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This is one of a series of articles where experts in assurance, reporting and regulatory matters discuss recent technical and policy developments in these areas.



Enhanced auditor reporting – practical ways to deliver insight

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Writing a listed entity's audit report under today's reporting standards is easy, but you'd be pushed to say that it's an exciting read! Fast forward a year and the reader will have the opportunity to gain insight into the focus of the auditor, what they thought was important and what they did about it.

The proposed new auditing standard on "communicating key audit matters"¹ will expand the scope of the audit report for listed entities through the requirement to include key audit matters (KAMs). But will the auditor seize this opportunity to be transparent? Will the reader now understand more about the audit and the auditor? Will the information conveyed be useful?

Writing insightful key audit matters is not easy. Every word counts when you aim to convey a complex message in a few short paragraphs. Maintaining a focus on what is important is critical. How do auditors make sure they grab this opportunity to provide real insights to the reader? How do we avoid swamping readers with detail they either don't need or don't understand (or both)?

The key audit matters give insight into what mattered to the auditor and why, rather than explaining an accounting policy or a risk from the entity's perspective.

¹ ASA 701 Communicating key audit matters in the independent auditor's report is expected to be released in December 2015 and effective for periods ending on or after December 2016.

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What is a key audit matter?

Definition: Key audit matters are those matters that, in the auditor's professional judgement, were of most significance in the audit of the financial report of the current period. Significance can be interpreted in a number of ways

Risk	Judgement	Effect on the audit
Where was the greatest risk of material misstatement? What were the significant audit risks?	What involved the most judgement by the auditor? eg over the persuasiveness of the audit evidence What involved the most judgement by management?	What was the impact on the audit of a significant event or transaction?
This could include matters that were significant by size or nature.	Examples include areas of high estimation uncertainty - such as impairment	This could include acquisitions, disposals, unusual transactions, related party transactions

Impact: Many factors may result in a matter being a key audit matter – whether due to size, nature or the sheer amount of effort that it took to audit. What is most important is how this impacted the audit. When reading the overall auditor's report it is helpful for the reader to understand where the auditor focussed their attention and why.

Context: Amongst matters communicated to the client, the key audit matters are those (in the auditor's view) that are of most significant. They do not include all matters communicated.

Examples: Impairment, asset valuation, litigation, taxation

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Putting it into practice

KPMG in Australia have prepared a number of mock up reports which we have provided in draft to clients. We've outlined a few of the opportunities and pitfalls we experienced.

<p>Lesson 1 – Partner involvement throughout the process is critical</p>	<p>Experience shows that the more involved the engagement partner is in writing the key audit matters, the more useful it is to the reader.</p> <p>As tempting as it may be for an engagement partner to ask the team to write the key audit matters, ultimately it will be the partner who influences the best outcome.</p> <p>It may well be more efficient for the partner to be more actively involved in drafting the report, sharing their insights with their team.</p>
<p>Lesson 2 – Be clear on what to include in a Key Audit Matter paragraph</p> <p>Readers need to know why the auditor thought this was important – it provides the context.</p> <p>The description of what the key audit matter is, reads best when it is focussed and succinct. Being specific to the audit of this entity will avoid boilerplate descriptions.</p> <p>How the auditor addressed the key audit matter should give insight into how they gathered the evidence. No one wants to read a laundry list of everything the auditor did. The auditor may choose to include procedures, findings, observations or a combination.</p>	
<p>Lesson 3 – Be specific</p> <ul style="list-style-type: none"> • About the client • About the key audit matter <p>“When you are more specific about the area of focus the KAM will be easier to read.”</p>	<p>Avoid boilerplate language by being specific about the precise nature of the key audit matter and how it presented itself for this client.</p> <p>Rather than writing about a very general area, e.g. impairment, consider focusing on a specific area where the audit team, including experts spent their time e.g. their consideration of the discount rate.</p>
<p>Lesson 4 - Make the most of the opportunity</p>	<p>The changes to the requirements in the audit report provide the opportunity to provide</p>

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	<p>transparency and insight into what an audit entails. It's an opportunity to demystify the process and demonstrate the independence and scepticism of the auditor.</p> <p>Explain in simple terms the key procedures that provided the best evidence.</p> <p>Consider whether there is an appetite to go beyond the basic requirements of the standard? Inclusion of graphs, group scoping, materiality etc. This may be a big decision for an audit firm and needs buy in from leadership.</p>
<p>Lesson 5 – Don't write for auditors</p> <p>The whole point of the expanded auditor's report is to explain the audit approach to a non-auditor.</p>	<p>Avoid:</p> <ul style="list-style-type: none"> • Descriptions that read like an A-Z guide on how to account for a particular transaction/balance. • Describing the entire audit approach to that matter, the reader is unlikely to be interested in every audit procedure performed. • audit jargon e.g. "completeness and existence of x." <p>Consider asking someone not associated with the audit to read the report. If it doesn't make sense to them, change the terminology, omit it altogether or rephrase.</p>
<p>Lesson 6 – Be consistent</p>	<p>Consider whether the description of the key audit matter matches the approach outlined in the "how you addressed the key audit matter" and vice versa.</p> <ul style="list-style-type: none"> • Is it necessary to describe a procedure when the matter has not been raised as part of the KAM? • Does the description of the key audit matter need to be improved?
<p>Lesson 7 – Be factual, don't exaggerate!</p> <p>It goes without saying; if you describe a procedure, make sure you actually did it!</p>	<p>Avoid inaccurate descriptions. These may imply that the auditor tested every control or looked at every invoice. Consider whether the language used is overstating the reality.</p> <p>Avoid certain words like "audit", "review", "verify" or other phrases that imply conclusions or opinions over a particular area.</p>

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<p>Lesson 8 – Consider your firm’s brand</p> <p>How expansive do you want the auditor’s report to be?</p> <p>How will audit reports present a consistent brand image?</p>	<p>The standard allows a wide range of acceptable key audit matter descriptions that range from providing details about procedures performed to findings and observations. What is your firm trying to achieve? Are firm leaders engaged?</p> <p>With such a wide range of options how will the audit firm achieve a level of brand consistency between reports issued by different partners without resorting to boilerplate templates?</p> <p>Audit firms may wish to consider:</p> <p>Whether to have a small group of partners who review all enhanced audit reports issued by the firm? What expertise and experience should these partners have? Will they have capacity to perform the review at the right time? Who else could review the reports? What role could the Engagement Quality Control Reviewer play in review?</p>
<p>Lesson 9 – it takes time</p>	<p>Don’t under-estimate how long it takes to write key audit matters especially in the first year.</p> <p>Some firms may want to build in branding/risk reviews which may add a little to the timeline.</p> <p>Some clients may be sensitive to certain matters, build this into the process timeline as they may need some time to become comfortable with your descriptions.</p> <p>There will be an impact on total hours/costs – consider how to build this into fee discussions.</p>

Don’t wait until the audit is complete to start drafting the key audit matters. Start writing now, ask relevant peers to give feedback and share your draft with your client.

Steps in communicating key audit matters

