

STAFF GUIDANCE



Implementation of Critical Audit Matters: The Basics

Overview

Requirements for auditors to communicate critical audit matters (CAMs) in the auditor's report will phase in starting in 2019, based on the PCAOB's new standard, [AS 3101, *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion*](#). The determination of CAMs is principles-based and depends on the facts and circumstances of each audit.

The Board adopted these changes to inform investors and other financial statement users about significant matters in the audit and how they were addressed. This document provides a high-level overview of the CAM requirements based on [PCAOB Release No. 2017-001](#).

What is a CAM?

A CAM is defined as any matter arising from the audit of the financial statements that was communicated or required to be communicated to the audit committee and that:

- ⦿ Relates to accounts or disclosures that are material to the financial statements; and
- ⦿ Involved especially challenging, subjective, or complex auditor judgment.

Matters communicated or required to be communicated to the audit committee

CAMs are drawn from matters required to be communicated to the audit committee—even if not actually communicated—and matters actually communicated—even if not required.

The standard does not exclude any required audit committee communications from the source of CAMs.

Relates to accounts or disclosures that are material to the financial statements

A CAM is required to relate to accounts or disclosures that are material to the financial statements. A CAM may relate to a component of a material account or disclosure and does not necessarily need to correspond to the entire account or disclosure in the financial statements.

What's included?

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When are CAM requirements effective?

- ⦿ Audits of large accelerated filers: Fiscal years ending on or after June 30, 2019.
- ⦿ Audits of all other companies to which the requirements apply: Fiscal years ending on or after December 15, 2020.

This guidance was prepared by PCAOB staff to help firms when implementing CAM requirements. This staff guidance document sets forth the staff's views on issues related to the implementation of the rules and standards of the PCAOB. It does not constitute rules of the Board, nor has it been approved by the Board. It supplements PCAOB Release No. 2017-001, *The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion and Related Amendments to PCAOB Standards* (June 1, 2017).

A CAM may not necessarily relate to a single account or disclosure, but could have a pervasive effect on the financial statements if it relates to many accounts or disclosures. A matter that does not relate to a material account or disclosure cannot be a CAM.

Involved especially challenging, subjective, or complex auditor judgment

The standard provides a list of factors for the auditor to take into account when determining whether a matter involved especially challenging, subjective, or complex auditor judgment:

- ⦿ The auditor’s assessment of the risks of material misstatement, including significant risks
- ⦿ The degree of auditor judgment related to areas in the financial statements that involved the application of significant judgment or estimation by management, including estimates with significant measurement uncertainty
- ⦿ The nature and timing of significant unusual transactions and the extent of audit effort and judgment related to these transactions
- ⦿ The degree of auditor subjectivity in applying audit procedures to address the matter or in evaluating the results of those procedures
- ⦿ The nature and extent of audit effort required to address the matter, including the extent of specialized skill or knowledge needed or the nature of consultations outside the engagement team regarding the matter
- ⦿ The nature of audit evidence obtained regarding the matter

The auditor should also take into account other factors specific to the audit.

Communication of CAMs

When communicating CAMs in the auditor’s report, the auditor is required to include introductory language in the “Critical Audit Matters” section of the auditor’s report.

For each CAM communicated in the auditor’s report, the auditor must:

- ⦿ Identify the CAM;
- ⦿ Describe the principal considerations that led the auditor to determine that the matter is a CAM;
- ⦿ Describe how the CAM was addressed in the audit; and
- ⦿ Refer to the relevant financial statement accounts or disclosures that relate to the CAM.

Identify the CAM

For each CAM communicated in the auditor’s report, the auditor is required to identify the CAM.

Describe the principal considerations that led the auditor to determine that the matter is a CAM

The description of the principal considerations should be specific to the circumstances and provide a clear, concise, and understandable discussion of why the matter involved

Which audits do not require CAMs?

CAMs are not required for audits of:

- Brokers and dealers
- Registered investment companies other than business development companies
- Employee stock purchase, savings, and similar plans
- Emerging growth companies

Auditors may early adopt CAM requirements or apply them voluntarily to audits for which they are not required.

especially challenging, subjective, or complex auditor judgment. The communication should be tailored to the audit to avoid standardized language and to reflect the specific circumstances of the matter.

Describe how the CAM was addressed in the audit

In describing how the CAM was addressed in the audit, the auditor may describe any, or a combination, of the following:

- The auditor’s response or approach that was most relevant to the matter
- A brief overview of the audit procedures performed
- An indication of the outcome of the audit procedures
- Key observations with respect to the matter

When describing CAMs in the auditor’s report, the auditor is not expected to provide information about the company that has not been made publicly available by the company unless such information is necessary to describe the principal considerations that led the auditor to determine that a matter is a CAM or how the matter was addressed in the audit.

If the auditor chooses to describe audit procedures, the descriptions are expected to be at a level that investors and other financial statement users would understand. In addition, the objective is to provide a useful summary, not to detail every aspect of how the matter was addressed in the audit.

Limiting the use of highly technical accounting and auditing terms in the description of CAMs, particularly if the auditor chooses to describe audit procedures, may help financial statement users better understand these matters in relation to the audit of the financial statements.

Language that could be viewed as disclaiming, qualifying, restricting, or minimizing the auditor’s responsibility for the CAMs or the auditor’s opinion on the financial statements is not appropriate and may not be used. The language used to communicate a CAM should not imply that the auditor is providing a separate opinion on the CAM or on the accounts or disclosures to which they relate.

Refer to the relevant financial statement accounts or disclosures that relate to the CAM

For each CAM communicated in the auditor’s report, the auditor is required to refer to the relevant financial statement accounts or disclosures.

Required Introductory Language

The CAM section of the auditor’s report is required to be titled “Critical Audit Matters.”

When communicating CAMs in the auditor’s report, the following introductory language is required to be included:

Critical Audit Matters

The critical audit matters communicated below are matters arising from the current period audit of the financial statements that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements and (2)

Which audit period is covered by CAMs?

The standard requires that CAMs only be communicated for the current audit period.

When the current period’s financial statements are presented on a comparative basis with those of one or more prior periods, the auditor may communicate CAMs relating to a prior period. This may be appropriate, for example, when:

- The prior period’s financial statements are made public for the first time, such as in an initial public offering.
- Issuing an auditor’s report on the prior period’s financial statements because the previously issued auditor’s report could no longer be relied upon.

involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matters below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

If the auditor communicates CAMs for prior periods, the introductory language should be modified to indicate the periods to which the CAMs relate.

If the auditor determines that there are no CAMs, the following language is required:

Critical Audit Matters

Critical audit matters are matters arising from the current period audit of the financial statements that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. We determined that there are no critical audit matters.

Documentation of CAMs

For each matter arising from the audit of the financial statements that:

- (1) Was communicated or required to be communicated to the audit committee; and
- (2) Relates to accounts or disclosures that are material to the financial statements;

the auditor must document whether or not the matter was determined to be a CAM (i.e., involved especially challenging, subjective, or complex auditor judgment) and the basis for such determination.

Consistent with the requirements of [AS 1215, Audit Documentation](#), the audit documentation is required to be in sufficient detail to enable an experienced auditor, having no previous connection with the engagement, to understand the determinations made to comply with the provisions of AS 3101.

- For matters determined to be CAMs, the description in the auditor's report (which, among other things, must describe the principal considerations that led the auditor to determine that a matter was a CAM) will generally suffice as documentation.
- For matters determined not to be CAMs, the amount of documentation required could vary with the circumstances. A single sentence may be sufficient, for instance, when the auditor's documentation prepared in the course of the audit includes sufficient detail about why the matter did not involve especially challenging, subjective, or complex auditor judgment. Other matters may require more extensive documentation.

Engagement Quality Reviewer (EQR)

The objective of the EQR is to perform an evaluation of the significant judgments made by the engagement team and the related conclusions reached in forming the overall conclusion on the engagement and in preparing the engagement report.

Can an audit have no CAMs?

The determination of CAMs is based on the facts and circumstances of each audit. It is expected that, in most audits to which the CAM requirements apply, the auditor will determine at least one CAM. However, there also may be audits in which the auditor determines there are no CAMs.

The EQR is required to evaluate the engagement team's determination, communication, and documentation of CAMs (see [paragraph .10j of AS 1220, Engagement Quality Review](#)). The documentation requirements for CAMs will facilitate review by the EQR.

Interactions with the Audit Committee and Management

Any matter that will be communicated as a CAM should already have been discussed with the audit committee, and the auditor is required to provide a draft of the auditor's report to the audit committee and discuss the draft with them (see [paragraph .21 of AS 1301, Communications with Audit Committees](#)).

As the auditor determines how best to comply with the communication requirements, the auditor could discuss with management and the audit committee the treatment of any sensitive information.

CAM Interaction with Explanatory and Emphasis Paragraphs

CAMs and explanatory paragraphs

CAMs are not a substitute for required explanatory paragraphs. There are circumstances in which the auditor is required to add explanatory language to the auditor's report, such as when there is substantial doubt about the company's ability to continue as a going concern or a restatement of previously issued financial statements, among others. There could be situations in which a matter meets the definition of a CAM and also requires an explanatory paragraph, such as going concern.

For these situations, both the explanatory paragraph and the required communication regarding the CAM would be provided, by either:

- Including the required communications for a CAM in the explanatory paragraph, with a cross-reference in the CAM section to the explanatory paragraph, or
- Including both the explanatory paragraph and the CAM communication separately in the auditor's report, with a cross-reference between the two sections. When both an explanatory paragraph and a CAM communication are provided, the CAM description should not include conditional language that would not be permissible in the explanatory paragraph (see [footnote 5 of AS 2415, Consideration of an Entity's Ability to Continue as a Going Concern](#)).

CAMs and emphasis paragraphs

If a matter that the auditor considers emphasizing meets the definition of a CAM, the auditor would provide the information required for a CAM, and would not be expected to include an emphasis paragraph in the auditor's report.

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