No. 2019-17
Updated 18 May 2020

To the Point

AICPA — final standard

AICPA issues final standard that changes the form and content of the auditor's report

Presenting the auditor's opinion at the front of the report adds visibility and makes the basis of the auditor's opinion more transparent.

What you need to know

- The AICPA issued a new standard that changes the form and content of the auditor's report to increase its informational value and make it more relevant.
- The standard requires auditors to present the "Opinion" section first in their reports, followed by the "Basis for Opinion" section, and to more clearly articulate management's responsibilities for the financial statements and the auditor's responsibilities for the audit.
- The standard requires the auditor to make certain new communications to those charged with governance, including communicating significant risks the auditor identifies.
- The standard establishes new guidance for auditors engaged to communicate on key audit matters, but it does not require communication of key audit matters unless the auditor is engaged to do so.
- The standard is effective for audits of financial statements for periods ending on or after 15 December 2021, and early implementation is permitted. This publication has been updated to reflect the AICPA's decision to delay the effective date by one year due to the COVID-19 pandemic and to allow early implementation.

Overview

The Auditing Standards Board (ASB) of the American Institute of Certified Public Accountants (AICPA) issued a new **Statement on Auditing Standards** (SAS)[1] that significantly changes the form and content of the auditor's report.

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In doing so, the ASB is trying to increase the informational value and relevance of the auditor's report. The standard more closely aligns the AICPA's auditor's reporting standards with those of the Public Company Accounting Oversight Board (PCAOB) and International Auditing and Assurance Standards Board (IAASB).

A notable difference is that the PCAOB standard requires auditors of most public companies to report on critical audit matters, while the AICPA standard requires auditors of private companies to report on key audit matters only when the auditor is engaged to do so.

The SAS also includes amendments to various standards to emphasize the auditor's responsibility to focus on management's financial statement disclosures throughout the audit, improve communications to those charged with governance and enhance the auditor's reporting related to going concern matters.

Key considerations

Form and content of the auditor's report

The standard requires auditors to reorganize their reports and present the "Opinion" section first, followed by the "Basis for Opinion" section. The "Basis for Opinion" section must include a statement that the auditor is required to be independent of the entity and meet the other ethical responsibilities, in accordance with the ethical requirements that relate to the audit.

The "Responsibilities of Management for the Financial Statements" section includes a new paragraph that describes management's responsibility for the evaluation of whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern, when the applicable financial reporting framework requires management to make that evaluation.

In the "Auditor's Responsibilities for the Audit of the Financial Statements" section, auditors must state that the auditor has the following responsibilities:

- Exercise professional judgment and maintain professional skepticism throughout the audit
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures that respond to those risks
- Obtain an understanding of internal control to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control (unless the auditor has a responsibility to express an opinion on the effectiveness of internal control and includes other language specified in the standard)
- Evaluate the appropriateness of the accounting policies used, the reasonableness of significant accounting estimates made by management and the overall presentation of the financial statements
- Conclude whether, in the auditor's judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time

The "Auditor's Responsibilities for the Audit of the Financial Statements" section will also state that the auditor is required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings and certain internal control-related matters that the auditor identified during the audit.

The SAS includes various illustrations of auditor's reports. The appendix of this publication provides an illustration of an auditor's report on comparative financial statements.

The SAS amends the auditing standards to increase the auditor's focus on financial statement disclosures throughout the audit and requires auditors to communicate new information to those charged with governance.

Amended auditing standards

The SAS amends various auditing standards to increase the auditor's focus on financial statement disclosures throughout the performance of the audit. The amendments do not, however, change the responsibilities of the auditor with respect to these disclosures. The ASB also enhanced the application guidance in the auditing standards to assist auditors in assessing risks related to disclosures.

The SAS amends AU-C section 260, *The Auditor's Communications With Those Charged With Governance,* to require the auditor to communicate (1) significant risks identified by the auditor in its overview of the planned scope and timing of the audit and (2) any circumstances that affect the form and content of the auditor's report (e.g., the auditor expects to modify the opinion, the auditor considers it necessary to include an emphasis of matter or other matter paragraph or a separate going concern section in its report).

The SAS also amends AU-C 570, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern,* to require the auditor to include a separate section in the auditor's report with the heading "Substantial Doubt About the Entity's Ability to Continue as a Going Concern" when, after considering identified conditions or events and management's plans, the auditor concludes that there is substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time. This section will draw attention to management's disclosure in the financial statements and state that the auditor's opinion is not modified with respect to the matter. The guidance currently in effect requires the auditor to include an emphasis of matter paragraph about the entity's ability to continue as a going concern, when necessary.

Key audit matters

The SAS creates new guidance for auditors that are engaged to communicate key audit matters, which are defined as matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements and are selected from matters communicated to those charged with governance. The standard does not require auditors to communicate these matters unless they are engaged to do so.

The SAS also provides reporting guidance for audits conducted in accordance with both the standards of the PCAOB and the AICPA when the audit is not within the jurisdiction of the PCAOB. Examples of these situations may include audits of clearing agencies and futures commission merchants registered with the US Commodity Futures Trading Commission (CFTC), as well as other entities registered with the CFTC. When an audit is conducted in accordance with the auditing standards of the PCAOB and the AICPA, the auditor would follow the requirements in the PCAOB standards regarding the determination and reporting of critical audit matters.

Effective date

The SAS is effective for audits of financial statements for periods ending on or after 15 December 2021, and early implementation is permitted. The SAS was originally effective for periods ending on or after 15 December 2020, and early implementation was not permitted. But in response to the COVID-19 pandemic, the AICPA issued **SAS No. 141**[2] to delay the effective date and permit early implementation.

Endnote:

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[1] Statement of Auditing Standards No. 134, *Auditor Reporting and Amendments, Including Amendments Addressing Disclosures in the Audit of Financial Statements.*

[2] Statement of Auditing Standards No. 141, *Amendment to the Effective Dates of SAS Nos. 134-140.*

SCORE No. 06397-191US
(Updated 18 May 2020)

ED None

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Appendix: Example of an auditor's report that complies with the new requirements

The following example of an auditor's report that complies with the SAS is one of several illustrations the ASB provided in the standard. As discussed earlier, the SAS requires the auditor to present its opinion first, followed by the basis for that opinion. To emphasize the new information auditors will be required to include in their reports, we have added shading.

Independent Auditor's Report

[Appropriate Addressee]

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of ABC Company, which comprise the balance sheets as of December 31, 20X1 and 20X0, and the related statements of income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of ABC Company as of December 31, 20X1 and 20X0, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of ABC Company and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about ABC Company's ability to continue as a going concern for [*insert the time period set by the applicable financial reporting framework*].

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users made on the basis of these financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of ABC Company's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about ABC Company's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters identified during the audit.

Report on Other Legal and Regulatory Requirements

[The form and content of this section of the auditor's report would vary depending on the nature of the auditor's other reporting responsibilities.]

[Signature of the auditor's firm]

[City and state where the auditor's report is issued]

[Date of the auditor's report]