
PCAOB Reproposes Enhanced Auditor Reporting Standard

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On May 11, the Public Company Accounting Oversight Board unanimously agreed to repropose a revised auditing standard governing the contents and form of the audit report delivered by registered public accounting firms in their audits of public company financial statements. According to the PCAOB, the new standard "seeks to enhance the form and content of the report to make it more relevant and informative to investors and other financial statement users." The reproposal is the latest development in a process dating back to a 2008 recommendation by the Department of the Treasury's Advisory Committee on the Auditing Profession. Following the 2008 recommendation, the PCAOB issued a concept release in June 2011, which was followed by a proposed standard in August 2013. (See our prior post from [August 2013](#) for a description of the 2013 proposal.) The reproposed standard is contained in a more than 200-page [release](#) and is summarized in a shorter [fact sheet](#).

Similar to the 2013 proposal, the reproposed standard maintains the current "pass/fail" auditor reporting model, but revises the structure and expands the required contents of audit opinions. Most notably, the reproposed standard retains, but narrows the scope of, the prior proposal's requirement that the auditor discuss "critical audit matters" that are identified by the auditor. Unlike the 2013 proposal, the PCAOB has not included any new auditor responsibilities for other information, besides the financial statements, contained in an issuer's annual report on Form 10-K.

Under the reproposed standard, a critical audit matter is a matter arising from the audit that was communicated or required to be communicated to the audit committee and that 1) relates to accounts or disclosures that are material to the financial statements and 2) involved "especially challenging, subjective, or complex auditor judgment." The reproposed standard sets a non-exclusive list of factors that auditors should consider to identify a critical audit matter, including the auditor's assessment of the risks of material misstatement, the degree of auditor subjectivity in determining or applying audit procedures, the nature and extent of audit effort required to address the matter, the degree of auditor judgment involved, the nature and timing of significant unusual transactions, and the nature of audit evidence obtained regarding the matter.

Communicating each critical audit matter in the audit report would include the following:

- identifying the critical audit matter;

- describing the principal considerations that led the auditor to determine that the matter is a critical audit matter;
- describing how the critical audit matter was addressed in the audit; and
- referring to the relevant financial statement accounts and disclosures that relate to the critical audit matter.

Critical audit matters are to be disclosed with respect to the audit of the current period financial statements, though disclosure of critical audit matters regarding the audit of prior periods may be presented in certain other situations, such as IPOs or reaudits. While auditors are not expected to disclose information about the company that has not been made publicly available, the repropose standard notes that such disclosure would be required if "necessary to describe the principal considerations that led the auditor to determine that a matter is a critical audit matter or how the matter was addressed in the audit."

The PCAOB expects that in most audits the auditor would identify at least one critical audit matter, though there might be circumstances in which the auditor determines that there are none. The PCAOB also made clear that the new standard would not change the circumstances in which an auditor would provide a qualified opinion, adverse opinion, or disclaimer of opinion on the financial statements. Critical audit matters would be discussed in a report containing a qualified opinion, but not an adverse opinion or disclaimer of opinion. Similarly, the repropose standard does not affect an auditor's ability to include other "emphasis of matter" or explanatory disclosures in its audit report.

The repropose standard makes other changes to the structure and content of all audit opinions. Among other things, the repropose standard requires the auditor's report to be addressed to the shareholders and the board of directors of the company. Audit opinions would also be required to include the following:

- a statement regarding the auditor's requirement to be independent;
- the phrase "whether due to error or fraud" in the description of the auditor's responsibility under PCAOB standards to obtain reasonable assurance whether the financial statements are free of material misstatements; and
- a statement regarding the auditor's tenure.

According to PCAOB Chair James R. Doty, "This proposal delivers on the intention of Congress to further the public interest in the preparation of more informative audit reports for public investors." The PCAOB did not specify any timetable for further action, though at its May 11 open meeting, PCAOB member Steven B. Harris noted his "hope that, after hearing from all interested parties, [the PCAOB] could vote on a final proposal by the end of the year." The PCAOB has invited comments on the repropose standard, which are due by August 15, 2016. Any new or revised standards adopted by the PCAOB are subject to approval by the Securities and Exchange Commission.

Authors



Alan J. Wilson

PARTNER

✉ alan.wilson@wilmerhale.com

☎ +1 202 663 6474

Thomas W. White

RETIRED PARTNER

☎ +1 202 663 6000