

---

---

**STANDING ADVISORY GROUP MEETING**

***AUDITOR'S REPORTING MODEL***

**MAY 18–19, 2016**

---

**Introduction**

On May 11, 2016, the Board issued for public comment *Proposed Auditing Standard—The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion and Related Amendments to PCAOB Standards*, PCAOB Release No. 2016-003 (May 11, 2016) ("reproposed standard"). The reproposed standard is intended to make the auditor's report more relevant and informative to investors and other financial statement users, particularly by including auditor reporting of "critical audit matters," which would provide audit-specific information about especially challenging, subjective, or complex auditor judgments.

The reproposed standard has been informed by comments received on the 2013 proposal,<sup>1</sup> the Board's April 2014 public meeting,<sup>2</sup> analysis of economic considerations, academic research, and international developments. In particular, while the concept of critical audit matters has been carried forward from the 2013 proposal, the reproposed requirements have been narrowed in a number of respects, including by:

- Limiting the source of potential critical audit matters to matters communicated or required to be communicated to the audit committee;
- Adding a materiality component to the definition of critical audit matter;
- Narrowing the definition to only those matters that involved especially challenging, subjective, or complex auditor judgment; and

---

<sup>1</sup> See *Proposed Auditing Standards—The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion; the Auditor's Responsibilities Regarding Other Information in Certain Documents Containing Audited Financial Statements and the Related Auditor's Report; and Related Amendments to PCAOB Standards*, PCAOB Release No. 2013-005 (Aug. 13, 2013) ("2013 proposal" or "proposed standard").

<sup>2</sup> See transcripts and participant statements from the public meeting, available on the Board's website in Rulemaking Docket Matter No. 034, *Proposed Auditing Standards on the Auditor's Report and the Auditor's Responsibilities Regarding Other Information and Related Amendments*.

This paper was developed by the staff of the office of the Chief Auditor as of May 11, 2016, to foster discussion among the members of the SAG. It is not a statement of the Board, nor does it necessarily reflect the views of the Board or staff.

- Revising the related documentation requirement.

In addition, the repropoed communication requirement has been expanded to require the auditor to describe how the critical audit matter was addressed in the audit.

At its May 18–19, 2016 Standing Advisory Group meeting, SAG members will be invited to discuss the repropoed standard, particularly their views regarding key changes to the auditor reporting of critical audit matters, such as:

- Source and definition of critical audit matters;
- Communication requirement for critical audit matters;
- Documentation requirement for critical audit matters; and
- Applicability of the auditor reporting of critical audit matters to various entities.

SAG members are also invited to discuss other elements of the repropoed standard, such as auditor tenure, auditor independence, or other improvements to the existing auditor's report.

This paper includes the following Appendices:

- Appendix I – Summary of the Reproposal (extracted from PCAOB Release No. 2016-003);
- Appendix II – Auditor Reporting of Critical Audit Matters (comparison to the 2013 proposal);
- Appendix III – Additional Improvements to the Auditor's Report (comparison to the 2013 proposal and existing auditor's report); and
- Appendix IV – Determining and Communicating Critical Audit Matters (extracted from PCAOB Release No. 2016-003).

This paper provides only a brief overview of the reproposal and should be read in conjunction with the full reproposal available on the Board's website.<sup>3</sup>

---

<sup>3</sup> PCAOB Release No. 2016-003 in Rulemaking Docket Matter No. 034.

## Appendix I – Summary of the Reproposal

The Board is reproposing the auditor reporting standard, *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion* ("reproposed standard" or "reproposal"). The reproposal would retain the pass/fail model of the existing auditor's report, which is generally acknowledged to be a useful signal as to whether the audited financial statements are presented fairly. Consistent with the Board's statutory mandate to "protect the interests of investors and further the public interest in the preparation of informative, accurate and independent audit reports,"<sup>1</sup> the reproposal also seeks to enhance the form and content of the report to make it more relevant and informative to investors and other financial statement users. In particular, the auditor's report would include a description of "critical audit matters," which would provide audit-specific information about especially challenging, subjective, or complex aspects of the audit as they relate to the relevant financial statement accounts and disclosures.

The reproposal builds on more than five years of Board outreach, in which many investors and other financial statement users have consistently urged the Board to make the auditor's report more relevant and informative. Outside the United States, other regulators and standard setters have also moved toward expanded auditor reporting.

The auditor's report is the primary means by which the auditor communicates information regarding the audit of the financial statements to investors and other financial statement users. As currently designed, however, the auditor's report conveys very little of the information obtained and evaluated by the auditor as part of the audit. And while the auditor's report has generally remained unchanged since the 1940s, companies' operations have become more complex and global, and the financial reporting frameworks have evolved toward an increasing use of estimates and fair value measurements. As part of the audit, auditors often perform procedures involving challenging, subjective, or complex judgments, such as evaluating calculations or models, the impact of unusual transactions, and areas of significant risk. Although the auditor is required to communicate with the audit committee regarding such matters, this information is not known to investors. Given the increased complexity of financial reporting, which requires the auditor to evaluate complex calculations or models and make challenging or subjective judgments, the current form of the auditor's report does little to address the information asymmetry<sup>2</sup> between investors and auditors. This may

---

<sup>1</sup> Section 101(a) of the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley").

<sup>2</sup> Economists often describe this imbalance, where one party has more or better information than another party, as "information asymmetry." As part of the system of financial reporting, the audit of the financial statements helps reduce the information

limit the extent to which the auditor's report can address the information asymmetry between investors and management.

In recent years, many investors and others have stated that auditors should provide additional information in the auditor's report to make the report more relevant and useful.<sup>3</sup> At the same time, other commenters, primarily issuers and accounting firms, have argued that it would be inappropriate for the auditor to provide financial analysis or disclosures on behalf of the company being audited. The reproposed standard is intended to respond to investor requests for additional information about the financial statement audit by increasing the relevance and usefulness of the auditor's report, without imposing requirements beyond the auditor's expertise or mandate.

The communication of critical audit matters would inform investors and other financial statement users of matters arising from the audit that required especially challenging, subjective, or complex auditor judgment, and how the auditor responded to those matters. The Board believes that critical audit matters are likely to be identified in areas that investors have indicated would be of particular interest to them, such as significant management estimates and judgments made in preparing the financial statements; areas of high financial statement and audit risk; unusual transactions; and other significant changes in the financial statements.

In addition to informing investors and other financial statement users about areas of the audit that were especially challenging, subjective, or complex and helping them understand how the auditor addressed these areas, the Board believes that the communication of critical audit matters should help focus investor attention on these matters and provide a new perspective on the financial statements. For instance, additional reporting by the auditor could facilitate analysis of the financial statements and help investors and analysts engage management with targeted questions about critical audit matters. To the extent the identification and communication of critical audit

---

asymmetry investors face by providing an independent opinion about whether the financial statements are presented fairly in all material respects.

<sup>3</sup> See survey, *Improving the Auditor's Report*, which was presented by the working group of the PCAOB's Investor Advisory Group ("IAG") on the Auditor's Report and The Role of the Auditor (Mar. 16, 2011) ("IAG 2011 survey"). See also CFA Institute's *Usefulness of the Independent Auditor's Report Survey Results* (May 4, 2011); *Independent Auditor's Report Survey Results* (Mar. 31, 2010); and *Independent Auditor's Report Monthly Poll Results* (Mar. 12, 2008) ("CFA survey and poll results"). See also transcripts and participant statements from the Board's April 2014 public meeting, available on the Board's website in Rulemaking Docket Matter No. 034, *Proposed Auditing Standards on the Auditor's Report and the Auditor's Responsibilities Regarding Other Information and Related Amendments* ("Docket 034").

matters increases focus by auditors, audit committees, and management on the matters identified as critical audit matters, it may also lead to an incremental increase in audit quality and the quality of information presented in the financial statements and related disclosures.

In addition to critical audit matters, the reproposal includes other improvements to the existing auditor's report under AS 3101 (currently AU sec. 508<sup>4</sup>), *Reports on Audited Financial Statements*, primarily intended to clarify the auditor's role and responsibilities related to the audit of the financial statements and make the auditor's report easier to read.

The reproposed standard would include the following significant changes to the existing auditor's report:

- *Critical audit matters*—would require communication in the auditor's report of any critical audit matters arising from the audit of the current period's financial statements.
  - *Definition of a critical audit matter*—any matter that was communicated or required to be communicated to the audit committee and that:
    - Relates to accounts or disclosures that are material to the financial statements, and
    - Involved especially challenging, subjective, or complex auditor judgment.
  - *Factors in determining critical audit matters*—the auditor would take into account a nonexclusive list of factors in determining whether a matter involved especially challenging, subjective, or complex auditor judgment,

---

<sup>4</sup> In 2015, the PCAOB adopted and the U.S. Securities and Exchange Commission ("SEC") approved the reorganization of PCAOB auditing standards using a topical structure and a single, integrated numbering system. See *Reorganization of PCAOB Auditing Standards and Related Amendments to PCAOB Standards and Rules*, PCAOB Release No. 2015-002 (Mar. 31, 2015); SEC, *Public Company Accounting Oversight Board; Order Granting Approval of Proposed Rules To Implement the Reorganization of PCAOB Auditing Standards and Related Changes to PCAOB Rules and Attestation, Quality Control, and Ethics and Independence Standards*, Exchange Act Release No. 75935 (Sept. 17, 2015), 80 FR 57263 (Sept. 22, 2015). The reorganized amendments will be effective as of December 31, 2016, but may be used and referenced before that date. See PCAOB Release No. 2015-002, at 21.

such as the auditor's assessment of the risks of material misstatement, including significant risks.

- *Communication in the auditor's report*—the auditor would identify the critical audit matter, describe the principal considerations that led the auditor to determine that the matter is a critical audit matter, describe how it was addressed in the audit, and refer to the relevant financial statement accounts and disclosures. If there are no critical audit matters, the auditor would so state in the auditor's report.
- *Documentation*—the auditor would document the basis for its determination of whether each matter that both: (1) was communicated or required to be communicated to the audit committee and (2) relates to accounts or disclosures that are material to the financial statements, involved especially challenging, subjective, or complex auditor judgment.
- *Additional Improvements to the Auditor's Report*
  - *Clarifications of existing auditor responsibilities*—enhance certain standardized language in the auditor's report, including adding a statement about auditor independence and the phrase "whether due to error or fraud," when describing the auditor's responsibilities under PCAOB standards to obtain reasonable assurance about whether the financial statements are free of material misstatements;
  - *Tenure*—add a basic element of the auditor's report related to auditor tenure; and
  - *Standardized form of the auditor's report*—require the opinion be the first section of the auditor's report and require section titles to guide the reader.

The reproposal has been informed by comments received on the 2013 proposal,<sup>5</sup> the Board's April 2014 public meeting,<sup>6</sup> analysis of economic considerations, academic research, and international developments. In particular, while the concept of critical

---

<sup>5</sup> See *Proposed Auditing Standards—The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion; the Auditor's Responsibilities Regarding Other Information in Certain Documents Containing Audited Financial Statements and the Related Auditor's Report; and Related Amendments to PCAOB Standards*, PCAOB Release No. 2013-005 (Aug. 13, 2013) ("2013 proposal" or "proposed standard").

<sup>6</sup> See transcripts and participant statements from the public meeting, available on the Board's website in Docket 034.

audit matters has been carried forward from the 2013 proposal, the repropoed requirements have been narrowed in a number of respects, including by:

- Limiting the source of potential critical audit matters to matters communicated or required to be communicated to the audit committee;
- Adding a materiality component to the definition of critical audit matter;
- Narrowing the definition to only those matters that involved especially challenging, subjective, or complex auditor judgment; and
- Revising the related documentation requirement.

In addition, the repropoed communication requirement has been expanded to require the auditor to describe how the critical audit matter was addressed in the audit. As under the 2013 proposal, the repropoed communication of critical audit matters would not change the auditor's current role of attesting to information prepared by management.

The repropoed standard would generally apply to audits conducted under PCAOB standards. However, unlike the 2013 proposal, communication of critical audit matters would not be required for audits of brokers and dealers reporting under the Securities Exchange Act of 1934 ("Exchange Act") Rule 17a-5; investment companies other than business development companies; and employee stock purchase, savings, and similar plans ("benefit plans").<sup>7</sup>

---

<sup>7</sup> The other requirements of the repropoed standard would be applicable to audits of these types of entities.

**Appendix II – Auditor Reporting of Critical Audit Matters**

Key Area	PCAOB 2013 Proposal	PCAOB 2016 Reproposal	Key Changes in the 2016 Reproposal Compared to the 2013 Proposal
<p><b>CAM Source and Definition</b></p>	<p><i>Source of CAMs</i> - ordinarily are matters of such importance that they are included in the matters required to be (1) documented in the engagement completion document (AS 1215 (currently Auditing Standard No. 3), <i>Audit Documentation</i>); (2) reviewed by the engagement quality reviewer (AS 1220 (currently Auditing Standard No. 7), <i>Engagement Quality Review</i>); (3) communicated to the audit committee (AS 1301 (currently Auditing Standard No. 16), <i>Communications with Audit Committees</i>); or (4) any combination of the three.</p>	<p><i>Source of a CAM</i> – any matter arising from the audit of the financial statements that <u>was communicated or required to be communicated to the audit committee</u>.</p> <p>Note: Required audit committee communications are set forth in PCAOB standards, including AS 1301 (currently Auditing Standard No. 16), <i>Communications with Audit Committees</i>, and Appendix B of that standard which refers to other PCAOB standards.</p>	<p>Narrowed the source of potential CAMs to matters communicated or required to be communicated to the audit committee.</p>
	<p><i>CAMs Definition</i> – those matters the auditor addressed during the audit of the financial statements that (1) involved the most difficult, subjective, or complex auditor judgments; (2) posed the most difficulty to the auditor in obtaining sufficient appropriate evidence; or (3) posed the most difficulty to the auditor in forming an opinion on the</p>	<p><i>CAM Definition</i> – any matter arising from the audit of the financial statements 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,</p>	<ul style="list-style-type: none"> <li>• Added a materiality component to the definition.</li> <li>• Narrowed the definition to those matters that "involved especially challenging, subjective, or complex auditor judgment."</li> <li>• Changed "most" to "especially" and replaced the word "difficult"</li> </ul>

Key Area	PCAOB 2013 Proposal	PCAOB 2016 Reproposal	Key Changes in the 2016 Reproposal Compared to the 2013 Proposal
	<p>financial statements.</p> <p>Note: Use of the word "most" is not intended to imply that only one matter under each criteria would qualify as a critical audit matter. Depending on the facts and circumstances of the audit, there could be several critical audit matters. Also, an audit matter could meet one, two, or all three of the criteria in the definition.</p>	<p>or complex auditor judgment.</p>	<p>with "challenging."</p>
<p><b>Factors Used to Determine CAMs</b></p>	<p>The 2013 proposal included a nonexclusive list of the following factors for the auditor to take into account when determining CAMs:</p> <ul style="list-style-type: none"> <li>a. The degree of subjectivity involved in determining or applying audit procedures to address the matter or in evaluating the results of those procedures;</li> <li>b. The nature and extent of audit effort required to address the matter;</li> <li>c. The nature and amount of available relevant and reliable evidence regarding the matter</li> </ul>	<p>The 2016 reproposal includes a nonexclusive list of factors for the auditor to take into account when determining CAMs:</p> <ul style="list-style-type: none"> <li>a. The auditor's assessment of the risks of material misstatement, including significant risks;</li> <li>b. The degree of auditor subjectivity in determining or applying audit procedures to address the matter or in evaluating the results of those procedures;</li> <li>c. The nature and extent of audit effort required to address the matter, including the extent of</li> </ul>	<ul style="list-style-type: none"> <li>• Retained but combined factors related to the extent of specialized skill or knowledge needed to apply audit procedures and the nature of consultations. – (<i>factors b, g and h in the 2013 proposal; factor c in the 2016 reproposal</i>)</li> <li>• Removed two factors related to the severity of relevant control deficiencies and the nature and significance of related corrected and uncorrected misstatements. – (<i>factors d and f in the 2013 proposal</i>)</li> <li>• Modified the factor related to the auditor's assessment of</li> </ul>

Key Area	PCAOB 2013 Proposal	PCAOB 2016 Reproposal	Key Changes in the 2016 Reproposal Compared to the 2013 Proposal
	<p>or the degree of difficulty in obtaining such evidence;</p> <p>d. The severity of control deficiencies identified relevant to the matter, if any;</p> <p>e. The degree to which the results of audit procedures to address the matter resulted in changes in the auditor's risk assessments, including risks that were not identified previously, or required changes to planned audit procedures, if any;</p> <p>f. The nature and significance, quantitatively or qualitatively, of corrected and accumulated uncorrected misstatements related to the matter, if any;</p> <p>g. The extent of specialized skill or knowledge needed to apply audit procedures to address the matter or evaluate the results of those procedures, if any; and</p> <p>h. The nature of consultations outside the engagement team regarding the matter, if any.</p>	<p>specialized skill or knowledge needed or the nature of consultations outside the engagement team regarding the matter;</p> <p>d. The degree of auditor judgment related to areas in the financial statements that involved the application of significant judgment or estimation by management, including estimates with significant measurement uncertainty;</p> <p>e. The nature and timing of significant unusual transactions and the extent of audit effort and judgment related to these transactions; and</p> <p>f. The nature of audit evidence obtained regarding the matter.</p>	<p>risks of material misstatement by encompassing more broadly the auditor's assessment of risks of material misstatement, including significant risks, rather than just changes in the auditor's risk assessment. – <i>(factor e in the 2013 proposal; factor a in the 2016 reproposal)</i></p> <ul style="list-style-type: none"> <li>• Modified the factor related to the auditor obtaining available relevant and reliable evidence by aligning it with the reproposed definition of critical audit matters, which no longer includes matters that posed the most difficulty to the auditor in obtaining sufficient appropriate evidence, and focusing just on the nature of audit evidence obtained regarding the matter. – <i>(factor c in the 2013 proposal; factor f in the 2016 reproposal)</i></li> <li>• Added the following new factors: <ul style="list-style-type: none"> <li>- The degree of auditor judgment related to areas in the financial statements that involved the application of significant judgment or</li> </ul> </li> </ul>

Key Area	PCAOB 2013 Proposal	PCAOB 2016 Reproposal	Key Changes in the 2016 Reproposal Compared to the 2013 Proposal
			<p>estimation by management, including estimates with significant measurement uncertainty. – <i>(factor d in the 2016 reproposal)</i></p> <ul style="list-style-type: none"> <li>- The nature and timing of significant unusual transactions and the extent of audit effort and judgment related to these transactions. – <i>(factor e in the 2016 reproposal)</i></li> </ul>
<p><b>Communication of CAMs</b></p>	<p>For each critical audit matter communicated in the auditor's report the auditor must:</p> <ol style="list-style-type: none"> <li>a. Identify the critical audit matter;</li> <li>b. Describe the considerations that led the auditor to determine that the matter is a critical audit matter; and</li> <li>c. Refer to the relevant financial statement accounts and disclosures that relate to the critical audit matter, when applicable.</li> </ol>	<p>For each critical audit matter communicated in the auditor's report the auditor must:</p> <ol style="list-style-type: none"> <li>a. Identify the critical audit matter;</li> <li>b. Describe the principal considerations that led the auditor to determine that the matter is a critical audit matter;</li> <li>c. Describe how the critical audit matter was addressed in the audit; and</li> <li>d. Refer to the relevant financial statement accounts and disclosures that relate to the critical audit matter.</li> </ol>	<ul style="list-style-type: none"> <li>• Clarified that the auditor is required to describe only the <u>principal</u> considerations that led the auditor to determine that the matter is a CAM.</li> <li>• Included a new requirement for the auditor to describe how each CAM was addressed in the audit.</li> <li>• Added a note to the communication requirement stating that the auditor is not expected to be the source of original information about the company.</li> </ul>

Key Area	PCAOB 2013 Proposal	PCAOB 2016 Reproposal	Key Changes in the 2016 Reproposal Compared to the 2013 Proposal
		<p>Note: When describing critical audit matters in the auditor's report the auditor is not expected to provide information about the company that has not been made publicly available by the company unless such information is 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.</p>	
<p><b>CAM Documentation</b></p>	<p>To provide sufficient detail for a clear understanding of the conclusions reached regarding the determination of critical audit matters, the audit documentation must contain sufficient information to enable an experienced auditor, having no previous connection with the engagement, to understand the basis for the auditor's determination that (1) each reported matter was a critical audit matter and (2) non-reported audit matters addressed in the audit that would appear to meet the definition of a critical audit matter were not critical audit matters.</p>	<p>The auditor must document the basis for the auditor's determination whether each matter that both:</p> <ol style="list-style-type: none"> <li>a. Was communicated or required to be communicated to the audit committee; and</li> <li>b. Relates to accounts or disclosures that are material to the financial statements</li> </ol> <p>involved especially challenging, subjective, or complex auditor judgment.<sup>22</sup></p> <p><sup>22</sup> Consistent with the</p>	<ul style="list-style-type: none"> <li>• Modified documentation requirement in line with changes to the proposed definition of CAMs</li> <li>• The potential population of matters that may need to be documented has been narrowed because of the revised definition of CAMs.</li> </ul>

Key Area	PCAOB 2013 Proposal	PCAOB 2016 Reproposal	Key Changes in the 2016 Reproposal Compared to the 2013 Proposal
		<p>requirements of AS 1215, the audit documentation should be in sufficient detail to enable an experienced auditor, having no previous connection with the engagement, to understand the determinations made to comply with the provisions of this standard.</p>	
<p><b>Applicability of CAMs</b></p>	<p>Applicable to all entities that are required to have their audits conducted in accordance with standards of the PCAOB.</p>	<p>Communication of critical audit matters is not required for audits of (1) brokers and dealers reporting under Exchange Act Rule 17a-5, (2) investment companies registered under the Investment Company Act of 1940 ("Investment Company Act"), other than companies that have elected to be regulated as business development companies, and (3) employee stock purchase, savings, and similar plans.</p>	<p>Based on consideration of the ownership and reporting characteristics of these entities and the comments received, communication of critical audit matters would not be required for audits of brokers and dealers, investment companies, other than business development companies, and employee stock purchase, savings, and similar plans.</p>
<p><b>Interaction between CAMs and Explanatory Paragraphs</b></p>	<p>Communication of critical audit matters does not alter existing requirements to add explanatory language and that the same matter could be described both in the critical audit matter section and</p>	<p>Critical audit matters are not a substitute for required explanatory language (paragraphs). If a matter that meets the definition of a critical audit matter also requires an explanatory paragraph, such as a</p>	<p>Clarified interaction between critical audit matters and explanatory paragraphs.</p>

Key Area	PCAOB 2013 Proposal	PCAOB 2016 Reproposal	Key Changes in the 2016 Reproposal Compared to the 2013 Proposal
	using explanatory language with a cross-reference, as appropriate.	matter related to going concern, the auditor may include the communication requirements of a critical audit matter in the explanatory paragraph with a cross-reference in the critical audit matter section to the explanatory paragraph. Alternatively, the auditor may choose to provide both an explanatory paragraph and the critical audit matter communication separately in the auditor's report with a cross-reference between the two sections.	
<b>Interaction between CAMs and Emphasis Paragraphs</b>	Communication of critical audit matters does not alter the auditor's ability to add an explanatory paragraph to the auditor's report to emphasize a matter in the financial statements. The auditor's communication of a critical audit matter may provide more information about the auditing aspect of the matter emphasized in the auditor's report.	<p>The reproposed standard retains the ability for the auditor to add a paragraph to the auditor's report to emphasize a matter regarding the financial statements ("emphasis paragraph").</p> <p>Emphasis paragraphs are not required but may be used by auditors to draw the reader's attention to matters, such as significant transactions with related parties and unusually important subsequent events.</p>	Clarified interaction between critical audit matters and emphasis paragraphs in the standard and the release.

Key Area	PCAOB 2013 Proposal	PCAOB 2016 Reproposal	Key Changes in the 2016 Reproposal Compared to the 2013 Proposal
		<p>If a matter that the auditor considers emphasizing meets the definition of a critical audit matter, the auditor would be required to identify the matter as a critical audit matter in the auditor's report and would be subject to the other communication requirements for critical audit matters. The auditor would not be expected to include an emphasis paragraph in the auditor's report about a matter that meets the definition of a critical audit matter.</p>	

**Appendix III – Additional Improvements to the Auditor's Report**

Key Area	PCAOB 2013 Proposal	Changes in PCAOB 2016 Reproposal	Changes from Existing Auditor's Report
<b>Auditor Independence</b>	A statement in the auditor's report that the auditor is a public accounting firm registered with the PCAOB and is required to be independent with respect to the company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the SEC and the PCAOB.	No change from the 2013 proposal.	Aside from the title, "Report of Independent Registered Public Accounting Firm," the auditor's report provides no further information regarding auditor independence.
<b>Addressee</b>	Requirement for the auditor's report to be addressed to: (1) investors in the company, such as shareholders, and (2) the board of directors or equivalent body. <sup>8</sup>  <sup>8</sup> For example, addressees might include other appropriate parties depending on the legal and governance structure of the company.	Requirement for the auditor's report to be addressed to: <del>(1) investors in the company, such as shareholders,</del> and <del>(2) the board of directors,</del> or <u>equivalent body<sup>8</sup> for companies not organized as corporations. The auditor's report may include additional addressees.</u>	<ul style="list-style-type: none"> <li>• Currently, there is no requirement for the auditor's report to be addressed to specific parties.</li> <li>• Under the existing standard, the auditor's report <u>may</u> be addressed to the company whose financial statements are being audited, its board of directors, or stockholders.</li> </ul>
<b>Financial Statement Notes and any Related</b>	A statement indicating that the financial statements, including the related notes and, if applicable,	A statement indicating that the financial statements, including the related notes and, <del>if applicable,</del> <u>any related</u>	Under the existing auditor reporting standard, the notes to the financial statements

Key Area	PCAOB 2013 Proposal	Changes in PCAOB 2016 Reproposal	Changes from Existing Auditor's Report
<b>Schedule(s)</b>	schedules, identified and collectively referred to in the report as the financial statements, were audited.	schedules(s), identified and collectively referred to in the report as the financial statements, were audited.  • No significant change from the 2013 proposal.	and the related schedules are not required to be identified as part of the audited financial statements.
<b>Error or Fraud</b>	A description of the auditor's responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements, <u>whether caused by error or fraud</u> .	No change from the 2013 proposal.	Under the existing auditor reporting standard, the auditor's report is not required to describe the auditor's responsibility related to error or fraud in planning and performing the audit.
<b>Nature of the Audit</b>	The description of the nature of the audit includes:  a. Performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks; b. Examining, on a test basis, appropriate evidence regarding the amounts and disclosures in the financial statements; c. Evaluating the accounting principles used and significant	The description of the nature of the audit includes:  a. Performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks; b. Examining, on a test basis, appropriate evidence regarding the amounts and disclosures in the financial statements; c. Evaluating the accounting principles used and significant estimates	The description of the nature of the audit is retained from the existing auditor reporting standard, but is revised to align it better with the language in the Board's risk assessment standards.

Key Area	PCAOB 2013 Proposal	Changes in PCAOB 2016 Reproposal	Changes from Existing Auditor's Report
	<p>estimates made by management; and</p> <p>d. Evaluating the overall presentation of the financial statements.</p>	<p>made by management; and</p> <p>d. Evaluating the overall presentation of the financial statements.</p> <ul style="list-style-type: none"> <li>• No significant change from the 2013 proposal.</li> </ul>	
<b>Auditor Tenure</b>	<p>A statement in the auditor's report containing the year the auditor began serving consecutively as the company's auditor.</p>	<p>A statement in the auditor's report containing the year the auditor began serving consecutively as the company's auditor;<sup>8</sup></p> <p><sup>8</sup> <u>For an investment company that is part of a group of investment companies, the statement contains the year the auditor began serving consecutively as the auditor of any investment company in the group of investment companies. See Section 12(d)(1)(G)(ii) of the Investment Company Act.</u></p> <ul style="list-style-type: none"> <li>• No significant change from the 2013 proposal.</li> <li>• Provided clarification regarding applying the auditor tenure disclosure to investment companies.</li> </ul>	<p>The auditor is not required to disclose the auditor tenure in the auditor's report.</p>
<b>Form of the Auditor's Report</b>	<p>No specific order of required basic</p>	<ul style="list-style-type: none"> <li>• Require the "Opinion on the Financial Statements" section to be</li> </ul>	<p>No specific order for required elements in the</p>

Key Area	PCAOB 2013 Proposal	Changes in PCAOB 2016 Reproposal	Changes from Existing Auditor's Report
	elements in the auditor's report.	<p>the first section of the auditor's report, immediately followed by the "Basis for Opinion" section.</p> <ul style="list-style-type: none"> <li>The reproposal does not specify the order for the remaining sections of the auditor's report, which would include explanatory paragraphs and critical audit matters. The location of explanatory paragraphs in the auditor's report is specified in other PCAOB standards, which describe the related reporting requirements.</li> </ul>	existing auditor's report.

**Appendix IV - Determining and Communicating Critical Audit Matters ("CAMs")**

