



NZ AUDITING
AND ASSURANCE
STANDARDS BOARD

AMENDMENTS TO THE INTERNATIONAL STANDARDS ON AUDITING (NEW ZEALAND) TO PROMOTE IMPROVED AUDIT QUALITY

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ISBN 978-1-927238-80-6

AMENDMENTS TO THE INTERNATIONAL STANDARDS ON AUDITING (NEW ZEALAND) TO PROMOTE IMPROVED AUDIT QUALITY

ISA (NZ) 200 *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (New Zealand)*

The mark-ups indicate additions that need to be made to ISA (NZ) 200

Application material

NZ A8.1

- Statement of financial position
- Statement of comprehensive income.
- Statement of recognised income and expense.

ISA (NZ) 220 *Quality Control for an Audit of Financial Statements*

The mark-ups indicate additions that need to be made to ISA (NZ) 220

21. [Amended by the NZAuASB. Refer to NZ21.1].

NZ21.1 For audits of financial statements of issuers, and those other audit engagements, if any, for which the firm has determined that an engagement quality control review is required, the engagement quality control reviewer, on performing an engagement quality control review, shall also consider the following:

- (a) The engagement team's evaluation of the firm's independence in relation to the audit engagement;
- (b) Whether appropriate consultation has taken place on matters involving differences of opinion or other difficult or contentious matters, and the conclusions arising from those consultations; and
- (c) Whether audit documentation selected for review reflects the work performed in relation to the significant judgements made and supports the conclusions reached.
(Ref: Para. A28-A31)

A1. Professional and Ethical Standard 3 (Amended) deals with the firm's responsibilities to establish and maintain its system of quality control for audit engagements. The system of quality control includes policies and procedures that address each of the following elements:

- Leadership responsibilities for quality within the firm;
- Relevant ethical requirements;
- Acceptance and continuance of client relationships and specific engagements;

- Human resources;
- Engagement performance; and
- Monitoring.

Professional and Ethical Standard 3 contains requirements which are at least as demanding as its international equivalent, ISQC 1 *Quality Control For Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*, as it addresses all the elements referred to in ISQC 1 and imposes obligations on the firm that achieves the aims of the requirements set out in ISQC 1.

ISA (NZ) 260 *Communication with Those Charged with Governance*

NZ19.1 If the auditor is concerned that a written report intended for those charged with governance has not been, or may not be, distributed to all members of that group, the auditor shall endeavour to ensure all members are appropriately informed of the contents of the report.

A18. Significant difficulties encountered during the audit may include such matters as:

- Significant delays in management providing required information.
- An unnecessarily brief time within which to complete the audit.
- Extensive unexpected effort required to obtain sufficient appropriate audit evidence.
- The unavailability of expected information.
- Restrictions imposed on the auditor by management.
- Management's, or where appropriate, those charged with governance's unwillingness to make or extend their assessment of the entity's ability to continue as a going concern when requested.

In some circumstances, such difficulties may constitute a scope limitation that leads to a modification of the auditor's opinion.

ISA (NZ) 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*

NZ A24.1 Ownership and Governance arrangements such as:

- The role of the board of directors and those charged with governance in determining policies for the levels of risk that the entity is willing to accept in its daily operations.
- The role of senior management in designing, implementing, and monitoring effective risk management systems to implement the policies prescribed by the board of directors.
- The presence of non-executive directors on the board and an independent compensation committee that reviews incentive plans, including commissions, discretionary bonuses, directors' service contracts, and profit-sharing plans.
- The role of line management in carrying out the prescribed procedures and control activities.
- The strength of the internal audit function and the audit committee and their role as an independent appraisal function.
- The strength of other significant committees, for example, risk management committee, asset and liability management committee, or general management committee.
- The adequacy of segregation of duties.
- Prior period financial reporting disclosures include the form, classification, terminology, basis of amounts and level of detail provided.

ISA (NZ) 501 Audit Evidence – Specific Considerations for Selected Items

In-house and/or External Legal Counsel

NZ10.1 Where in-house legal counsel has the primary responsibility for litigation and claims and is in the best position to corroborate representations from management and those charged with governance, the auditor shall endeavour to obtain a representation letter from the in-house legal counsel, seeking information similar to that sought from the entity's external legal counsel. (Ref: Para. NZ A24.1 – NZ A24.2)

11. If:

- (a) management refuses to give the auditor permission to communicate or meet with the entity's ~~external~~ legal counsel, or the entity's ~~external~~ legal counsel refuses to respond appropriately to the letter of enquiry, or is prohibited from responding; and (Ref: Para. NZ A24.3 – NZ A24.4)
- (b) the auditor is unable to obtain sufficient appropriate audit evidence by performing alternative audit procedures, (Ref: Para. NZ A24.5 – NZ A24.6)

the auditor shall modify the opinion in the auditor's report in accordance with ISA (NZ) 705. (Ref: Para. NZ A24.7)

NZ A1.1 It is the responsibility of those charged with governance of an entity to adopt policies and procedures to identify, evaluate, record and report on the outcome of any material litigation and claims. However, since the factors that would be considered in the accounting for and reporting of litigation and claims are within the direct knowledge and control of the management of an entity, management is the primary source of information. Ordinarily, the auditor would seek audit evidence from different sources to corroborate management's assertions.

NZ A18.1 The procedures identified in paragraphs 10 and A18 would ordinarily include the following:

- Reviewing and discussing with management the procedures within the entity's internal control structure for identifying and recording litigation and claims and bringing them to the attention of management;
- Reviewing and discussing with management the procedures within the entity's internal control structure for the identification, control and recording of litigation and claims and associated revenues and expenses in appropriate accounts; and
- Obtaining and discussing with management:
 - (i) A list of litigation and claims, including a description of the matters and an estimate of their likely financial consequences; and
 - (ii) An analysis identifying litigation and claims.

NZ A18.2 Audit procedures that are undertaken for different purposes might also identify litigation and claims. Such procedures include:

- Examining contracts, loan agreements, leases, insurance policies and claims, and other correspondence;
- Reading minutes of meetings of the audit committee, shareholders and appropriate committees;
- Obtaining information concerning guarantees from bank confirmations; and
- Enquiries of management and other employees of the entity.

NZ A23.1 An example of a letter of specific enquiry is included in [NZ] Appendix 1.

NZ A23.2 An auditor may in some circumstances request that management send a letter of enquiry to the entity's legal counsel who are not identified as currently handling the entity's litigation and claims. For example when the entity has changed legal counsel on a particular matter, or when legal counsel engaged by the entity has resigned, the auditor would consider the need for enquiries concerning the reasons for the change or resignation.

In house and/or External Legal Counsel (Ref: Para. NZ 10.1)

NZ A24.1 If both in-house and external legal counsel are involved in advising the entity on the same litigation and claims, the auditor would ordinarily seek a letter of enquiry from the legal counsel with the primary responsibility for that matter. However, there may be circumstances where the in-house legal counsel has primary responsibility, but the matter has involved substantial participation by an external legal counsel, and is of such significance that the auditor would consider obtaining a letter of enquiry from the external legal counsel to determine that their opinion does not differ materially from that of the in-house legal counsel.

NZ A24.2 In circumstances where both in-house and external legal counsel have devoted substantial attention to litigation and claims involving the entity and primary responsibility rests with the external legal counsel, evidence obtained from an in-house legal counsel is not an adequate substitute for any information that the external legal counsel may refuse to furnish.

Legal Counsel's Inability to Respond Comprehensively or Limitations in a Response (Ref: Para 11(a))

NZ A24.3 If a response is not received from the entity's legal counsel, or the response received is incomplete, the auditor would ordinarily consider:

- (a) requesting management to contact the entity's legal counsel to either seek a complete answer to the original request, or an explanation for the lack of, or limitation in, a response, which ought to be sent directly to the auditor; or
- (b) making arrangements to discuss with management or the entity's legal counsel the reasons for the lack of, or limitation in, a response.

Alternative Audit Procedures (Ref. Para. 11(b))

NZ A24.4 Where the auditor has not obtained sufficient appropriate audit evidence as to a material financial statement assertion regarding litigation and claims, under ISA (NZ) 330, the auditor needs to consider whether alternative audit procedures can provide further audit evidence. Alternative audit procedures may include:

- (a) further enquiries of management, about for instance the processes, procedures and assumptions they implement, adopt or make to ensure litigation and claims are recognised and disclosed in accordance with the applicable financial reporting framework;
- (b) where possible, making arrangements to discuss litigation and claims with management and the entity's legal counsel;
- (c) further review of documents in management's possession concerning litigation and claims, including the entity's board minutes; and
- (d) further examination of accounts rendered by the entity's external legal counsel.

Other Audit Reporting Considerations (Ref: Para. 11)

NZ A24.5 In those circumstances where, due to uncertainties, the entity's legal counsel is unable to

form a conclusion to corroborate representations from management and those charged with governance, the auditor needs to consider the effect on the auditor's report arising from the extent of disclosure of the uncertainty in the financial statements:

- (a) where the auditor considers that the disclosure of the uncertainty in the financial statements is adequate, the auditor needs to consider including an Emphasis of Matter paragraph, in accordance with ISA (NZ) 706¹, or
- (b) if in the auditor's opinion the disclosure of the uncertainty is inadequate or unreliable, a modified opinion needs to be expressed in accordance with ISA (NZ) 705.

[NZ] Appendix 1

(Ref: Para. 5 and A7)

This example letter relates to specific enquiry directed to the entity's external legal counsel, but may be adapted, as appropriate, to specific enquiry directed to the entity's internal legal counsel.

Example of a Letter of Specific Enquiry to External Legal Counsel (For an Audit Client)

(Client Letterhead)

(Date)

(Name and Address of External Legal Counsel)

Dear ...

In connection with the preparation and audit of the financial statements of (name of company) (and the following subsidiaries and/or divisions) for the reporting period ended (date) we request that you provide to this company, at our cost, the following information:

- 1 Confirmation that you are acting for the company (and the above-named subsidiaries and/or divisions) in relation to the matters mentioned below and that the directors' description and estimates of the amounts of the financial settlement (including costs and disbursements) which might arise in relation to those matters are in your opinion reasonable.

Name of Company
(subsidiary or
division)

Directors' Description of
Matter (including current
status)

Directors' Estimate of the
Financial Settlement
(inclusive of costs and
disbursements)

¹ ISA (NZ) 706, "Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report".

2 Should you disagree with any of the information included in 1 above, please comment on the nature of your disagreement.

3 In addition to the above, a list of open files that you maintain in relation to the company (and the above mentioned subsidiaries and/or divisions).

4 In relation to the matters identified under 2 and 3 above, we authorise you to discuss these matters with our auditor (name and address), if requested, and at our cost.

It is understood that:

- (a) the company (and the above-named subsidiaries and/or divisions) may have used other legal counsel in certain matters;
- (b) the information sought relates only to information relating to litigation and claims referred to your firm (including branches or subsidiaries) which were current at any time during the above-mentioned reporting period, or have arisen since the end of the reporting period and up to the date of your response;
- (c) unless separately requested in writing, you are not responsible for keeping the auditors advised of any changes after the date of your reply;
- (d) you are only required to respond on matters referred to you as legal counsel for the company (and the above-mentioned subsidiaries and/or divisions), not on those within your knowledge solely because of the holding of any office as director, secretary or otherwise of the company (and the above-mentioned subsidiaries and/or divisions) by a consultant, partner or employee of your firm; and
- (e) your reply is sought solely for the information of, and assistance to, this company in connection with the audit of, and report with respect to, the financial statements of the company (and the above-mentioned subsidiaries and/or divisions) and will not be quoted or otherwise referred to in any financial statements or related documents of the company (and the above-mentioned subsidiaries and/or divisions) nor will it be furnished to any governmental agency or other person, subject to specific legislative requirements, without the prior written consent of your firm.

Your prompt assistance in this matter will be appreciated. If you are unable to confirm or provide the information requested above, please advise us and our auditor the reasons for any limitation or impediment to fulfilling this request.

Please forward a signed copy of your reply directly to our auditors, (name) at (address), by (date).

Yours faithfully,

(Signature and Title of client)

ISA (NZ) 540 Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures

NZ A7.1 Impairment testing of assets.

ISA (NZ) 570 Going Concern

13. ~~[Replaced by the NZAuASB. Refer to NZ 13.1] In evaluating the assessment of the entity's ability to continue as a going concern, the auditor shall cover the same period as that used by those charged with governance to make their assessment as required by the applicable financial reporting framework, or by law or regulation if it specifies a longer period. If the assessment of the entity's ability to continue as a going concern covers less than twelve months from the date of the financial statements as defined in ISA (NZ) 560,² the auditor shall request those charged with governance to extend their assessment period to at least twelve months from that date. (Ref: Para. A10-A12)~~

NZ13.1 In evaluating the assessment by those charged with governance of the entity's ability to continue as a going concern, the auditor shall consider the relevant period, which may be the same or may differ from that used by those charged with governance to make their assessment as required by the applicable financial reporting framework. If the assessment of the entity's ability to continue as a going concern covers less than the relevant period, the auditor shall request those charged with governance to correspond to the relevant period used by the auditor. (Ref: Para. A10-A12)

NZ13.2 Relevant period means the period of at least 12 months from the date of the auditor's current report.

Application material

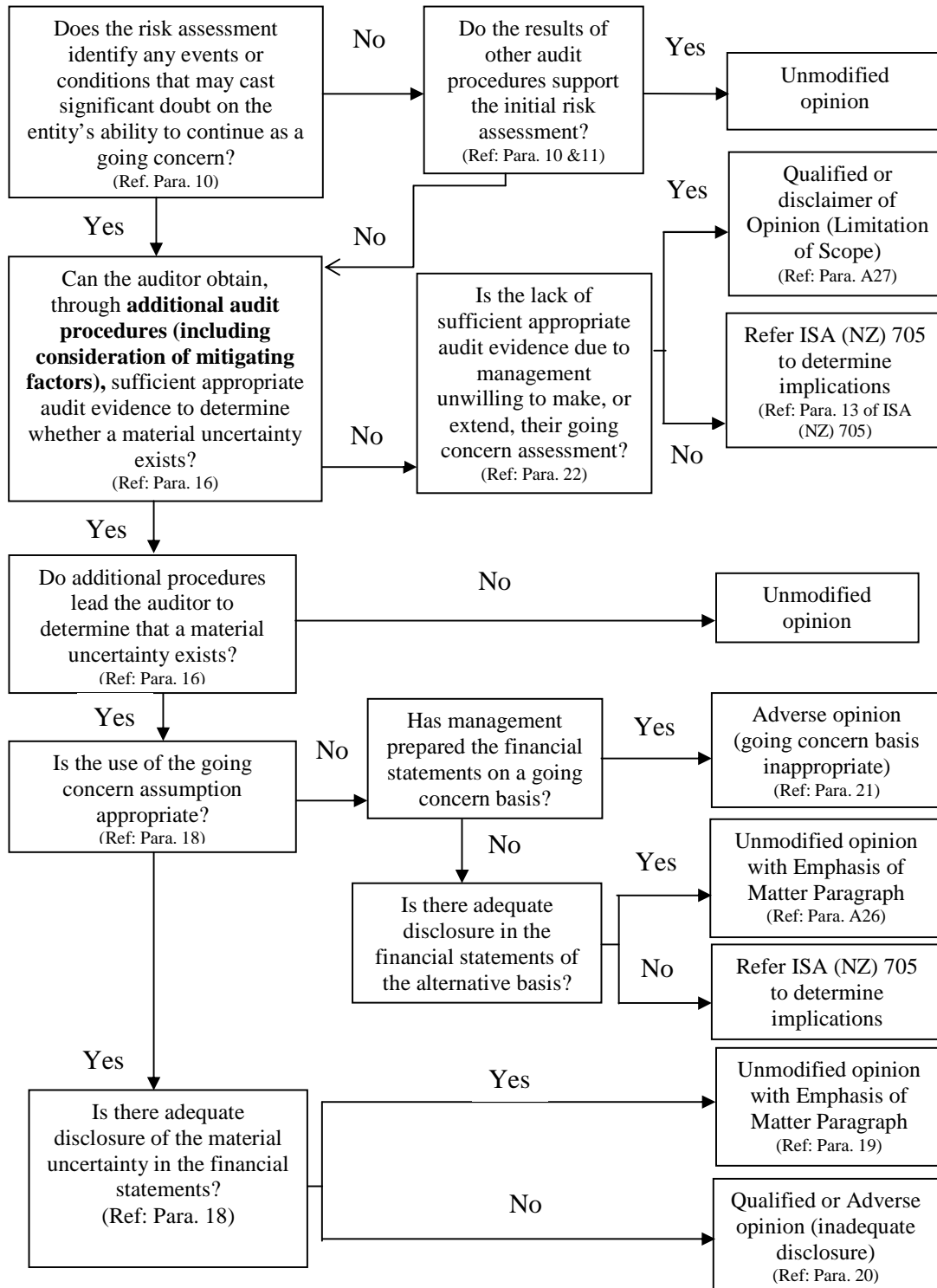
A14. ~~[Amended by the NZAuASB. Refer to NZ A14.1].~~

[NZA14.1] Other than enquiry of those charged with governance, the auditor does not have a responsibility to perform any other audit procedures to identify events or conditions that may cast significant doubt on the entity's ability to continue as a going concern beyond the relevant period, which, as discussed in paragraph NZ 13.2, is at least twelve months from the date of the auditor's report on the current financial statements. ~~assessed by those charged with governance, which, as discussed in paragraph 13, would be at least twelve months from the date of the financial statements.~~

[NZA19.1] Refer to [NZ] Appendix 1 for a diagrammatic illustration of the links between going concern considerations and the types of audit opinions.

[NZA21.1] Refer to [NZ] Appendix 2 for an Illustrative Auditor's Report that contains an unqualified opinion with an Emphasis of Matter paragraph.

Linking Going Concern Considerations and Types of Audit Opinions



Note: Audit opinions in this diagram must comply, as appropriate, with:
 ISA (NZ) 700 *Forming an Opinion and Reporting on Financial Statements*
 ISA (NZ) 705 *Modifications to the Opinion in the Independent Auditor's Report*
 ISA (NZ) 706 *Emphasis of Matter Paragraphs and Other Mater Paragraphs in the Independent Auditor's Report*

Illustration of an Auditor’s Report that Includes an Emphasis of Matter Paragraph due to a Material Uncertainty regarding Going Concern

Circumstances include the following:

- **Audit of a complete set of general purpose financial statements for a reporting entity as defined by the Financial Reporting Act 1993.**
- **The terms of the audit engagement reflect the description of the responsibility of those charged with governance for the financial statements in ISA (NZ) 210.³**
- **There is uncertainty resulting from a net loss for the year and net liabilities exceeding net assets.**

INDEPENDENT AUDITOR’S REPORT

To the Shareholders of ABC Limited

Report on the Financial Statements

We have audited the financial statements of ABC Limited on pages to, which comprises the balance sheet as at 30 June 20X1, the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors’ Responsibility for the Financial Statements

The directors are responsible for the preparation of financial statements in accordance with generally accepted accounting practice in New Zealand and that give a true and fair of the matters to which they relate, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor’s Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing (New Zealand). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers

³ ISA (NZ) 210, “Agreeing the Terms of Audit Engagements.”

internal control relevant to the entity's preparation of the financial statements that gives a true and fair view 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 the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence that we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Other than in our capacity as auditor we have no relationship with, or interests in, ABC Limited.

Opinion

In our opinion the financial statements on pages ... to ... :

- comply with generally accepted accounting practice in New Zealand;
- give a true and fair view of the financial position of ABC Limited as at June 30, 20X1, and of its financial performance for the year then ended.

Emphasis of Matter

Without modifying our opinion, we draw attention to Note X to the financial statements, which indicates that the company incurred a net loss of ZZZ during the year ended 30 June 20X1 and, as of that date, the company's current liabilities exceeded its total assets by YYY. These conditions, along with other matters as set forth in Note X, indicate the existence of a material uncertainty that may cast significant doubt about the company's ability to continue as a going concern and therefore, the company may be unable to realise its assets and discharge its liabilities in the normal course of business.

Report on Other Legal and Regulatory Requirements

In accordance with the Financial Reporting Act 1993, we report that:

- We have obtained all the information and explanations that we have required.
- In our opinion proper accounting records have been kept by ABC Limited as far as appears from our examination of those records.

[Add any matters required to be included under any other legislation or regulation.]

[Auditor's signature]

[Date of the auditor's report]

[Auditor's address]

ISA (NZ) 580 *Written Representations*

[NZ A20.1] If the auditor intends to rely on some, or all, of the written representations made by those charged with governance in a written public statement, the auditor ordinarily communicates their intention to place such reliance.

ISA (NZ) 600 *Special Considerations – Audits of Group Financial Statements*

[NZ A65.1] In the public sector, group management may not always be readily identifiable at the whole of government level. Furthermore, responsibility for internal control may remain at individual entity level only. In such cases, the auditor determines the appropriate level of management with whom to communicate.

ISA (NZ) 710 *Comparative Information – Corresponding Figures and Comparative Financial Statements*

[NZ A7.1] In New Zealand, the auditor’s opinion on financial statements prepared under New Zealand generally accepted accounting practice refers to financial statements for the current period, which include corresponding figures, and not to comparative financial statements. Consequently, paragraphs 15, 16, 17, 18 and 19, and related paragraphs A8, A9, A10, and A11 have no application.

EG Au1 Overview of Auditing and Assurance Standards

Proposed amendment

15 Auditing and assurance standards issued by the XRB or the NZAuASB are the primary indicators of good assurance practice in New Zealand. The standards contain objectives, definitions, requirements, application and other explanatory material, introductory material, and appendices. They set out the requirements or basic principles and essential procedures that assurance practitioners should follow when conducting an assurance engagement, and the behaviours that they should display as part of, and surrounding, that work. The assurance practitioner should apply the mandatory components of the auditing and assurance standards when conducting an assurance engagement. The mandatory components are included under the headings listed below:

- Effective Date;
- Objective(s);
- Definition(s);

- Requirements.

16 The assurance practitioner should have an understanding of the entire text of the standard, including its application and other explanatory material, to understand its objectives and to apply its requirements properly. The explanatory material is included in each standard under the headings listed below:

- Introduction(s);
- Application and Other Explanatory Material;
- Conformity with International Standards;
- Appendices

Appendices, which form part of the application material, are an integral part of a standard. The purpose and intended use of an appendix are explained in the body of the related standards or within the title and introduction of the appendix itself. Explanatory material does not create or extend mandatory components. ~~They also contain explanatory guidance used to improve knowledge and understanding of the scope and application of the requirements, basic principles and essential procedure.~~

Effective Date

Amendments to the International Standards on Auditing (New Zealand) to Promote Improved Audit Quality is effective for audits of financial statements for periods ending on or after 31 December, 2014.