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PCAOB Expands CAMs Guidance

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Last week, the Public Company Accounting Oversight Board published new staff guidance to support implementation of the impending critical audit matters (CAMs) disclosure requirements, which first become effective later this year for audits of fiscal years ending on or after June 30, 2019, for large accelerated filers. (See our July 25, 2018 and October 30, 2017 posts)

The new "Implementation of Critical Audit Matters" guidance consists of three separate documents (a) The Basics, (b) Staff Observations from Review of Audit Methodologies, and (c) A Deeper Dive on the Determination of CAMs (the "Guidance"). "The Basics" document succinctly outlines the basic elements of what constitutes a CAM and the related disclosure requirements, while the latter two documents offer a more granular perspective on specific implementation issues. These documents expand the PCAOB's current set of resources related to recent and upcoming changes to the auditor's report, which are maintained on the PCAOB's "New Auditor's Report" website. While mostly directed to auditors, the Guidance offers some useful insights for companies and their audit committees.

Of particular interest to companies and their audit committees, the Guidance offers some direction for the drafting of CAMs disclosures, which is based on observations from materials submitted by 10 U.S. audit firms to the PCAOB's Office of the Chief Auditor between May 2018 and January 2019. The Guidance does not, however, go so far as to provide an example of "model" CAMs disclosure. (For an example of CAMs disclosure, see the Center for Audit Quality's December 2018 *Lessons Learned, Questions to Consider, and an Illustrative Example* publication) A few of the thematic observations highlighted in the Guidance by the PCAOB staff include:

- *Describing Principal Considerations*. The PCAOB staff observed some CAMs disclosures that simply stated that a matter involved especially challenging, subjective, or complex auditor judgment. Such disclosure, as the Guidance notes, "does not fulfill the requirement of the standard" to include "a clear, concise, and understandable discussion of ***why*** the matter involved especially challenging, subjective, or complex auditor judgment."
- *Describing How a Matter Was Addressed in the Audit*. Similar to describing principal considerations, CAMs disclosure must also include a tailored description of how the CAM was addressed in the audit. In this regard, the PCAOB staff observed some audit firm materials that directed auditors to include a description of general internal control testing in

every CAMs disclosure. While the Guidance does not necessarily object to that approach, it does make clear that auditors “are expected to tailor CAM communications to the audit to avoid standardized language and to reflect the specific circumstances of the matter.”

- *Discussing CAMs with the Audit Committee*. As it relates to the audit committee’s responsibility with respect to CAMs disclosure, the Guidance reiterates that “[a]ny matter that will be communicated as a CAM *should* already have been discussed with the audit committee, and the auditor *is required to provide* a draft of the auditor’s report to the audit committee and discuss the draft with them.” (emphasis added) As the PCAOB staff observed, “[s]ome audit firm methodologies indicated that the auditor would provide draft CAMs for the audit committee’s review and feedback.” In response, the Guidance reminds that while “dialogue regarding CAMs is expected, auditors should remember that CAMs are the responsibility of the auditor—not the audit committee.”

Relatedly, the “Deeper Dive” Guidance document includes a useful set of FAQs that, among other things, shed some light on what to expect when benchmarking CAMs disclosures. Reiterating the principles-based nature of CAMs, the PCAOB staff noted that “differences in auditors’ judgment, as well as in the nature, timing, and extent of the audit response required in the specific circumstances, will influence the determination of CAMs.” For purposes of year-over-year comparison, CAMs can be expected to vary. The Guidance states that while “some matters may be CAMs each year, . . . others may be CAMs in a single period or intermittently.” For instance, the Guidance notes that implementation of a new accounting standard might be a CAM one year but not thereafter. By contrast, the Guidance points to deferred tax asset accounts as an example situation that might give rise to CAMs intermittently, such as in years when additional auditor judgment and effort is required to assess the usability of net operating loss carryforwards.

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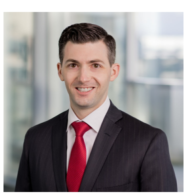

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