affirmative statement in the auditor’s report. Should other requirements change in response to our concerns, paragraph A28 could be deleted.

#### **Specific Request for Comment 5 – Reporting**

As highlighted in our cover note, we have fundamental concerns with the ASB moving ahead with its reporting proposals. We believe the reporting as proposed will increase the expectations gap by requiring language in the auditor’s report that is ambiguous and susceptible to a wide array of interpretation by users - in particular, when compared with the nature and extent of the auditor’s effort set out in the proposed SAS.

The proposed other information paragraph of the auditor’s report includes the statement “...or otherwise appears to be materially misstated” in reference to other information not related to the financial



statements or the auditor's knowledge obtained in the audit. We do not think users will understand the limited nature of the procedures the auditor would perform on this type of other information based on the way the reporting has been drafted (i.e., remain alert to whether such information appears to be materially misstated).

Our concerns in relation to reporting can be illustrated when considering the list of matters that may be in other information as described in paragraph A15 of the proposed SAS. A company could include in its annual report a statement that its system of internal control was operating with no deficiencies, but in a financial statement only audit for a non-public company we would not have a sufficient basis to form a conclusion on this statement. We may have assessed some of the controls for operating effectiveness, and thus, might have knowledge to assess if management's statement was accurate for those controls, but we would be unable to fully consider the statement to determine if this statement is a material misstatement of fact or whether the other information is materially misstated. Based on how the reporting is drafted in the proposed SAS, it is likely users might interpret the auditor's statement that there is nothing to report as concurrence with management's statement on the control environment.

We believe today's requirement for the auditor to include an Other Matter paragraph when a material inconsistency is identified and the other information has not been corrected remains appropriate. This requirement could also be extended to circumstances in which a material misstatement of fact is identified and the other information has not been corrected. Finally, the ASB could consider whether greater specificity in terms of the required Other Matter paragraph would be useful (e.g., a required heading such as *Other Information Accompanying the Audited Financial Statements*).

See paragraph 23 of Appendix 2 for our suggested edits to the proposed SAS.

### *Multiple Reports*

Confusion may arise to the extent that the financial statements and the auditor's report are included within multiple documents by a company if a discrete conclusion on other information is included in our report. Application guidance in paragraph A21 acknowledges, but does not provide a solution to, the fact that "there may also be circumstances in which the company's annual report is a combination of documents, each subject to different requirements or reporting practice by the company with respect to the timing of their release."

Further clarification is necessary in particular if the auditor is required to expressly identify the other information in the auditor's report. Additionally, as a practical challenge, to the extent the financial statements and auditor's report are subsequently included in a separate document (e.g., an exempt securities offering) the auditor's report may need to be reissued to remove reference to the previous annual report or to potentially reference the exempt securities offering. We are concerned there is no guidance in the proposed SAS to address implications for the dating and potential reissuance of the auditor's report.

Finally, we believe there are practical challenges with the suggestion in paragraph A59 of providing transparency when other information has not been obtained as of the date of the auditor's report, and suggest this guidance be removed.



## **Documentation**

We believe the proposed other information standard should provide incremental guidance on the nature and extent of required documentation to support the requirement in paragraph 25. Our recommendations to limit the auditor's incremental procedures to other information directly related to the audited financial statements should reduce the audit effort compared to what is currently proposed. Nonetheless, it still presents greater involvement by the auditor regarding other information than is required under the extant standard. If the proposed SAS is finalized as it is currently proposed, we believe it is even more essential that documentation guidance be provided to clarify what is expected to demonstrate compliance with the work effort and support the auditor's conclusion as to whether a material misstatement of the other information exists.

## **Availability of other information**

In our experience, some but not all of the annual report may not be available to the auditor at the date of the auditor's report. Companies frequently do not finalize their annual reports until well after the auditor's report has been issued. Accordingly, the nature and extent of what is included in the annual report may evolve until its issuance. As a result, we question whether the expectation in paragraph 6 of the proposed SAS is appropriate. It may be preferable to provide guidance that the auditor would instead apply AU-C 560.<sup>7</sup>

There may be additional practical challenges in reporting. For example, if only some of the information included in an annual report is available as of the date of the auditor's report, in accordance with the proposed SAS the auditor would identify what has been received. When a company expects to issue an annual report but it is not made available to the auditor prior to the date of the auditor's report, the auditor's report would not include any reference to the auditor's responsibilities relating to other information or conclusion thereon. The differences in reporting may not be well-understood by users of the report.

## **Effective date**

We believe the proposed SAS needs significant revision before it could be effectively implemented and achieve its intended objectives, and may require re-exposure before it can be finalized. For this reason, we are of the view the proposed effective date (for audits of financial statements for periods beginning on or after June 15, 2019) will prove challenging.

Additionally, we are supportive of the ASB making all of the provisions related to auditor reporting effective at the same time. Because we are concerned that that underlying changes in the performance requirements set out in the proposed SAS will require more time to implement, we suggest the suite of standards currently under revision become effective no sooner than for periods ending on or after December 15, 2020.

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<sup>7</sup> AU-C section 560, *Subsequent Events and Subsequently Discovered Facts*



## Appendix 2

The following represents suggestions as to how the proposed SAS could be revised to address the concerns we express in this letter. Changes are shown in underline and strikethrough. Suggestions in relation to potential changes in application material are shown beneath the requirements in brackets and italics.

### Introduction

#### Scope of This Proposed SAS

1. This proposed Statement on Auditing Standards (SAS) addresses the auditor's responsibilities relating to other information, whether financial or nonfinancial information (other than financial statements and the auditor's report thereon), included in an entity's annual report. An entity's annual report may be a single document or a combination of documents that serve the same purpose.

*[No change to the requirement. We suggest par. A1 be relocated to support par. 13.]*

2. This proposed SAS also may be applied, adapted as necessary in the circumstances, to other documents to which the auditor, at management's request, devotes attention.

*[No change to the requirement. With respect to par. A2, we believe it is potentially complicated for the proposed reporting requirement to apply in these circumstances.]*

3. This proposed SAS is written in the context of an audit of financial statements by an independent auditor. Accordingly, the objectives of the auditor in this proposed SAS are to be understood in the context of the overall objectives of the auditor as stated in paragraph .12 of AU-C section 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards*. The requirements in the standards are designed to enable the auditor to achieve the objectives specified in the standards, and thereby the overall objectives of the auditor.

*[Elements of this paragraph moved to the following paragraph.]*

- ~~4~~7. The auditor's responsibilities under this proposed SAS do not constitute an assurance engagement on other information or impose an obligation on the auditor to obtain assurance about the other information. The auditor's opinion on the financial statements does not cover the other information, and the auditor has no responsibility for determining whether such information is properly stated or for performing procedures to corroborate other information beyond the procedures required by paragraphs 18-19 of this proposed SAS. ~~nor does it~~ This proposed SAS does not require the auditor to obtain audit evidence beyond that required to form an opinion on the financial statements.

*[We suggest reordering to further explain the context of the auditor's responsibilities. Changes include language from par. 1 of extant AU-C section 720 to better clarify the auditor's responsibilities, in particular given our concerns over nonfinancial other information, and incorporation of language from AS 2710 that clarifies the limits to the auditor's responsibilities.]*



54. This proposed SAS requires the auditor to read and consider the other information of which the auditor is aware because ~~other information that is materially inconsistent with the financial statements or the auditor's knowledge obtained in the audit may indicate that there is a material misstatement of the financial statements or that a material misstatement of the other information exists, either of which may undermine the credibility of the audited financial statements and the auditor's report thereon~~ may be undermined by material inconsistencies between the audited financial statements and other information.

*[Changes to include language from par. 1 in extant AU-C section 720, and also reinstate the use of extant terminology.]*

65. Other information may include amounts or other items, including qualitative statements, that are intended to be the same as, to summarize, or to provide greater detail about amounts or other items in the audited financial statements and other amounts ~~or other items about which the auditor has obtained knowledge in the audit.~~ Other information may also include other matters.

*[Changes to remove the concept of knowledge obtained in the audit from the scope section.]*

76. The auditor's responsibilities relating to other information (other than applicable reporting responsibilities) in accordance with this proposed SAS apply regardless of whether the other information is obtained by the auditor prior to or after the date of the auditor's report.

*[See comments on availability of other information in Appendix 1. We believe this premise that the auditor's responsibilities are the same when the information is obtained after the date of the auditor's report departs from the concept in AU-C 720 today that AU-C 560 would apply.]*

8. Law or regulation may impose additional obligations on the auditor in relation to other information that are beyond the scope of this proposed SAS.

*[No changes proposed.]*

9. This proposed SAS also addresses other information for which a designated accounting standard setter<sup>1</sup> has issued standards or guidance regarding the format to be used and content to be included when such information is voluntarily presented in an annual report—for example, GASB Statement No. 44, *Economic Condition Reporting: The Statistical Section*.

<sup>1</sup> Designated accounting standards setter is defined in paragraph .04 of AU-C section 730, Required Supplementary Information.

*[Propose elevating the guidance in par. A4 to the introduction for clarity.]*

10. Other AU-C sections explain how this proposed SAS is to be applied with respect to information in certain documents other than annual reports, including:
- AU-C section 925, *Filings with the U.S. Securities and Exchange Commission Under the Securities Act of 1933*.
  - AU-C section 945, *Auditor Involvement with Exempt Offering Documents*.

*[Propose elevating the guidance in par. A3 to the introduction for clarity. Reference also should be made to AU-C section 945.]*



- ~~119.~~ This proposed SAS does not apply to supplemental information addressed by AU-C section 725, *Supplementary Information in Relation to the Financial Statements as a Whole*, or required supplementary information addressed by AU-C section 730, *Required Supplementary Information*.

*[No change]*

### **Effective Date**

- ~~1240.~~ This proposed SAS will be effective for audits of financial statements for periods beginning on or after June 15, 2019.\* Early implementation is not permitted.

\* This proposed effective date is provisional but will not be earlier than June 15, 2019.

*[See feedback on effective date in Appendix 1.]*

### **Objectives**

- ~~1341.~~ The objectives of the auditor, ~~having read the other information,~~ are as follows:

- a. To read and consider whether (i) there is a material inconsistency between the other information included in a company's annual report and the audited financial statements and (ii) the other information contains a material misstatement of fact
- ~~b. To consider whether there is a material inconsistency between the other information and the auditor's knowledge obtained in the audit~~
- ~~be. To respond appropriately, when the auditor identifies that such material inconsistencies appear to exist, or when the auditor otherwise becomes aware that other information appears to be materially misstated d. including, where applicable, To reporting in accordance with this proposed SAS~~

*[Changes to explicitly refer to the annual report, as well as remove the concept of knowledge obtained in the audit from the objectives and to incorporate extant terminology, consistent with changes proposed to the definitions and requirements.]*

### **Definitions**

- ~~1442.~~ For purposes of the auditing standards, the following terms have the meanings attributed below:

**Annual report.** A document, or combination of documents, prepared typically on an annual basis by management or those charged with governance in accordance with law, regulation, or custom, the purpose of which is to provide owners (or similar stakeholders) with information on the entity's operations and the entity's financial results and financial position as set out in the financial statements. An annual report contains, ~~accompanies, or incorporates by reference~~ the financial statements and the auditor's report thereon and usually includes information about the entity's developments, its future outlook and risks and uncertainties, a statement by the entity's governing body, and reports covering governance matters. Annual reports include annual reports of



governments and organizations for charitable or philanthropic purposes that are available to the public.

*[We suggest deleting the concepts of accompanying the financial statements or incorporating them by reference, as explained in response to Question 1 in Appendix 1. Suggest linking par. A5-A11 to the requirement in par. 13, rather than to the definition.]*

**Misstatement of the other information.** A misstatement of the other information exists when the other information is incorrectly stated or otherwise misleading (including because it omits or obscures information necessary for a proper understanding of a matter disclosed in the other information).

**Inconsistency.** Other information that conflicts with information contained in the audited financial statements. A material inconsistency may raise doubt about the audit conclusions drawn from audit evidence previously obtained and, possibly, about the basis for the auditor's opinion on the financial statements.

**Misstatement of fact.** Other information that is unrelated to matters appearing in the audited financial statements that is incorrectly stated or presented in the annual report. A material misstatement of fact may undermine the credibility of the annual report.

*[Changes to revert to extant terminology and remove new term in light of concerns with the manner in which the definition is articulated.]*

**Other information.** Financial or nonfinancial information (other than financial statements and the auditor's report thereon) included in an entity's annual report, excluding required supplemental information.<sup>FN</sup>

<sup>FN</sup> Required supplementary information is defined in paragraph .04 of section 730, *Required Supplementary Information*.

*[Changes to make explicit reference to required supplemental information in the same manner extant AU-C 720 and to align with par. 9 of the proposed SAS]*

## Requirements

### Obtaining the Other Information

13. The auditor should do the following:
  - a. Determine, through discussion with management, and obtain management's written acknowledgment regarding, which document or documents compose the annual report, and the entity's planned manner and timing of the issuance of such documents.
  - b. Make appropriate arrangements with management to obtain in a timely manner and, if possible, prior to the date of the auditor's report, the final version of the document or documents composing the annual report.
  - c. When some or all of the documents determined in (a) will not be available until after the date of the auditor's report on the financial statements, request management to provide a written



representation that the final version of the documents will be provided to the auditor when available, and prior to the document's issuance by the entity, such that the auditor can complete the procedures required by this proposed SAS.

15. The auditor should make inquiries of management and those charged with governance to determine whether an annual report is required or otherwise planned to be issued and, if so, the nature of information to be included in the annual report and expected timing of its issuance.
16. The auditor should make appropriate arrangements with management or those charged with governance to obtain the annual report prior to the report release date, and obtain written acknowledgment that the annual report will be provided to the auditor before its issuance. If it is not possible to obtain the annual report prior to the report release date, the auditor should read such information as soon as practicable.
- 17~~14~~. If the auditor becomes aware that the entity did not provide the auditor with the final version of documents determined in accordance with paragraph 13a to be part of the annual report prior to the issuance of those documents to third parties, the auditor should take appropriate action.

*[See Specific Request for Comment 2 in Appendix 1. Changes to focus on inquiries to understand management's plans, as well as any plans those charged with governance may have to issue documents that may meet the definition of an annual report, reflecting language in par. 7 of the extant standard, with written acknowledgment to confirm management and those charged with governance are aware they need to make the annual report available to the auditor prior to its issuance. We suggest linking the guidance in par. A5-A11 to this requirement, continuing to include guidance on the types of information that may be included in an annual report, as well as being explicit about what documents do not constitute an annual report for purposes of the SAS.]*

#### **Reading and Considering the Other Information When the Other Information Is Obtained Prior to the Date of the Auditor's Report**

- ~~15. The auditor should read the other information and do the following:~~
  - ~~a. Consider whether there is a material inconsistency between the other information and the financial statements. As the basis for this consideration, the auditor should, to evaluate their consistency, compare selected amounts or other items in the other information (that are intended to be the same as, to summarize, or to provide greater detail about the amounts or other items in the financial statements) with such amounts or other items in the financial statements.~~
  - ~~b. Consider whether there is a material inconsistency between the other information and the auditor's knowledge obtained in the audit, in the context of audit evidence obtained and conclusions reached in the audit.~~
18. The auditor should read the other information, and with respect to other information directly related to the audited financial statement, perform the following additional procedures:
  - a. Compare selected amounts and qualitative statements in the other information, and the consistency of the manner of their presentation, that are the same as, or provide greater detail



about, the amounts in the financial statements, to (1) the amounts in the audited financial statements, or (2) accounting records that are subject to the audit, or have been derived directly from such accounting records by analysis or computation.

- b. Recalculate the mathematical accuracy of the amounts in the other information that are calculated using amounts in (1) the other information, (2) the audited financial statements, or (3) accounting records that are subject to the audit, or have been derived directly from such accounting records by analysis or computation.

~~19~~<sup>16</sup>. While reading the other information in accordance with paragraph ~~18~~<sup>15</sup>, the auditor should remain alert for indications that the other information not directly related to the audited financial statements potentially contains a material misstatement of fact based on the auditor's knowledge gained in the course of conducting the audit in the context of the audit evidence obtained ~~not related to the financial statements or the auditor's knowledge obtained in the audit appears to be materially misstated.~~

*[See Specific Request for Comment 3 in Appendix 1. Suggestions are intended to differentiate efforts in relation to nonfinancial other information and information derived from the audited financial statements and reintroduce the concept of a material misstatement of fact. Existing application material could be restructured and further refined to explain how the auditor considers other information that is directly related to the financial statements, and how the auditor may gain knowledge in the course of conducting the audit in relation to nonfinancial other information, retaining material that highlights the limitations and challenges in doing so. For example, care should be taken not to overemphasize the matters in par. A36, given the auditor's understanding in performing risk assessment procedures is for the purpose of assessing risks, not for the purpose of considering whether other information is correctly stated.]*

*Additional guidance to support par. 15b would be helpful to explain the auditor would recalculate the amounts when the formula is described in the annual report, the formula is generally understood, or the recalculation can be performed without referring to a formula. Amounts, such as totals or percentages, that are calculated using simple mathematical operations, such as addition or division, ordinarily can be recalculated without referring to a formula. If the auditor needs to refer to a formula for the recalculation of an amount, the auditor would be required to recalculate the amount only when the formula is provided or described in the annual report. However, the auditor would not be required to evaluate the appropriateness or sufficiency of the formula used in the calculation.]*

**Responding When a Material Inconsistency Appears to Exist or Other Information Appears to Contain a Material Misstatement of Fact ~~be Materially Misstated~~**

~~20~~<sup>17</sup>. If the auditor identifies that a material inconsistency between the audited financial statements and other information directly related to the audited financial statements appears to exist or the other information appears to contain a material misstatement of fact ~~(or becomes aware that the other information appears to be materially misstated)~~, the auditor should discuss the matter with management and, if necessary, perform other procedures to consider ~~conclude~~ the following:

- ~~a~~<sup>b</sup>. Whether a material misstatement of the financial statements exists



ba. Whether a material inconsistency or a material misstatement of ~~fact the other information~~ exists

e. ~~Whether the auditor's understanding of the entity and its environment needs to be updated~~

*[See Specific Request for Comment 3 in Appendix 1. Suggestions to simplify, concept of the understanding of the entity and its environment subsumed in par. 19. Additional guidance to explain considerations related to material misstatements of fact would be helpful to highlight the limitations of the auditor's expertise and the possible need for the auditor to obtain legal advice or suggest the client do so, in particular if the auditor does not have the expertise to assess the validity of certain statements within nonfinancial other information. ]*

### **Responding When a Material Misstatement ~~in~~ of the Financial Statements Exists ~~or the Auditor's Understanding of the Entity and Its Environment Needs to Be Updated~~**

21. If, as a result of performing the procedures in paragraphs ~~18-17~~ ~~20-17~~, the auditor concludes that a material misstatement ~~in~~ of the audited financial statements exists ~~or the auditor's understanding of the entity and its environment needs to be updated~~, the auditor should respond appropriately in accordance with the other SASs, including requesting management to revise the financial statements and considering the implications on the auditor's report.

*[Although the concept of updating the auditor's understanding of the entity and its environment is deleted in the requirements in paragraphs 20-21, par. A57 could be revised to explain if the auditor determines the financial statements are materially misstated it may be an indication this understanding needs to be updated. We also suggest considering additional application guidance about whether the financial statements are or are not subsequently corrected and the potential impact on the auditor's report.]*

### **Responding When the Auditor Continues to Believe ~~Concludes~~ That a Material Inconsistency or a Material Misstatement of Fact ~~the Other Information~~ Exists**

~~22-18~~ 22. If, after performing other procedures as required by paragraph 20, the auditor continues to believe ~~concludes~~ that a material inconsistency or a material misstatement of fact ~~the other information~~ exists, the auditor should request management to correct the other information:

- a. If management agrees to make the correction, the auditor should determine that the correction has been made.
- b. If management refuses to make the correction, the auditor should communicate the matter with those charged with governance and request that the correction be made.

~~23-19~~ 23. If the auditor concludes that a material misstatement exists in other information obtained prior to the date of the auditor's report, and the other information is not corrected after communicating with those charged with governance, the auditor should take appropriate action, including the following:

- a. Include in the auditor's report an other-matter paragraph describing the material inconsistency or material misstatement of fact, in accordance with section 706, *Emphasis-of-Matter Paragraphs and Other-Matter Paragraphs in the Independent Auditor's Report*:



~~Consider the implications for the auditor's report and communicate with those charged with governance about how the auditor plans to address the material misstatement in the auditor's report (see paragraph 23cii);~~

- b. ~~Withhold the auditor's report; or~~
- c. ~~Withdraw from the engagement if withdrawal is possible under applicable law or regulation.~~

### **Reading and Considering the Other Information When the Other Information Is Obtained After the Date of the Auditor's Report**

~~24a. If the auditor obtains the other information after the date of the auditor's report, the auditor should:~~

- a. ~~Perform the procedures in paragraphs 18-22~~
- b. ~~If the auditor continues to believe concludes that a material inconsistency or material misstatement of fact exists in other information obtained after the date of the auditor's report, the auditor should do the following:~~
  - a. ~~— If the other information is corrected, perform the procedures considered necessary in the circumstances.~~
  - b. ~~— If and the other information is not corrected after communicating with those charged with governance, take appropriate action considering the auditor's legal rights and obligations to seek to have the uncorrected material misstatement appropriately brought to the attention of anyone in receipt of the financial statements and the auditor's report.~~

*[See Specific Request for Comment 3 in Appendix 1. Suggestions to simplify the approach and incorporate extant terminology.]*

### **Reporting**

- ~~22. The auditor's report should include a separate section with the heading "Other Information," or other appropriate heading, when, at the date of the auditor's report, the auditor has obtained some or all of the other information.~~
- ~~23. When the auditor's report is required to include an other information section in accordance with paragraph 22, the section should include the following:~~
  - a. ~~— A statement that management is responsible for the other information~~
  - b. ~~— An identification of other information, if any, obtained by the auditor prior to the date of the auditor's report~~
  - e. ~~— A statement that the auditor's opinion does not cover the other information and that the auditor does not express an opinion or any form of assurance on the other information~~



- d. ~~A description of the auditor's responsibilities relating to reading, considering, and reporting on other information as required by this proposed SAS~~
- e. ~~Either~~
  - i. ~~a statement that the auditor has nothing to report or~~
  - ii. ~~if the auditor has concluded that there is an uncorrected material misstatement of the other information, a statement that describes the uncorrected material misstatement of the other information~~

~~24. When the auditor expresses a qualified or adverse opinion in accordance with AU-C section 705, Modifications to the Opinion in the Independent Auditor's Report, the auditor should consider the implications of the matter giving rise to the modification of opinion for the statement required in paragraph 23e.~~

*[See Specific Request for Comment 5 in Appendix 1.]*

#### **Documentation**

- 25. In addressing the requirements of paragraphs .08-.11 of AU-C section 230, *Audit Documentation*, as those requirements apply to this proposed SAS, the auditor should include the following in the audit documentation:
  - a. The procedures performed under this proposed SAS
  - b. The final version of the other information on which the auditor has performed the work required under this proposed SAS

*[See comments on documentation in Appendix 1.]*