

Week 3

Readings:

Eroding Auditor Independence a Concern for PCAOB Members

Consulting- significant source of revenue and continues to grow faster than audit sector

Auditors have a fiduciary duty

Reasonable Investor Rule: how would an investor view a client relationship

PCAOB still finds a relatively high percentage of deficient audits in its firm inspections. Common reasons include:

Failure to exercise professional skepticism

Ignoring contradictory evidence

Poor audit planning

Lack of training of personnel

Tight deadlines

- These are all factors the firms can control (and fix).
- PCAOB very concerned about auditors altering audit documentation. This comes with severe sanctions and disciplinary orders.
- One recommendation is that the PCAOB should clearly identify companies with deficient audits in their firm inspection reports. What do you think of this?

POGO believes PCAOB is too lenient on enforcing actions against firms and individuals

Financial penalties way too low

- The Financial Reporting Council (U.K. equivalent of PCAOB) has asked the Big Four in the U.K. to separate their consulting businesses from their audit businesses (to be completed by 2024).
- The goal of this is to strengthen auditors' professional skepticism and limit distractions from audit quality.
- The new proposal is to create the Audit, Reporting and Governance Authority (ARGA) – apparently to be more like the US regulator. Instead of FRC
 - This new regulator may oversee the big firms' separation of their audit and consulting businesses.

Another reform discusses limiting the Big 4's share of FTSE 350 audits

PCAOB Approves Rule for Naming Audit Partner

Form AP is called the "middle ground approach" – filed with PCAOB

When the auditor issued a qualified opinion due to scope limitation (audit issue)

- A paragraph, called the *Basis for Qualified Opinion Paragraph*, is added immediately after the opinion section and describes the reasons the auditor was not able to obtain sufficient evidence.
- The opinion paragraph includes the phrase, “*except for*”.

When the auditor issues qualified opinion due to departure from GAAP (FS issue)

- A paragraph, called the *Basis for Qualified Opinion Paragraph*, is added immediately after the opinion section and describes the nature and effects of the misstatements. This paragraph should also quantify the misstatement, if practicable.

Qualified= material, not pervasive

Disclaimer of Opinion issued when scope limitation is material and pervasive.

- *Basis for Disclaimer of Opinion Paragraph*, is added immediately after the opinion section and describes the reasons the auditor was not able to obtain sufficient evidence to express an opinion.

The opinion paragraph states that the auditor does not express an opinion on the financial statements

Adverse Opinion (Non-Issuer)

- When the auditor issues an adverse opinion due to a departure from GAAP (financial statement issue):
- A paragraph, called the *Basis for Adverse Opinion Paragraph*, is added immediately after the opinion section and describes and quantifies the nature and effects of the misstatements.
- The opinion paragraph includes the phrase, “*do not present fairly*”.

Remember, an adverse opinion is issued when the departure from GAAP is material and pervasive

If there are immaterial departures from GAAP, or immaterial scope limitations, what kind of report would be issued?

Unqualified Opinion, must be material to issue a different opinion

Other Reporting Issues

- What is the date of the Auditor’s Report? The auditor should date the report no earlier than the date on which the auditor has obtained sufficient appropriate evidence to support the opinion. The auditor has no responsibility to carry out auditing procedures subsequent to that date. In other words, the auditor’s responsibility doesn’t extend past that date.