

Implementation Guide to
Standard on Auditing (SA) 701,
**Communicating Key Audit Matters in
the Independent Auditor's Report**



The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
New Delhi

© The Institute of Chartered Accountants of India.

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted, in any form, or by any means, electronic, mechanical, photocopying, recording, or otherwise, without prior permission, in writing, from the publisher.

Edition : August 2018

Committee/
Department : Auditing and Assurance Standards Board

Email : aasb@icai.in

Website : www.icai.org

Price : Rs. 50/-

ISBN : 978-81-8441-934-4

Published by : The Publication Department on behalf of the Institute of Chartered Accountants of India, ICAI Bhawan, Post Box No. 7100, Indraprastha Marg, New Delhi – 110 002.

Printed by : Sahitya Bhawan Publications, Hospital Road, Agra 282 003.
August/2018/P2323(New)

Foreword

Standards on Auditing issued by the Institute of Chartered Accountants of India (ICAI) are critical in ensuring and enhancing audit quality. It is essential that the auditors understand and implement the requirements of these Standards in their audit engagements. The Implementation Guides to Standards on Auditing are an important resource for the auditors to appropriately understand the requirements of these Standards and help them implement these Standards appropriately. These Implementation Guides also provide solutions to various practical problems faced by the auditors in implementing these Standards in real life audit situations.

In the year 2016, ICAI revised the extant suite of auditor's reporting standard (i.e. SAs 700, 705, 706) and also issued a new standard SA 701, "Communicating Key Audit Matters in the Independent Auditor's Report". These set of standards has changed the paradigm of auditor's reporting. Moreover, these standards are expected to reinvigorate the audit and change the manner in which auditors communicate their work in their key deliverable i.e. auditor's report.

Earlier these standards were applicable for audits of financial statements for periods beginning on or after April 1, 2017. However considering the magnitude of changes driven by these standards, the Council of ICAI felt the urgent need to create awareness on the standards and accordingly decided to defer the applicability of these standards by a year. Now these standards are effective for audits of financial statements for periods beginning on or after April 1, 2018.

I am happy that the Auditing and Assurance Standards Board of ICAI has brought out this "Implementation Guide to Standard on Auditing (SA) 701, "Communicating Key Audit Matters in the Independent Auditor's Report" for the benefit of the members. The Implementation Guide has been written in an easy to understand language in the form of frequently asked questions (FAQs) and contains detailed and focused guidance on various issues involved. The aim of this Implementation Guide is to provide

appropriate guidance on SA 701 to the members so as to enable them to discharge their reporting responsibilities smoothly and effectively under this Standard.

I compliment CA. Shyam Lal Agarwal, Chairman, AASB, CA. Sanjay Vasudeva, Vice-Chairman, AASB and all the members of the Auditing and Assurance Standards Board for bringing out this Implementation Guide for the benefit of the members. I am sure that the members and other interested readers would find this Implementation Guide immensely useful.

February 2, 2018
New Delhi

CA. Nilesh S. Vikamsey
President, ICAI

Preface

As the members are aware that ICAI in 2016 issued a series of new/revised standards on auditor reporting comprising Revised SAs 700, 705, 706, 260, 570 and a new SA 701, “Communicating Key Audit Matters in the Independent Auditor’s Report”. SA 701 is mandatory in the case of audit of listed entities and casts a new reporting requirement on auditors of listed entities to communicate key audit matters in their audit reports. This Standard is also applicable in audit of unlisted entities in situations where law or regulation requires communication of key audit matters in the audit report. SA 701 is effective for audits of financial statements for periods beginning on or after April 1, 2018. SA 701 has strong interrelationship with other elements of the audit report e.g. emphasis of matter/ other matter paragraphs, modified opinion, going concern aspect. As a proactive measure, the Auditing and Assurance Standards Board (AASB) of ICAI decided to develop an Implementation Guide on SA 701 to provide appropriate guidance to the members so that they can discharge their reporting responsibilities under this Standard in an effective manner.

It gives me immense pleasure to place in hands of the members, this “Implementation Guide to SA 701, Communicating Key Audit Matters in the Independent Auditor’s Report” brought out by AASB. The Implementation Guide has been written in simple and easy to understand language and contains detailed guidance on various issues involved in this new reporting requirement. For ease of usage and understanding of the readers, the Implementation Guide has been written in a “Question – Answer” format containing frequently asked questions (FAQs) on SA 701 and responses to those questions.

At this juncture, I wish to express my sincere gratitude to CA. Abhijit Bandyopadhyay, Board member and his team for their dedicated efforts in developing the basic draft of this Implementation Guide despite their other pressing preoccupations. I would also like to thank CA. Deepa Agarwal, Board member and her team who have updated and aligned this

Implementation Guide in line with the discussion held in the Board.

I wish to express my sincere thanks to CA. Nilesh S. Vikamsey, Honourable President, ICAI and CA. Naveen N.D. Gupta, Honourable Vice President, ICAI for their guidance and support to the activities of the Board.

I wish to place on record high appreciation of CA. Sanjay Vasudeva, Vice Chairman of the Board for his whole-hearted support. I also wish to place on record my sincere thanks to all the Board Members and all the Council Members for their suggestions, support and guidance in finalising this Implementation Guide as well as other pronouncements of the Board. I also wish to thank CA. Megha Saxena, Secretary, AASB and other officers and staff of AASB for their continued co-operation.

I am confident that the Implementation Guide would be well received by the members and other interested readers.

February 4, 2018
Jaipur

CA. Shyam Lal Agarwal
Chairman,
Auditing and Assurance Standards Board

Contents

Foreword

Preface

Page No.

Introduction	1-2
Frequently Asked Questions (FAQs)	3-32
Appendix: Illustrative Examples of Key Audit Matters	33-38

Introduction

The purpose of communicating key audit matters (KAM) is to enhance the communicative value of the auditor's report by providing greater transparency about the audit that was performed. Communicating key audit matters provides additional information to intended users of the financial statements to assist them in understanding those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Communicating key audit matters may also assist intended users in understanding the entity and areas of significant management judgment in the audited financial statements.

Communicating key audit matters in the auditor's report is in the context of the auditor having formed an opinion on the financial statements as a whole and does not constitute a separate opinion on individual matters. Communicating key audit matters in the auditor's report is not:

- a substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation.
- a substitute for expressing a modified opinion when required by the circumstances of a specific audit in accordance with SA 705 (Revised), "Modifications to the Opinion in the Independent Auditor's Report".
- a substitute for reporting in accordance with SA 570 (Revised), "Going Concern" when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern.
- a separate opinion on individual matters.

SA 701 requires the communication of key audit matters in the auditor's report for audits of complete sets of general purpose financial statements of listed entities or when required by law or regulation.

Key audit matters are defined as those matters that, in the

Implementation Guide to SA 701

auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Key audit matters are selected from matters communicated with those charged with governance.

The auditor is required to communicate with those charged with governance the matters to be included in auditor's report. This communication is intended to make management and those charged with governance aware of the matters that auditor intends to communicate in the auditor's report, and to provide them with an opportunity to obtain further clarification where necessary. It may also enable management or those charged with governance to consider whether new or enhanced disclosures may be useful when these matters will be communicated in the auditor's report. The auditor may provide those charged with governance a draft of the auditor's report to assist with these discussions. However, the final content of the auditor's report, which is also required to be communicated to those charged with governance, remains the auditor's responsibility.

From the matters that required significant auditor attention, the auditor determines matters which were of the most significance in the audit of the financial statements of the current period and therefore are KAMs. In most cases, KAMs will relate to significant or complex matters disclosed in the financial statements. Examples of KAMs might include valuation of goodwill and other long-term assets, valuation of financial instruments, difficult or unique aspects of revenue recognition, or accounting for significant acquisitions. KAMs are included in a separate section of the auditor's report with introductory language explaining the nature and intent of KAMs, including that the matters were addressed in the context of the audit as a whole and that the auditor does not provide a separate opinion on these matters.

It will be important for KAMs to be relevant and useful for investors and other users. To accomplish this, auditors must make sure that the information is as entity-specific as possible, and related to the facts and circumstances of the audit of the current period. However, it remains the responsibility of management, with the oversight of those charged with governance, to communicate relevant information to users about entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework.

Frequently Asked Questions (FAQs)

Given below are the responses on key issues of SA 701 in a Question – Answer format.

Question 1: What is the applicability date of SA 701, new reporting standard?

Response 1: The new reporting standard SA 701 is applicable for audits of financial statements for periods beginning on or after April 1, 2018.

Question 2: For which audits does the auditor need to follow the SA 701 mandatorily?

Response 2: SA 701 mandatorily applies to audits of complete sets of general purpose financial statements of listed entities for period beginning on or after April 1, 2018.

Question 3: Since SA 701 is mandatory only for listed entities, whether it is applicable on audits of unlisted entities?

Response 3: Yes, SA 701 is applicable for audit of unlisted entities under the following circumstances:

- When the auditor decides to communicate key audit matters in the auditor's report, or
- When the auditor is required by law or regulation to communicate key audit matters in the auditor's report.

For example, it can be given by the auditors on voluntary basis when communication of KAM will:

- promote consistency and comparability in auditor's reporting; and
- assist intended users of the financial statements in understanding those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period.

When an auditor is not mandatorily required to communicate key audit matters under SA 701, the discussions with those charged with governance for such entities may highlight interest or value in

Implementation Guide to SA 701

the communication of matters to the intended users of the financial statements. The auditor's report is a deliverable by the auditors and hence the decision to communicate key audit matters is to be taken by the auditors only.

Question 4: Is SA 701 applicable for audits of complete sets of general purpose financial statements for periods beginning before April 1, 2018, wherein the audit reports are signed after April 1, 2018?

Response 4: SA 701 applies to audits of complete sets of general purpose financial statements of listed entities for periods beginning on or after April 1, 2018. Hence, audit reports signed after April 1, 2018 which pertain to financial statements for periods beginning before April 1, 2018 will not be governed by SA 701.

Question 5: Does SA 701 apply for audits of interim financial statements or when an auditor does an audit of financial results in accordance with the requirements of Regulation 33 or Regulation 52 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015?

Response 5: SA 701 applies only to audits of complete set of general purpose financial statements of a listed entity. Therefore, if an audit report on interim financial statements is submitted only to the Board of Directors, the same cannot be construed as general purpose financial statements and hence SA 701 will not apply in such cases. However, if such interim financial statements are complete in all respects and are hosted on the company's website, the same can be construed to be general purpose financial statements and hence SA 701 will apply in such cases.

Financial results under SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015 are not a complete set of financial statements and hence in audit of these financial results, SA 701 is not applicable.

Question 6: Is early adoption of reporting under SA 701 permissible?

Response 6: No, SA 701 does not provide for early adoption and hence it is interpreted that early adoption of SA 701 is not permissible.

Question 7: Is reporting under SA 701 applicable for audit reports provided for tax financial statements for periods beginning on or after April 1, 2018?

Response 7: SA 701 is applicable for audits of complete set of general purpose financial statements of listed entities. Although tax financial statements are considered as general purpose financial statements since they are provided to a regulator, they are not intended to meet the common financial information needs of a wide range of users. Therefore, SA 701 does not apply to tax financial statements.

Question 8: Since SA 701 applies for audits of listed entities, the status of listing is to be determined as of which date?

Response 8: SA 701 would apply to an entity which is listed as on the reporting date (Balance Sheet date). Consequently, if during the reporting period, a listed entity gets delisted, SA 701 would not apply to such entity, since as at the reporting date it is not a listed entity.

Question 9: Whether SA 701 applies to the entities which are in the process of getting listed as at the reporting date?

Response 9: SA 701 is applicable to only listed entities. Hence, if an entity is in the process of getting listed as at the reporting date then SA 701 is not applicable to it. However, it will be applicable from the financial year in which the entity is listed.

Question 10: If a company has its securities listed on a foreign stock exchange, but has no listing in India, is the auditor required to communicate key audit matters as per SA 701?

Response 10: SA 701 applies to audits of complete sets of general purpose financial statements of listed entities. Therefore, SA 701 should be applied when the securities of an entity are listed on any stock exchange in India or outside India. The securities include shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature.

Question 11: What is the purpose for bringing in the requirement for reporting on key audit matters in the auditor's report?

Response 11: The purpose of communicating key audit matters is to enhance the communicative value of the auditor's report by providing greater transparency about the audit that was performed. Communicating key audit matters provides additional information to intended users of the financial statements to assist them in understanding those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Communicating key audit matters may also assist intended users in understanding the entity and areas of significant management judgment in the audited financial statements.

Question 12: What are key audit matters?

Response 12: Key audit matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Key audit matters are selected from matters communicated with those charged with governance.

Question 13: Is providing key audit matters in an auditor's report in the nature of providing a separate opinion on individual matters reported as key audit matter?

Response 13: No. Communicating key audit matters in the auditor's report is in the context of the auditor having formed an opinion on the financial statements as a whole.

Further, communicating key audit matters is not:

- A substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation;
- A substitute for the auditor expressing a modified opinion when required by the circumstances of a specific audit engagement in accordance with SA 705 (Revised);

- A substitute for reporting in accordance with SA 570 (Revised) when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern; or
- A separate opinion on individual matters.

Question 14: When an auditor disclaims his opinion on the financial statements, can communication of key audit matters as per SA 701 be made?

Response 14: When an auditor disclaims his overall opinion on the financial statements, he is prohibited from communicating key audit matters, unless such reporting is required by law or regulation (As per Paragraph 29 of SA 705(Revised)). However, if the auditor disclaims an area in the financial statements and provides an overall qualified opinion, communicating other key audit matters would still be relevant to enhancing intended users' understanding of the audit, and therefore the requirements to determine key audit matters apply.

Question 15: When an auditor expresses a qualified or adverse opinion on the financial statements, can communication of key audit matters as per SA 701 be made?

Response 15: Yes. If the auditor determines one or more key audit matters in addition to the matter which is giving rise to qualified or adverse opinion, the auditor can communicate those matter(s) as KAM.

Question 16: How should an auditor determine what a key audit matter is?

Response 16: A funnel approach may be adopted to determine which matters are required to be reported as key audit matter in the auditor's report. The starting point would be the matters that are communicated to those charged with governance, filtered for those matters that required significant auditor attention and then finally filtered for matters of most significance in the audit, which then would be the key audit matter for inclusion in the auditor's report.

Implementation Guide to SA 701

Step 1: Matters communicated with those charged with governance

Some of the matters that are normally communicated with those charged with governance *inter-alia* are:

- Auditor's responsibilities in relation to the financial statement audit.
- Planned scope and timing of the audit, including significant risks identified:
 - Plan to address the significant risks of material misstatement, whether due to fraud or error.
 - Plan to address areas of higher assessed risks of material misstatement.
 - Approach to internal control relevant to the audit.
 - Application of materiality.
 - Nature and extent of specialized skill or knowledge, including use of an auditor's expert.
 - Where SA 701 applies, preliminary views about matters that may be areas of significant auditor attention and therefore may be key audit matters.
- Significant findings from the audit.
 - Where SA 701 applies, this would be relevant to determine matters that required significant auditor attention and therefore may be key audit matters.
- Auditor independence.

Reference may be made to SA 260 (Revised)¹ in this regard for listing of matters that are required to be communicated to those charged with governance.

Step 2: Matters that required significant auditor attention

Matters that required significant auditor attention primarily relate to matters that pose challenges to the auditor in forming an opinion or obtaining evidence that in his judgement was sufficient and appropriate under the circumstances. The auditor shall take into

¹ SA 260(Revised), Communication with Those Charged with Governance.

account the following in this regard:

- Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with Paragraph 5 of SA 315². Some points to be considered are:
 - SA 260 (Revised) requires communication of significant risks to those charged with governance and plans for addressing the same.
 - Significant risks require special audit consideration and are often areas that require significant auditor attention.
 - Exceptions for considering as key audit matter could be the presumed significant fraud risks - revenue recognition and management override of controls.
- Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty.
- The effect on the audit of significant events or transactions that occurred during the period. Some points to be considered are:
 - Events or transactions that had a significant effect on the financial statements or the audit. Examples – significant transactions with related parties, significant transactions outside the normal course of business, unusual transactions.
 - Significant economic, accounting, regulatory, industry or other developments that impacted the management's assumptions or judgements.

Step 3: Matters that were of most significance in the audit of current period

When determining matters that were of most significance in an audit, some points to be considered are:

- Areas where the auditor had more in-depth, frequent or robust interactions with those charged with governance on more

² SA 315, Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment.

Implementation Guide to SA 701

difficult and complex matters. For example, the auditor may have had more in-depth, frequent or robust interactions with those charged with governance on more difficult and complex matters, such as the determination of certain accounting estimates that were the subject of significant auditor or management judgment.

- Other factors to be considered are:
 - Importance of the matter to intended users' understanding of the financial statements and its materiality.
 - Nature of the underlying accounting policy compared to other entities within its industry.
 - Nature and materiality of corrected and uncorrected misstatements³.
 - Nature and extent of audit effort required, including the need for specialized skill or knowledge and consultations outside the engagement team.
 - Nature and severity of difficulties in applying the audit procedures, evaluating results of those procedures, and obtaining relevant and reliable evidence. For example, auditor may experience significant difficulties in matters such 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 unwillingness to make or extend its

³ When uncorrected misstatement exceeds thresholds, it would qualify for modification (including IFCoFR), in which case it will not be a KAM.

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.

- Severity of control deficiencies.
- Impact on several related areas (example: long term contracts – impact on revenue recognition, litigation, contingencies etc.)

Determining which, and how many, of those matters that required significant auditor attention were of most significance in the audit of the financial statements of the current period is a matter of professional judgment. The number of key audit matters to be included in the auditor's report may be affected by the size and complexity of the entity, the nature of its business and environment, and the facts and circumstances of the audit. In general, the greater the number of matters initially determined to be key audit matters, the more the auditor needs to reconsider whether each of these matters meets the definition of a key audit matter. Lengthy lists of key audit matters are contrary to the notion of such matters being those of most significance in the audit. (Please refer paragraph A30 of SA 701)

Question 17: How should an auditor communicate key audit matters?

Response 17: A separate section with title "Key audit matters" is to be included in the auditor's report. In this section the language should clearly cover the following:

- Key audit matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period; and
- These matters were addressed in the context of the audit of the financial statements as a whole, and in forming the auditor's opinion thereon, and the auditor does not provide a separate opinion on these matters.

Implementation Guide to SA 701

Illustrative paragraph of key audit matters:

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

[Description of each key audit matter in accordance with SA 701.]

Refer to **Appendix** to the Implementation Guide for illustrative examples of key audit matters.

Question 18: What is the auditor's responsibility to report a key audit matter for which there are no relevant disclosures in the financial statements?

Response 18: When communicating key audit matters, the fact that there are no disclosures in the financial statements related to a matter determined to be a key audit matter does not relieve the auditor from the requirement to communicate it. An auditor may determine a key audit matter related to the audit for which relevant disclosure requirements do not exist in the applicable financial reporting framework. For example, the implementation of a new IT system (or significant changes to an existing IT system) during the period may be an area of significant auditor attention, in particular if such a change had a significant effect on the auditor's overall audit strategy or related to a significant risk (e.g., changes to a system affecting revenue recognition). (Please refer paragraph A18 of SA 701)

Also, if an auditor determines that it is necessary to include information about the entity in order to effectively describe a key audit matter that has not been disclosed by management and management does not agree to disclose that information, the auditor should re-consider the adequacy of the disclosures in accordance with applicable financial reporting framework. The auditor should communicate the matter as a key audit matter unless law or regulation precludes public disclosure about the matter or in extremely rare circumstances, the auditor determines that the matter should not be communicated in the auditor's report

because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Question 19: Where should the placement of the key audit matters section be in the auditor’s report?

Response 19: Generally, Key Audit Matters section is required to be placed after the Basis for Opinion paragraph and before the Management’s Responsibility paragraph.

In case, ‘Material uncertainty relating to going concern’ section is required as per SA 570(Revised), then KAM section is placed after that section.

Further, regarding placement of KAM section, paragraph A16 of SA 706 (Revised), “Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor’s Report” provides as under:

When a Key Audit Matters section is presented in the auditor’s report, an Emphasis of Matter (EOM) paragraph may be presented either directly before or after the Key Audit Matters section, based on the auditor’s judgment as to the relative significance of the information included in the Emphasis of Matter paragraph. The auditor may also add further context to the heading “Emphasis of Matter”, such as “Emphasis of Matter – Subsequent Event”, to differentiate the Emphasis of Matter paragraph from the individual matters described in the Key Audit Matters section.

Question 20: Paragraph 11(a) of SA 701 clearly indicates that the key audit matters relate to matters that were of most significance in the audit of financial statements of the current period. Does this mean that one needs to completely ignore the earlier period key audit matters?

Response 20: Since in India, the “corresponding figures approach” is followed for general purpose financial statements as referred to in SA 710, Comparative Information — Corresponding Figures and Comparative Financial Statements, the audit report is

always only for the current period that is under consideration. Notwithstanding that the auditor's determination of key audit matters is for the audit of the financial statements of the current period and this SA does not require the auditor to update key audit matters included in the prior period's auditor's report, it may nevertheless be useful for the auditor to consider whether a matter that was a key audit matter in the audit of the financial statements of the prior period continues to be a key audit matter in the audit of the financial statements of the current period.

Question 21: Since the key audit matters relate to the current period, can the same be different for different years?

Response 21: Identification of a key audit matter is a matter of professional judgement. Although it is possible for key audit matters to be different in different years, given that identification of key audit matters is a result of the risk assessment procedures adopted by an auditor, it may be unlikely that key audit matters would be entirely different in different years.

Question 22: Is it possible for different entities in the same industry to have different key audit matters communicated by their auditors?

Response 22: Yes, it is possible that different entities in the same industry and also those who have similar type of business have different key audit matters that are communicated by their auditors. The matters that qualify for communication as key audit matters, are largely driven by the risk assessment process of the auditor and entity specific conditions and circumstances.

However, certain matters may be determined as key audit matters in a particular industry across a number of entities due to the circumstances of the industry or the underlying complexity in financial reporting. In describing why the auditor considered the matter to be one of most significance, it may be useful for the auditor to highlight aspects specific to the entity (e.g., circumstances that affected the underlying judgments made in the financial statements of the current period) in order to make the description more relevant for intended users. This also may be important in describing a key audit matter that recurs over periods.

Question 23: Are all significant risks considered to be key audit matters?

Response 23: Paragraphs 14–17 of SA 260 (Revised) require the auditor to communicate various matters with those charged with governance, including the auditor’s responsibilities in relation to the audit, the planned scope and timing of the audit, significant findings from the audit and auditor independence. In this regard, the auditor is required to communicate about the significant risks identified by the auditor, as part of communicating an overview of the planned scope and timing of the audit. From those matters communicated with those charged with governance, the auditor determines the matters that required significant auditor attention. From the matters that required significant auditor attention, the auditor further determines the matters which were of most significance and therefore are the key audit matters.

Paragraphs A27–A30 of SA 701 provide guidance and factors that may influence this determination. Paragraph A20 of SA 701 explains that areas of significant management judgment and significant unusual transactions may often be identified as significant risks and therefore significant risks are often areas that require significant auditor attention. However, paragraph A21 of SA 701 highlights that this may not be the case for all significant risks. For example, SA 240, “The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements” presumes that there are risks of fraud in revenue recognition and management override of controls and accordingly requires the auditor to treat these assessed risks of material misstatement due to fraud as significant risks. Depending on their nature, these risks may not require significant auditor attention, and therefore would not be considered as key audit matters.

Question 24: Should all matters communicated to those charged with governance be key audit matters?

Response 24: No. Matters that are communicated to those charged with governance act as a starting point in determining key audit matters. The decision-making process in determining key audit matters is designed to select a smaller number of matters from the matters communicated with those charged with

Implementation Guide to SA 701

governance, based on the auditor's judgment about which matters were of most significance in the audit of the financial statements of the current period.

Auditor's determination of key audit matters is limited to those matters of most significance in the audit of the financial statements of the current period.

Question 25: Is there a threshold for the number of key audit matters that needs to be communicated by the auditor?

Response 25: No, there is no threshold that has been prescribed in SA 701. It is completely a matter of professional judgement of the auditor. The number of key audit matters to be included in the auditor's report may be affected by the size and complexity of the entity, the nature of its business and environment, and the facts and circumstances of the audit engagement. In general, the greater the number of matters initially determined to be key audit matters, the more the auditor may need to reconsider whether each of these matters meets the definition of a key audit matter. Lengthy lists of key audit matters may be contrary to the notion of such matters being those of most significance in the audit.

Question 26: Can there be a situation when there is no key audit matter for an auditor to communicate?

Response 26: Yes, there could be situations where there are no key audit matters to be communicated.

The determination of key audit matters involves making a judgment about the relative importance of matters that required significant auditor attention. Therefore, it may be rare that the auditor of a complete set of general purpose financial statements of a listed entity would not determine at least one key audit matter from the matters communicated with those charged with governance to be communicated in the auditor's report. However, in certain limited circumstances (e.g., for a listed entity that has very limited operations), the auditor may determine that there are no key audit matters for communication. This needs to be communicated to those charged with governance and included in the auditor's report.

Implementation Guide to SA 701

When the auditor has determined that there are no key audit matters to communicate in the auditor's report, the communication with those charged with governance may provide an opportunity for the auditor to have further discussion with others who are familiar with the audit and the significant matters that may have arisen (including the engagement quality control reviewer, where one has been appointed). These discussions may cause the auditor to re-evaluate the auditor's determination that there are no key audit matters. (Please refer paragraph A63 of SA 701)

Illustration of how communication needs to be made in the auditor's report when there is no key audit matter, in the key audit matters section:

<< We have determined that there are no key audit matters to communicate in our report. >>

Question 27: Can there be a situation wherein apart from a modification, there is no other key audit matter that the auditor has identified for communication in his report?

Response 27: Yes, such a situation may arise. If the auditor determines, depending on the facts and circumstances of the entity and the audit, that the only key audit matters for communication are those matters that relate to a modification, the auditor shall include a statement to this effect under the heading Key Audit Matters in his report.

Illustration:

In the key audit matters section, the auditor to state:

<<Except for the matter described in the Basis for Qualified (Adverse) Opinion section or Material Uncertainty Related to Going Concern section, we have determined that there are no other key audit matters to communicate in our report.>>

Question 28: Whether Key Audit Matters section is required to be given in cases where no key audit matter has been determined by the auditor?

Response 28: Yes. In fact, SA 701 prescribes three situations in which Key Audit Matters section will be given but no key audit matter will be communicated under that section. These situations are as under:

Implementation Guide to SA 701

1. Auditor determines that there is no key audit matter to be communicated.
2. Auditor determines that a key audit matter should not be communicated due to restrictions in paragraph 14 of SA 701 and no other key audit matter has been determined by him.
3. The only key audit matter determined by the auditor is a matter giving rise to modified opinion or a material uncertainty related to going concern.

Question 29: What is the interplay between Emphasis of Matter paragraph and Key audit matter?

Response 29: When SA 701 applies, the use of Emphasis of Matter paragraphs is not a substitute for a description of individual key audit matters. In other words, when a matter has been determined to be a key audit matter, the auditor is required to include the matter in the auditor's report in accordance with SA 701. The auditor should not use an Emphasis of Matter paragraph or Other Matter paragraph to highlight the matter instead of the requirements in SA 701 and Emphasis of Matter paragraph or an Other Matter paragraph cannot be used as a substitute for reporting the matter as a key audit matter.

Further, matters that are determined to be key audit matters in accordance with SA 701 may also be, in the auditor's judgment, fundamental to users' understanding of the financial statements. In such cases, in communicating the matter as a key audit matter in accordance with SA 701, the auditor may wish to highlight or draw further attention to its relative importance. The auditor may do so by presenting the matter more prominently than other matters in the Key Audit Matters section (e.g., as the first matter) or by including additional information in the description of the key audit matter to indicate the importance of the matter to users' understanding of the financial statements.

There may be a matter that is not determined to be a key audit matter in accordance with SA 701 (i.e., because it did not require significant auditor attention), but which, in the auditor's judgment, is fundamental to users' understanding of the financial statements

(e.g., a subsequent event). If the auditor considers it necessary to draw users' attention to such a matter, the matter is included in an Emphasis of Matter paragraph in the auditor's report in accordance with SA 706 (Revised).

For example, when the auditor concludes in accordance with SA 570 (Revised) that no material uncertainty exists relating to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern, the auditor may nevertheless determine that one or more matters relating to this conclusion arising from the auditor's work effort under SA 570(Revised) are key audit matter(s). In such circumstances, the auditor's description of such key audit matters in the auditor's report could include aspects of the identified events or conditions disclosed in the financial statements, such as substantial operating losses, available borrowing facilities and possible debt refinancing, or non-compliance with loan agreements, and related mitigating factors. (Please refer paragraph A41 of SA 701)

Question 30: Will matters relating to going concern now be reported as key audit matter as required by SA 701 or an Emphasis of Matter as required by SA 570 (Revised) or SA 706(Revised)?

Response 30:

Scenario 1: Material Uncertainty w.r.t. Going Concern exists

In the event of existence of a material uncertainty that casts a significant doubt on the entity's ability to continue as a going concern in the foreseeable future, the same by nature would be a key audit matter. There could be 2 situations here. First, where adequate disclosure about the material uncertainty is made in the financial statements and second, where adequate disclosure about the material uncertainty is not made in the financial statements.

Reporting in Situation 1

If adequate disclosure about the material uncertainty is made in the financial statements, the auditor shall express an unmodified opinion and the material uncertainty is required to be disclosed separately under a separate section 'Material uncertainty related

Implementation Guide to SA 701

to going concern', after 'Basis for Opinion' paragraph as required by SA 570 (Revised). In the case of a listed entity, in addition to the disclosure under the aforesaid separate section, under the key audit matters section also, the auditor is required to make a reference. Therefore, in the event of a material uncertainty, when an Emphasis of Matter paragraph used to be provided earlier has now been replaced with inclusion as a separate paragraph with heading 'Material uncertainty related to going concern' and would no longer be an Emphasis of Matter paragraph.

Illustration: In the auditor's report having unmodified opinion:

<<Material Uncertainty Related to Going Concern

We draw attention to Note XX in the financial statements, which indicates that the Company incurred a net loss of ZZZ during the year ended March 31, 20X1 and, as of that date, the Company's current liabilities exceeded its total assets by YYY. These events or conditions, along with other matters as set forth in Note XX, indicate that a material uncertainty exists that may cast significant doubt on the Company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In addition to the matter described in the *Material Uncertainty Related to Going Concern* section, we have determined the matters described below to be the key audit matters to be communicated in our report.

[Description of each key audit matter in accordance with SA 701]>>

Reporting in Situation 2

If adequate disclosure about the material uncertainty is not made in the financial statements, the auditor shall express a qualified or

adverse opinion, as appropriate, in accordance with SA 705(Revised). In the Basis for Qualified (Adverse) Opinion section the auditor shall state that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the financial statements do not adequately disclose this matter.

Illustration: In the auditor's report having qualified or adverse opinion:

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In addition to the matter described in the Basis for Qualified Opinion Section (or basis for Adverse Opinion section), we have determined the matters described below to be the key audit matters to be communicated in our report.

[Description of each key audit matter in accordance with SA 701.]

Scenario 2: Material Uncertainty w.r.t. Going Concern does not exist

If events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern but, based on the audit evidence obtained the auditor concludes that no material uncertainty exists, the auditor shall evaluate whether, in view of the requirements of the applicable financial reporting framework, the financial statements provide adequate disclosures about these events or conditions.

Under such circumstance, in the case of a listed entity, the same may be considered as a key audit matter. Further, it may also be fundamental to the understanding of the financial statements. Under such circumstance, it may be placed as the first key audit matter to denote its importance. In such circumstances, the auditor's description of such key audit matters in the auditor's report could include aspects of the identified events or conditions disclosed in the financial statements, such as substantial operating losses, available borrowing facilities and possible debt

Implementation Guide to SA 701

refinancing, or non-compliance with loan agreements, and related mitigating factors.

Question 31: Can there be circumstances in which a matter determined to be a key audit matter is not communicated in the auditor's report?

Response 31: Yes, under the following circumstances a matter determined to be a key audit matter is not communicated in the auditor's report:

- Law or regulation precludes public disclosure about the matter;
- In extremely rare circumstances, the auditor determines that the matter should not be communicated in the auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication. This shall not apply if the entity has publicly disclosed information about the matter.

When the auditor concludes not to communicate a key audit matter in the auditor's report, the auditor may consider it necessary to obtain a written representation from management, as to why public disclosure about the matter is not appropriate, including management's view about the significance of the adverse consequences that may arise as a result of such communication.

Reference may be made to paragraphs A52 to A56 of SA 701 in this regard.

Question 32: How should the auditor deal with significant matters that may not have been publicly disclosed by the entity?

Response 32: The auditor's reporting standards provide guidance for communicating matters that meet the definition of key audit matters, as the overall aim of communicating key audit matters is to provide greater transparency to users of the auditor's report. Such matters must be included in the auditor's report unless law or regulation precludes public disclosure about the matter or, in extremely rare circumstances, the auditor determines that the matter should not be communicated in the auditor's report

because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

There may be matters that meet the definition of key audit matters (i.e., because they required significant auditor attention) but for which information has not been publicly disclosed by the entity (i.e. “sensitive matters”). One example may be an alleged fraud or illegal act, which involved a significant amount of attention by the auditor, management and audit committee but was ultimately resolved without issue. Another example may arise when underlying events or conditions exist that raise questions about the entity’s ability to continue as a going concern, but management and the auditor conclude that no material uncertainty related to going concern exists.

In the absence of a conclusion that a material uncertainty exists, communicating a key audit matter related to a going concern “close call” may be difficult. However, the auditor may include a key audit matter describing an underlying event or condition (for example, a significant debt obligation that will need to be refinanced) that received significant auditor attention and was disclosed in the financial statements. In addition, SA 570(Revised), “Going Concern” promotes greater auditor’s emphasis on disclosures in the financial statements in “close call” situations. The auditor’s decision not to communicate a “sensitive matter” would be based upon full consideration of the facts and circumstances, along with discussions with management and the audit committee about the possibility of public disclosure by the entity about the matter.

Question 33: On determination of a matter to be a key audit matter, how should the same be described in the auditor’s report?

Response 33: The description of each key audit matter in the Key Audit Matters section of the auditor’s report shall include a reference to the related disclosure(s), if any, in the financial statements and shall address:

Implementation Guide to SA 701

- Why the matter was considered to be one of most significance in the audit and therefore determined to be a key audit matter; and
- How the matter was addressed in the audit.

The adequacy of the description of a key audit matter is a matter of professional judgment. The description of a key audit matter is intended to provide a succinct and balanced explanation to enable intended users to understand why the matter was one of most significance in the audit and how the matter was addressed in the audit. Limiting the use of highly technical auditing terms also helps to enable intended users who do not have a reasonable knowledge of auditing to understand the basis for the auditor's focus on particular matters during the audit. The nature and extent of information provided by the auditor is intended to be balanced in the context of the responsibilities of the respective parties (i.e., for the auditor to provide useful information in a concise and understandable form, while not inappropriately being the provider of **original information** about the entity).

Original information is any information about the entity that has not otherwise been made publicly available by the entity (e.g., has not been included in the financial statements or other information available at the date of the auditor's report, or addressed in other oral or written communications by management or those charged with governance, such as a preliminary announcement of financial information or investor briefings). Such information is the responsibility of the entity's management and those charged with governance. It is appropriate for the auditor to seek to avoid the description of a key audit matter inappropriately providing original information about the entity. The description of a key audit matter is not usually of itself original information about the entity, as it describes the matter in the context of the audit. However, the auditor may consider it necessary to include additional information to explain why the matter was considered to be one of most significance in the audit and therefore determined to be a key audit matter, and how the matter was addressed in the audit, provided that disclosure of such information is not precluded by law or regulation. When such information is determined to be necessary by the auditor, the auditor may encourage management or those charged with governance to disclose

additional information, rather than the auditor providing original information in the auditor's report.

The following paragraphs provide an insight on how key audit matters are to be described:

Description of individual key audit matters:

- **Why was the matter considered to be a key audit matter**
 - a) Factors that led to the conclusion for considering it as a key audit matter.
 - b) Circumstances of the industry and aspects specific to the entity.
 - c) Economic conditions, new or emerging accounting policies, changes in entity's strategy or business model.

It is important to describe why the key audit matter is considered to be of most significance in the audit; the related guidelines are as below:

- Include a precise, concise and entity-specific explanation about the nature of the matter. In many cases, a key audit matter will relate to an account, line item, or event included in the financial statements; however, identification of the account or "headline" alone is not a sufficient description of the nature of the matter. Further, the title of an item in the financial statements is not truly the substance of the key audit matter; the nature of a key audit matter typically consists of the specific audit issue(s) or risks related to that account or line item, which should be specifically and precisely identified.
- Provide a clear rationale for the auditor's selection of the matter as one of most significance in the audit. This rationale is entity-specific, in that it explains why the key audit matter was most significant in the audit of the particular entity. This generally includes more than an explanation of the magnitude of the account balance since magnitude alone is not the basis for selection of the key audit matter.

- **How the matter was addressed in the audit**

- a) Aspects of the auditor's response or approach relevant to the matter or specific to the assessed risk of material misstatement.
- b) Brief overview of procedures performed.
- c) Indication of outcome of the auditor's procedures.
- d) Key observations with respect to the matter.

Auditor's description of how the matter was addressed in the audit typically consists of a brief overview of audit procedures performed. The three primary objectives for this description are that it:

- Reflects the actual audit work performed. The audit procedures performed for a key audit matter should be adequately summarized to provide an explanation of actual audit work performed that is more than what is actually in the workpapers.
- Demonstrates responsiveness to the nature of the key audit matter. There should be a close correlation between the description of nature of the key audit matter and the description of how the matter was addressed in the audit.
- Includes details specific to the audit. Although it is important that there is a level of consistency in how certain procedures are described, it is essential that the description includes details that are specific to how these procedures were executed for the particular audit. This may include, for example: details about specific business units or segments, assumptions, or management's calculations or models; the involvement of certain specialists; or particular internal or external information that the auditor used in performing his procedures.

- **Reference to the related disclosures, if any**

At a minimum, the auditor should include the title of the note and the applicable index or reference. The auditor may include page number(s) to assist readers in locating the disclosures. The auditor may also refer to elements of a disclosure when such elements are most relevant to the nature of the key audit matter, in which case the auditor refers

to the relevant paragraphs, sub-headings or tables within the applicable note(s). The auditor does not make reference to Other Information included in an annual report or similar documents (i.e. data and disclosures outside of the financial statements).

Question 34: Should conclusions be provided for every key audit matter?

Response 34: No, it is not mandatory to provide conclusions for every key audit matter, because the ultimate audit conclusions are provided in the auditor's opinion on the financial statements. However, if an auditor chooses to provide a conclusion for every key audit matter, he may do so.

The auditor may also provide an indication of the outcome of the auditor's response in the description of the key audit matter in the auditor's report. However, if this is done, care is needed to avoid the auditor giving the impression that the description is conveying a separate opinion on an individual key audit matter or that in any way may call into question the auditor's opinion on the financial statements as a whole. (Please refer paragraph A51 of SA 701)

Question 35: Should the key audit matters be provided in any specific order?

Response 35: There is no specific order in which key audit matters are required to be communicated in the auditor's report. The order of presentation of individual matters within the Key Audit Matters section is a matter of professional judgment. For example, such information may be organized in order of relative importance, based on the auditor's judgment, or may correspond to the manner in which matters are disclosed in the financial statements. (Please refer paragraph A32 of SA 701)

Question 36: What is the effect, if any, on the key audit matter previously communicated in the auditor's report in circumstances when the auditor reissues the report or amends the report previously issued?

Response 36: In certain circumstances under SA 560⁴, the auditor may be required to issue a new auditor's report or amend

⁴ SA 560, Subsequent Events.

Implementation Guide to SA 701

the auditor's report previously issued. For example, this may occur when facts become known to the auditor after the financial statements have been issued that may have caused the auditor to amend the auditor's report had such facts been known to the auditor at the date of the auditor's report. In this circumstance, if management amends the financial statements, SA 560 requires that an Emphasis of Matter (EOM) paragraph or Other Matter (OM) paragraph be included in the new or amended auditor's report that refers to a note to the financial statements that more extensively discusses the reason for the amendment of the previously issued financial statements and to the earlier report provided by the auditor.

Although the auditor is required to include an EOM or OM paragraph in the auditor's report to comply with the requirement of SA 560, SA 706(Revised) indicates that an EOM or OM paragraph cannot be a substitute for a KAM when KAM are communicated. In circumstances where the auditor reissues the auditor's report, the auditor therefore may also need to consider whether the matter that has resulted in the new or amended auditor's report (i) gives rise to an additional KAM that should be communicated, or (ii) relates to a matter previously communicated as a KAM and whether revisions to the description of that KAM are therefore necessary. Other matters previously communicated as KAM are not likely to be affected because such matters were previously determined to be matters of most significance in the audit for purposes of the original auditor's report.

Considering whether any updates to the KAM may be necessary, in addition to the EOM or OM paragraph required by SA 560, relates to the objective of communicating KAM. The description of a KAM is intended to provide additional information to intended users of the financial statements beyond what is included in an EOM paragraph (i.e., more than a reference to the matter being emphasized and to relevant disclosures in the financial statements). The auditor also may consider cross-referencing the respective descriptions in the EOM or OM paragraph and the updated KAM in the auditor's report to clarify that both are in respect of the same matter.

Question 37: How should an auditor address the requirements of SA 701 in the case of consolidated financial statements, especially where SA 701 does not apply to some of the components?

Response 37: SA 600, 'Using the Work of Another Auditor' establishes standards to be applied in situations where a principal auditor, reporting on the financial information of an entity, uses the work of another auditor with respect to the financial information of one or more components included in the financial information of the entity. This Standard also discusses the principal auditor's responsibility in relation to his use of the work of the other auditor. Further, Guidance Note on Audit of Consolidated Financial Statements also provides guidance on the specific issues and audit procedures to be applied in an audit of consolidated financial statements. The principal auditor or the group auditor while reporting on key audit matters in accordance with SA 701 should comply with the requirements of SA 600 and the aforesaid Guidance Note.

The group auditor would be required to assess matters that in his professional judgement, are key audit matters from the perspective of consolidated financial statements. This needs to be done at the planning stage and updated during performance of the audit. With reference to the auditor's responsibility, there could be two situations in an audit of consolidated financial statements - when the parent's auditor is also the auditor of all the components to be included in the consolidated financial statements and when the parent's auditor is not the auditor of one or more components and therefore, uses the work of other auditors in the audit.

When the parent's auditor is also the auditor of all the components to be included in the consolidated financial statements, he would be required to assess matters that in his professional judgement are key audit matters from a perspective of the consolidated financial statements.

In a case where the parent's auditor is not the auditor of all the components to be included in the consolidated financial statements, the auditor of the consolidated financial statements should consider the requirements of SA 600, 'Using the Work of Another Auditor'.

Question 38: In the case of joint audits, how should the joint auditors address the requirements of SA 701?

Response 38: As per SA 299⁵, “Responsibility of Joint Auditors”, joint auditors conduct the audit jointly and report on the financial statements of the entity. Under such circumstance, at the planning stage itself, the joint auditors must agree on what the key audit matters are and update the same during performance of the audit. The joint auditors should identify key audit matters for their respective area of responsibility since in respect of audit work divided among the joint auditors, each joint auditor is responsible only for the work allocated to him.

Further, there could be some common areas of work wherein all the joint auditors will be jointly and severally responsible e.g. in respect of the audit work which is not divided among the joint auditors and is carried out by all of them. The reporting of key audit matter paragraphs should be made jointly by the joint auditors in the auditor’s report, however the supporting for work done in this regard would be separate. Further, where the joint auditors are in disagreement with regard to any key audit matter to be covered by the report, each one of them should report the matter in the separate report in accordance with the requirements of SA 299.

Question 39: What are some examples of key audit matters?

Response 39: Some examples of key audit matters are:

- Certain complex areas relating to revenue recognition.
- Provisions and contingencies.
- Taxation matters (multiple tax jurisdictions, uncertain tax positions, deferred tax assets).
- Assessment of impairment.
- Put arrangements over non-controlling interests.
- IT systems and controls.

⁵ Reference may also be made to the requirements of SA 299(Revised), “Joint Audit of Financial Statements” which is applicable for audits of financial statements for periods beginning on or after April 1, 2018.

In short, areas where there are significant estimates / judgements involved, where the auditor had the need to use experts, where the auditor had the need to seek consultation, where there are significant transactions with related parties that are outside the normal course of business, any matter that has the potential to have a significant effect on the auditor's overall strategy, are good starting points in determining key audit matters.

Question 40: Does the auditor has an obligation to communicate to those charged with governance the key audit matters that he has identified for communication in the auditor's report?

Response 40: The auditor is required to communicate with those charged with governance:

- Those matters the auditor has determined to be the key audit matters; or
- If applicable, depending on the facts and circumstances of the entity and the audit, the auditor's determination that there are no key audit matters to communicate in the auditor's report.

Question 41: What are the documentation requirements to be maintained by the auditor with respect to SA 701?

Response 41: The auditor shall include in the audit documentation:

- The matters that required significant auditor attention as determined in accordance with paragraph 9 of SA 701, and the rationale for the auditor's determination as to whether or not each of these matters is a key audit matter in accordance with paragraph 10 of SA 701;
- Where applicable, the rationale for the auditor's determination that there are no key audit matters to communicate in the auditor's report or that the only key audit matters to communicate are those matters addressed by paragraph 15 of SA 701;
- Where applicable, the rationale for the auditor's determination

Implementation Guide to SA 701

not to communicate in the auditor's report a matter determined to be a key audit matter; and

- Where applicable, a written representation from management as to why public disclosure about a matter determined to be a key audit matter is not appropriate, including management's view about the significance of the adverse consequences that may arise as a result of such communication.

In this regard, it is important to note that as per this Standard, auditors are not required to document why other matters communicated with those charged with governance were not matters that required significant auditor attention. (Please refer paragraph A64 of SA 701)

Appendix

Illustrative Examples of Key Audit Matters

A. Accounting for lease rental income

Description of Key Audit Matter

Lease rental income amounted to INR XXXX million for the year ended 31 March 2018. Generally lease revenue is recognized net of discount, in accordance with the terms of lease contracts over the lease term on a straight line basis using a standard IT system implemented in late 2017. Also there are few lease arrangements where revenue recognition is not subject to straight line basis depending on the nature of the lease arrangements and performance of the lease. There is an inherent risk around the accuracy of the revenue recorded given the complexity of the IT system and impact of the terms of lease agreements to the revenue recognition. Within case of rental income, there are also specific arrangements related to (i) rent income computed by reference to lease turnover and (ii) tenant incentives and guaranteed rent increases which warrant additional audit focus as they involve high level of management estimates and judgments and hence have an increased inherent risk of error due to the non-standard nature of such transactions.

Description of Auditor's Response

Our audit procedures included considering the appropriateness of the Company's revenue recognition accounting policies and assessing compliance with the policies in terms of the applicable accounting standards.

We performed test of controls, assisted by our IT specialists, over revenue recognition with specific focus on whether lease income is recorded over the lease term on a straight line basis or other applicable basis as per the terms of the lease contract. We performed tests of details, on a sample basis, to review the case contracts entered into with the customers to assess whether lease income recorded is as per the contract terms and also to identify

any non-standard lease clauses and to assess the appropriateness of the rental income accounting. We assessed the completeness of lease rental income recorded during the year through matching the data used in the revenue recognition to the approved lease agreements with the customers. We also performed detailed substantive analytical procedures of case rental income and the timing of its recognition.

Regarding rent income calculated from lessee turnover, we performed test of controls and matched the working to the reports received from lessees and where no reports were available, we tested management estimates. For tenant incentives and guaranteed rent increases, we matched it to the lease agreements as per the sample and tested management estimates.

B. Revenue recognition

Description of Key Audit Matter

Revenue from rendering of container handling services is recognised and accrued with reference to the throughput handled and the terms of agreements for such service. For the year ended 31 March 2018, revenue from container handling services amounting to INR XXXX million is recognised based on the containers handled as well as the tariff applied. The tariff applied is the rate agreed with customers or estimated by management based on the latest terms of the agreement or latest negotiation with customers and other industry considerations as appropriate.

Due to the large variety and complexity of contractual terms, as well as ongoing negotiations with customers, significant judgements are required to estimate the tariff rates applied. If the actual rate differs from the estimated rate applied, this will have an impact on the accuracy of revenue recognised in the current year and accrued as at year end.

Description of Auditor's Response

We have performed the following procedures in relation to the accuracy of revenue recognised and accrued:

- Understood, evaluated and tested the key controls over the tariff applied in container handling services. We selected a sample of transactions and:
- Agreed the applied tariff to the respective terms in the contracts or latest correspondence with customers where the tariff has been estimated by management.
- Agreed throughput handled, used in the calculation of tariffs, to the operating system recording throughput.
- Tested revenue calculations and agreed the revenue recognised to the underlying accounting records.
- Checked the bank advices or credit notes on a sample basis for the net settlement and reviewed aged items for any disputed amounts.

C. Going concern assessment - Effect of volatility in precious metal prices

Description of Key Audit Matter

The recent volatility and decline in spot and forward precious metal prices may create doubt about the Group's and parent Company's ability to continue as a going concern.

The Group and parent Company financial statements were prepared on a going concern basis. Management's statement in respect of going concern is set out in Note X to the financial statements.

Description of Auditor's Response

- We analysed management's report to gain an understanding of the inputs and process underpinning the cash flow model prepared for the purpose of the going concern assessment.
- We assessed the budgeting process by walking through the conversion of reserves and resources data into mine plans and production figures and by comparing actual realised cost levels to budgeted cost assumptions.

Implementation Guide to SA 701

- We verified that the cash flow model accurately reflects the approved 2017 budget and that the assumptions underpinning the 2018 cash flows are consistent with those in the 2017 budget.
- We evaluated the external inputs and assumptions within the going concern model by comparing them to assumptions and estimates used elsewhere in the preparation of the financial statements and benchmarking them against market observable external data.
- We assessed the sensitivities and stress testing that management performed on the going concern forecast.
- We assessed the possible mitigating actions identified by management in the event that actual cash flows are below forecast.

D. Going concern assumption, financing and covenants

Description of Key Audit Matter

The availability of sufficient funding and the testing of whether the company will be able to continue meeting its obligations under the financing covenants are important for the going concern assumption and, as such, are significant aspects of our audit. This test or assessment is largely based on the expectations of and the estimates made by management. The expectations and estimates can be influenced by subjective elements such as estimated future cash flows, forecasted results and margins from operations. Estimates are based on assumptions, including expectations regarding future developments in the economy and the market.

Description of Auditor's Response

We have used our own internal experts in evaluating the assumptions and forecasts made by management in the 2017 Budget and the 2018-2019 Mid-Term Plan. We have specifically devoted attention to the assumptions made with respect to the future value added, the results and the cash flows in order to

assess the company's ability to continue meeting its payment obligations and its obligations under the financing covenants in the year ahead.

For notes on the going concern assumption and financing requirements, see the going concern principle section on page xx and notes xx and xx of the financial statements respectively.

E. Carrying value of goodwill

Description of Key Audit Matter

ABC Group has goodwill of INR XXX million contained within 22 cash generating units ('CGUs').

Impairment charges to goodwill have been recognised in prior periods. With challenging trading conditions continuing in certain territories, the Group's performance and prospects could be impacted increasing the risk that goodwill is impaired.

For the CGUs that contain goodwill, the determination of recoverable amount, being the higher of fair value less costs to sell and value-in-use, requires judgement on the part of management in both identifying and then valuing the relevant CGUs. Recoverable amounts are based on management's view of variables such as future average revenue per user, average customer numbers and customer churn, timing and approval of future capital, spectrum and operating expenditure and the most appropriate discount rate.

In the year ended 31 March 2018, a pre-tax impairment charge of INR XX million was recognised related to goodwill in Romania.

Refer to the note XX – critical accounting judgements and key sources of estimation uncertainty, note X – Impairment losses and note XX – Intangible assets.

Description of Auditor's Response

We evaluated the appropriateness of management's identification of the Group's CGUs and the continued satisfactory operation of the Group's controls over the impairment assessment process.

Implementation Guide to SA 701

Our procedures included discussion with management on the suitability of the impairment model and reasonableness of the assumptions, with particular attention paid to the European businesses, through performing the following:

- benchmarking company's key market-related assumptions in management's valuation models with industry comparators and with assumptions made in the prior years including revenue and margin trends, capital expenditure on network assets and spectrum, market share and customer churn, foreign exchange rates and discount rates, against external data where available, using our valuation expertise;
- testing the mathematical accuracy of the cash flow models and agreeing relevant data to Board approved Long-Range Plans; and
- assessing the reliability of management's forecast through a review of actual performance against previous forecasts.

We validated the appropriateness of the related disclosures in note X and note XX of the financial statements, including the sensitivities provided with respect to Germany, Spain, and Romania.