Practice aid

AICPA & CIMA

Consideration of ESG-Related Matters in an Audit of Financial Statements

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Contents

Notice to readers

Authoritative Status

This practice aid is an other auditing publication as defined in AU-C section 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards (GAAS)*,[1] and is nonauthoritative. In applying the auditing guidance included in an other auditing publication, the auditor should exercise professional judgment and assess the relevance and appropriateness of such guidance to the circumstances of the audit.

Statements on Auditing Standards (SASs)That Are Not Yet Effective

The Auditing Standards Board has issued the following SASs which are effective for audits of financial statements for periods ending on or after December 15, 2023:

- SAS No. 143, *Auditing Accounting Estimates and Related Disclosures*
- SAS No. 144, *Amendments to AU-C Sections 501, 540, and 620 Related to the Use of Specialists and the Use of Pricing Information Obtained From External Information Sources*
- SAS No. 145, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*

If the text or paragraph references in this practice aid would change as a result of SAS Nos. 143-145, a gray-shaded footnote has been inserted to identify the change and the effective date.

[1] All AU-C sections can be found in AICPA *Professional Standards*.

Introduction

Environmental, social, and governance (ESG) has become an area of increasing focus. For example, the demand by investors, regulators, and other users (stakeholders) for information about the effects of ESG-related matters on entities and their financial reporting has grown dramatically. At the same time, management is seeing the benefits of focusing on and communicating information about the risks posed by ESG-related matters as well as management's activities and plans for addressing them.

As stakeholders of financial statements place a heightened emphasis on ESG-related matters, it is important for management and auditors of financial statements to continue to consider how such matters may affect the entity's business and operating environment and whether those matters could have a material effect on the financial statements. In response to this increasing focus, the Financial Accounting Standards Board (FASB)[2] and the International Financial Reporting Standards (IFRS) Foundation,[3] have issued papers highlighting the connection between ESG-related matters and their effect on financial statements. The AICPA continues to be focused on addressing ESG matters important to practitioners, including the development of this practice aid, to help support the profession.

The terms ESG, *sustainability*, and *corporate social responsibility* are often used interchangeably, and different investors and stakeholders may describe ESG differently. For the purpose of this publication, the following is an explanation of each of the components of the ESG acronym[4]:

- The environmental component addresses how an entity is exposed to and manages risks and opportunities related to the environment, for example, climate-related matters, natural resource scarcity, pollution, waste, and an entity's impact on the environment.
- The social component encompasses information about an entity's values and business relationships and addresses topics such as fair labor practices, the use of ethically sourced material in the production of products, product quality and safety, human capital such as employee health and safety, and diversity and inclusion policies and efforts.
- The governance component of ESG encompasses information about the system of rules, practices, and processes by which an entity is directed and controlled, and addresses topics such as the structure and diversity of the board of directors, executive compensation, critical event responsiveness, entity resiliency, and policies and practices related to lobbying, political contributions, bribery, and corruption.

Although ESG can encompass a wide range of matters that may have the potential to affect an entity's financial statements, Chapter 1 of *Consideration of ESG-Related Matters in an Audit of Financial Statements* focuses on the effects of climate-related matters. The ESG Working Group will continue to convene, and as new topics are developed, this practice aid will be updated.

This practice aid does not address considerations for non-audit engagements, such as examination and review engagements performed under Statements on Standards for Attestation Engagements (attestation standards) that address ESG-related information. AICPA Guide Attestation Engagements on Sustainability Information Guide (Including Greenhouse Gas Emissions Information) provides authoritative guidance for performing examination and review engagements that address sustainability information in accordance with the attestation standards.

[2] Financial Accounting Standards Board, FASB Staff Educational Paper: Intersection of Environmental Social and Governance Matters with Financial Accounting Standards, March 2021.

[3] IFRS Foundation, Effects of climate-related matters on financial statements, November 2020.

[4] Association for International Certified Professional Accountants and Center for Audit Quality, ESG reporting and attestation: A roadmap for audit practitioners, February 2021.

Chapter 1: Consideration of Climate Related Matters in an Audit of Financial Statements

Climate change is a topic that is increasingly important to stakeholders and has the potential to affect an increasing number of entities of all types and sizes. The effect of climate-related matters on financial reporting and the external audit may vary depending on a variety of factors. For certain entities, climate-related matters are more likely to have a pervasive effect, for example, entities that insure, finance, or invest in entities that are more extensively affected by climate change. For other entities, the effects of climate-related matters may be limited to an aspect of the entity's operations, for example, its supply chain, input costs, customers, financing, insurance, or compliance with applicable laws and regulations.

Climate-related risks are often categorized as either

- physical risks arising from climate change, for example, flood, drought, and wildfire, or
- transition risks arising from the transition from an economy that relies on fossil fuels that produce greenhouse gas emissions to one that relies on alternative sources.

This chapter seeks to highlight the following:

- What the auditor needs to know about management's policies and procedures related to
  - capturing information about climate-related matters that may affect the entity's financial statements,
  - assessing the risks of material misstatement of the financial statements resulting from such matters, and
  - appropriately evaluating such matters to determine whether they may need to be reflected in the entity's financial statements.
- How the auditor may consider and evaluate management's response to climate-related matters in an audit of financial statements conducted in accordance with GAAS.[5]

Responsibilities of Management

Management is responsible for preparing the financial statements of the entity in accordance with the applicable financial reporting framework. When applying current accounting standards, entities may consider climate-related changes in their business and operating environment when those changes have a material effect on the financial statements.[6] Risks associated with climate-related changes are considered in the context of the overall environment in which the entity operates, including industry, regulatory ,and entity specific factors. The following is a description of these three types of factors:[7]

- **Industry Factors**
  Examples of industry factors include the degree of competitiveness within the industry, customer preferences, supplier relationships, and technological developments. Entities in certain industries or geographic locations may need to implement changes to enable their business activities to continue in

[5] Audits performed in accordance with the PCAOB standards are not contemplated in this practice alert.

[6] Financial Accounting Standards Board, FASB Staff Educational Paper: Intersection of Environmental Social and Governance Matters with Financial Accounting Standards, March 2021.

[7] International Auditing and Assurance Standards Board (IAASB) Staff Practice Alert, The Consideration of Climate-Related Risks in an Audit of Financial Statement, October 2020. The regulatory and business environment associated with climate-related matters continues to evolve. The guidance in this practice aid is not intended to be an exhaustive list of factors to consider when evaluating management's responses to the effect of climate-related matters on an entity's financial statements, but rather focuses on factors to consider or issues that may emerge given the current regulatory and business environment.

the event of extreme climate-related events, such as wildfires or flooding. These measures may require significant expenditures (including long-term technological improvements) and may increase operating costs. Alternatively, entities in industries that do not take such actions may be subject to business disruption and property loss.

- **Regulatory Factors**
  The regulatory environment encompasses, among other matters, the legal and political environment in which entities operate. The regulatory environment related to ESG matters continues to evolve, with a current emphasis on climate change. Some entities face uncertainty about future climate regulations. For example, some regulations may create economic disincentives for entities to continue to emit carbon by imposing levies or taxes on high-emission sources, while other regulations may seek to incentivize entities to adopt specific operating practices, such as changing to lower emission or more sustainable land-use practices. Changes in climate regulation or policy may affect a wide range of business inputs and outputs such as energy pricing, carbon taxes, mandatory emission and energy standards, and industry targets. For example, the rapid emergence of climate-related legislation in different jurisdictions means that entities need to be aware of existing or proposed climate-related laws and regulations and the extent to which those laws and regulations may affect the entity's operating, investing, and financing activities.

- **Entity Specific Factors**
  Management may need to consider entity-specific factors such as investor activism or the effects on the entity of shifting consumer preferences for environmentally friendly alternatives. For example, changes in consumer preferences may decrease the demand for certain products and create the need for the entity to obtain new technology and equipment to make innovations in its product, an accomplishment that may be dependent on another entity specific factor – the entity's ability to obtain financing.

Entities may find it helpful to consider climate-related risks within the context of the entity's overall enterprise risk management (ERM) program; doing so may assist management in developing effective responses to, and provide increased transparency about, those risks and their potential effects on the entity.[8]

Responsibilities of Those Charged With Governance

Those charged with governance have responsibility for overseeing the strategic direction of the entity and the obligations related to the accountability of the entity. This includes overseeing the financial reporting process and the external audit. As a result, those charged with governance have a role to play with respect to the consideration of climate-related risks in the context of overseeing the entity's financial reporting process. Examples of responsibilities of those charged with governance as they relate to climate-related matters may include obtaining information about management's risk assessment activities and its plans for mitigating those risks, and exploring with management how climate-related risks may affect the entity's significant accounting policies, accounting estimates, and financial statement disclosures.

Entities may be at different stages in their consideration of climate-related matters as it relates to financial reporting, and it is important for those charged with governance to understand the entity's current status with respect to such considerations and whether the entity has begun to consider future risks and opportunities that may arise as a result of climate-related matters. In addition, how this is done may vary depending on the environment in which the entity operates and changes thereto.

Those charged with governance may also want to discuss these matters with the auditor; for example, to understand how climate-related risks may be considered in the audit and to share related insights. An effective audit of the financial statements requires two-way dialogue between those charged with governance and the auditor so that the auditor can understand how risks are being identified and managed at the governance level.

[8] For additional information on considering ESG-related risks as part of enterprise risk management, please see https://www.coso.org/Documents/COSO-WBCSD-ESGERM-Executive-Summary.pdf.

Responsibilities of the Auditor

The auditor has a responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement to enable the auditor to report on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework. Climate-related risks may affect the auditor's determination of materiality in accordance with AU-C section 320, *Materiality in Planning and Performing an Audit* (See the information about AU-C 320 in Table 1, "Certain AU-C Sections Relevant to Climate-Related Matters and Examples of Such Matters" on page 11).

AU-C section 315A, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement,*[9] requires the auditor to obtain an understanding of the entity and its environment, including the entity's internal control as it relates to the audit.[10] In particular, understanding how management assesses and responds to risks (including climate-related risks) may help the auditor

- identify risks,
- determine whether the effect of such risks could give rise to the risk of material misstatement of the entity's financial statements, and
- develop appropriate audit responses to address these assessed risks.

For example, in obtaining an understanding of the entity, it's environment, and its risk assessment process, auditors may find it helpful to obtain information about the following matters:

- Whether and how the entity has considered climate-related risks and opportunities
- The extent of management's knowledge and awareness of the effects of climate-related matters on the entity, the industry, and geographic locations in which the entity operates
- Whether the entity has considered the effects of macroeconomic conditions such as inflation, which may occur when climate-related events result in, for example, a shortage of an essential component of a product, reducing the availability of the product, causing the price of the product to rise, and in some cases, causing consumers to move on to a replacement product
- The process management has used to identify aspects of its operations, suppliers, or markets that may be affected by shifts in consumer preferences towards environmentally friendly alternatives, the transition to low-carbon economies, and the transition by the entity itself to low-carbon alternatives
- The time horizon management has used in considering climate-related risks
- How the financial impacts of identified risks have been assessed and incorporated into financial budgeting, projections, and the financial reporting process
- What management has done to ensure that it complies with emerging climate-related regulations and meets requirements regarding climate-related disclosures in the entity's financial statements, including determining whether it has a reasonable basis for information presented or disclosed in the entity's financial statements
- Management's decarbonization plan, if applicable.

In accordance with paragraph .06 of AU-C section 315A,[11] risk assessment procedures should include inquiries of management and other appropriate individuals within the entity, including individuals within the internal audit function (if the function exists). In obtaining an understanding of the aforementioned matters, other appropriate individuals that the auditor may make inquiries of are individuals within operations, legal, or product development. In addition, reviewing one or more internal or external sources (for example, climate-related

[9] SAS No. 145, Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement is codified in AU-C section 315 of the same title and will supersede AU-C section 315A once effective. SAS No. 145 is effective for audits of financial statements for periods ending on or after December 15, 2023. Gray shaded content in this practice aid denotes new standards that are not yet effective.

[10] SAS No. 145 elevates the importance of understanding the applicable financial reporting framework and restructures the relevant requirements in AU-C section 315A. Under SAS No. 145, this sentence would be replaced with "AU-C section 315 requires the auditor to obtain an understanding of the entity and its environment, the applicable financial reporting framework, and the entity's system of internal control as it relates to the audit."

[11] Paragraph .14 of AU-C section 315 arising from SAS No. 145 contains similar requirements. SAS No. 145 is effective for audits of financial statements for periods ending on or after December 15, 2023.

information disclosed in other information, separately produced sustainability reports, or management communications through press releases and website content) may provide the auditor with an understanding of climate-related matters that may affect the entity and its environment.

The knowledge obtained from risk assessment procedures forms the basis for identifying risks including climate-related risks that could affect the entity and its financial statements, and for evaluating whether such risks give rise to a risk of material misstatement. Auditing standards require auditors to design and implement overall responses to address the assessed risks of material misstatement at the financial statement level and to design and perform further audit procedures whose nature, timing, and extent are based on, and responsive to, the assessed risks of material misstatement at the relevant assertion level.

In addition to risk assessment, the consideration of climate related matters may be relevant to other aspects of the audit. Table 1, "Certain AU-C Sections Relevant to Climate-Related Matters and Examples of Such Matters" on page 9 addresses some AU-C sections that might be relevant to climate-related matters considered in an audit of financial statements.

Table 1: Certain AU-C Sections Relevant to Climate-Related Matters and Examples of Such Matters

AU-C section	Examples of climate-related matters that may be relevant when applying the identified AU-C section
Risk assessment and response to assessed risk	
AU-C sec. 315A, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement* Requires the auditor to • identify and assess the risks of material misstatement in the financial statements through understanding the entity and its environment, including the entity's internal control. • perform risk assessment procedures[12] to provide a basis for the identification and assessment of risks of material misstatement at the financial statement and relevant assertion levels. If the auditor determines that risks of material misstatement represent a significant risk as described in paragraphs 28-29 of AU-C 315A,[13] the auditor is required by AU-C 260.11 to communicate that to those charged with governance as well as take other steps as outlined in AU-C 315A.	The following are some of the matters that AU-C sec. 315A requires the auditor to obtain an understanding of, and examples of how they might relate to climate-related events or conditions: • Relevant industry, regulatory, and other external factors, including the applicable financial reporting framework[14] – For an automobile manufacturer, an industry trend toward manufacturing electric vehicles and phasing out the production of vehicles that use fossil fuels. – For a mining entity, the enactment of new climate-related laws and regulations, the violation of which could result in penalties or the suspension of business. – For a hotel located on a coast, a rise in the sea level and erosion of beaches that makes the hotel a less attractive destination.

[12] Paragraph .06 of AU-C section 315A states that risk assessment procedures should include the following:

a. Inquiries of management, appropriate individuals within the internal audit function (if such function exists) others within the entity who, in the auditor's professional judgment, may have information that is likely to assist in identifying risks of material misstatement due to fraud or error (Paragraph .14a of AU-C section 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement* (SAS No. 145) changes this sentence to "inquiries of management and of other appropriate individuals within the entity, including individuals within the internal audit function (if the function exists). SAS No. 145 is effective for audits of financial statements for periods ending on or after December 15, 2023, with early implementation permitted.)
b. Analytical procedures
c. Observation and inspection

[13] See paragraph .32 of AU-C section 315 (SAS No. 145).

[14] See paragraph .19a.ii. of AU-C section 315 for corresponding requirements from SAS No. 145. SAS No. 145 is effective for audits of financial statements for periods ending on or after December 15, 2023.

AU-C section	Examples of climate-related matters that may be relevant when applying the identified AU-C section
Risk Assessment and Response to Assessed Risk	
	• The nature of the entity including its operations – The entity produces a product that requires a part that has become either unavailable or overpriced due to climate-related matters occurring in the part of the world where it is produced. – A commercial real estate company owns properties located in areas subject to climate-related events and is required to pay above market for financing. – An agricultural producer is affected by the occurrence of drought that reduces yields or volume. • The entity's objectives, strategies, and related business risks that may result in risks of material misstatement – The entity has begun to develop electric vehicles using a labor force that is relatively new to this technology, increasing the risk that the vehicles will be defective. The entity has no track record in manufacturing and selling electric vehicles, which increases estimation uncertainty when determining the provision for warranty claims. – A manufacturer is implementing its net zero commitment to decrease its greenhouse gas emissions by a specified date, which affects almost every aspect of its manufacturing process. – An online retailer is replacing the Styrofoam packaging it uses to ship its products with biodegradable packaging. The retailer hired a consultant to advise the company regarding the most suitable packaging materials and is phasing out the Styrofoam packaging in favor of the biodegradable packaging, which is made of plant matter. The biodegradable packaging is more costly and requires a change in packaging machinery and process.

[15] See paragraph .19a.i. of AU-C section 315 for corresponding requirements from SAS No. 145. SAS No. 145 is effective for audits of financial statements for periods ending on or after December 15, 2023.

AU-C section	Examples of climate-related matters that may be relevant when applying the identified AU-C section
Risk assessment and response to assessed risk	
AU-C sec. 320, *Materiality in Planning and Performing an Audit* Addresses the auditor’s responsibility to apply the concept of materiality in planning and performing an audit of financial statements. Misstatements, including omissions, are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.	The auditor’s determination of materiality is a matter of professional judgment and is affected by the auditor’s perception of the financial information needs of users of the financial statements. Auditors of entities that are affected by climate-related risks may take that into account when determining materiality.
AU-C sec. 330, *Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained* Addresses the auditor’s responsibility to design and implement responses to the risks of material misstatement identified and assessed by the auditor in accordance with AU-C sec. 315A[16] and to evaluate the audit evidence obtained in an audit of financial statements.	The nature, timing and extent of the audit procedures performed to respond to risks of material misstatement associated with climate-related matters is a matter of professional judgment and is dependent on the nature of the assessed risk. The following are examples of further audit procedures an auditor might perform to respond to an assessed risk of material misstatement affected by climate-related matters: • Obtaining third party forecasts of future demand for refined petroleum products to evaluate the potential impairment of assets for an oil and gas refinery • Holding discussions with the entity’s attorneys regarding climate-related matters and conducting a search for climate litigation and claims brought against the entity to respond to the risk that provisions could be understated or that contingent liability disclosures may be omitted • Determining if management has adjusted the residual valuation of equipment and related depreciation expense to reflect a decreased demand for the entity’s product and the shortened useful life of equipment used to produce it.

[16] See AU-C section 315 for requirements under SAS No. 145. SAS No. 145 is effective for audits of financial statements for periods ending on or after December 15, 2023.

AU-C section	Examples of climate-related matters that may be relevant when applying the identified AU-C section
Risk assessment and response to assessed risk	
AU-C sec. 250, *Consideration of Laws and Regulations in an Audit of Financial Statements* Addresses the auditor's responsibility to consider laws and regulations in an audit of financial statements. AU-C sec. 250 identifies two different kinds of laws and regulations and the auditor's responsibility when considering them. It requires the auditor to do the following: • Obtain sufficient appropriate evidence regarding material amounts and disclosures in the financial statements that are determined by the provisions of those laws and regulations generally recognized to have a direct effect on their determination • Perform specified audit procedures that may identify instances of noncompliance with other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, for which compliance may be fundamental to the operating aspects of the business and the entity's ability to continue as a going concern.[17]	Climate-related matters may affect the legal and regulatory environment that the entity operates in. An example would be a law or regulation that prohibits the manufacturing of vehicles whose emissions exceed a specified amount. A breach of such law or regulation may have a material effect on the financial statements (e.g., a breach may result in a contingent liability for potential litigation and fines or penalties).
AU-C sec. 450, *Evaluation of Misstatements Identified During the Audit* Addresses the auditor's responsibility to evaluate the effect of identified misstatements on the audit and the effect of uncorrected misstatements, if any, on the financial statements. AU-C sec. 450 indicates that circumstances related to some misstatements may cause the auditor to evaluate them as material, individually or when considered together with other misstatements, even if they are lower than materiality for the financial statements as a whole.	An example of a circumstance related to climate-related matters that may affect the evaluation of misstatements is the extent to which the misstatement is an omission of qualitative disclosures about environmental matters that present certain risks and uncertainties that could significantly affect the amounts reported in the financial statements as required under the financial reporting framework.

[17] Paragraph A11 of AU-C sec. 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*, states the following:

Noncompliance with other provisions of such laws and regulations, and the laws and regulations described in paragraph .06b, may result in fines, litigation, or other consequences for the entity, the costs of which may need to be provided for or disclosed in the financial statements but are not considered to have a direct effect on the financial statements, as described in paragraph .06a.

AU-C section	Examples of climate-related matters that may be relevant when applying the identified AU-C section
Audit evidence	
AU-C sec. 540A, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures* Addresses the auditor's responsibilities relating to accounting estimates, including fair value accounting estimates and related disclosures, in an audit of financial statements.[18]	The following are examples of estimates included in the financial statements that may be affected by climate-related matters: • The valuation of property, plant, and equipment after a climate-related event has occurred or when there is a high probability of a recurrence of such an event • Provisions for the cost of reforestation of abandoned strip mines • The valuation of intangible assets such as an entity's brand after the entity has been publicly identified as being responsible for plastic pollution contributing to carbon emissions • The net realizable value of inventory when the entity is affected by regulatory changes that could reduce the demand for a product and thereby make the inventory obsolete, or a significant weather event that causes physical damage to inventory AU-C sec. 540 requires the auditor to obtain an understanding of how management makes the accounting estimates and the data on which they are based.[19] This would include understanding • the entity's process for capturing information about climate-related matters and their possible effects on the financial statements • the nature and source of the information and the circumstances under which it is obtained.

[18] SAS No. 143, *Auditing Accounting Estimates and Related Disclosures* is codified in AU-C section 540 of the same title and will supersede AU-C section 540A once effective. SAS No. 143 is effective for audits of financial statements for periods ending on or after December 15, 2023.

[19] Paragraph .08c. of AU-C section 540A, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*. See paragraph .12h. ii. of AU-C section 540, *Auding Accounting Estimates and Related Disclosures*, for relevant requirements under SAS No. 143. SAS No. 143 is effective for audits of financial statements for periods ending on or after December 15, 2023.

AU-C section	Examples of climate-related matters that may be relevant when applying the identified AU-C section
Audit evidence	
	Examples of matters that the auditor may take into account in auditing accounting estimates include the following: • Whether management has assessed the continued use of previous methods, assumptions, and data used in making estimates, and if not, whether the methods, assumptions, and data used remain appropriate.[20] For example, insurance entities may need to increase their loss reserves, including incurred but not reported loss adjustment expense due to greater property damage from hurricanes with increased severity as a result of changes in weather patterns • The degree to which an accounting estimate is subject to estimation uncertainty, for example, climate-related matters may make it more difficult to make precise and reliable predictions about the incidence and effect of future events or conditions, for example, the frequency of extreme droughts affecting harvests. • The degree to which the accounting estimate is subject to complexity, which may require the use of specialized skill or knowledge to determine the effects of the changing climate-related event or condition.[22] AU-C sec. 540 also requires the auditor to obtain sufficient appropriate audit evidence about whether the disclosures in the financial statements related to accounting estimates are in accordance with the requirements of the applicable financial reporting framework and, for accounting estimates that give rise to significant risks, to evaluate the adequacy of the disclosure of estimation uncertainty in the financial statements in the context of that framework.[23] Many of the estimates affected by climate-related matters may have a high degree of estimation uncertainty.

[20] Paragraph .12b. of AU-C section 540A. See paragraph .A37 of AU-C section 540 for relevant requirements under SAS No. 143.

[21] Paragraph .10 of AU-C section 540A. See paragraph .15a. of AU-C section 540 for relevant requirements under SAS No. 143.

[22] Paragraph .14 of AU-C section 540A. See paragraphs .14 and .15b. of AU-C section 540 for relevant requirements under SAS No. 143.

[23] See paragraphs .19-.20 of AU-C section 540A, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures*. See paragraphs .31, and .35-.36 of AU-C section 540 for relevant requirements under SAS No. 143.

AU-C section	Examples of climate-related matters that may be relevant when applying the identified AU-C section
Audit evidence	
AU-C sec. 620A, *Using the Work of an Auditor's Specialist*[24] Addresses the auditor's responsibilities relating to the work of an individual or organization possessing expertise in a field other than accounting or auditing when that work is used to assist the auditor in obtaining sufficient appropriate audit evidence.	When auditing areas affected by climate-related matters, a specialist with expertise or specialized skill in a field other than accounting and auditing may be needed. The following are examples of how the work of a specialist may be used in an audit of an entity affected by climate related matters: • To test the reasonableness of management's calculation of the provision recognized for decommissioning offshore oil and gas operations or rehabilitating environmental damage, when required by law or regulation • To assist in understanding how management has considered future demand for refined petroleum product
AU-C sec. 570, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern* Addresses the auditor's responsibilities in the audit of financial statements relating to the entity's ability to continue as a going concern and the implications for the auditor's report. This section applies to all audits of a complete set of financial statements, regardless of whether the financial statements are prepared in accordance with a general-purpose or a special-purpose framework and includes guidance if events or conditions have been identified that may cast substantial doubt on the entity's ability to continue as a going concern. AU-C sec. 570 requires the auditor to conclude, based on the audit evidence obtained, whether substantial doubt exists about an entity's ability to continue as a going concern for a reasonable period of time and to evaluate the possible financial statement effects, including the adequacy of disclosure regarding the entity's ability to continue as a going concern for a reasonable period of time. If the auditor concludes that substantial doubt exists, the auditor is required to consider management's plans to alleviate that doubt and to evaluate disclosures regarding these matters	The following are examples of climate-related matters that could raise substantial doubt about an entity's ability to continue as a going concern, and factors that may or may not alleviate that doubt: • The disruption of business and the uncertainty created by operating in a geographic location that has a history of being highly susceptible to extreme weather events mitigated by evidence that the entity has leased a plant in, and will relocate to, an area that is less vulnerable to such events • Increased compliance costs related to enacted emissions regulations mitigated by a plan developed by a specialist that will enable the entity to comply with those regulations • Significant litigation claims by a city vulnerable to sea level rise and flooding against an energy company responsible for carbon emissions and the views of attorneys regarding the likelihood that the litigation will succeed.

[24] The amendments to AU-C section 620, *Using the Work of an Auditor's Specialist*, arising from SAS No. 144, Amendments to AU-C Sections 501, 540, and 620 Related to the *Use of Specialists and the Use of Pricing Information Obtained From External Information Sources*, have been codified in AU-C section 620 and will supersede AU-C section 620A of the same title once effective. SAS No. 143 is effective for audits of financial statements for periods ending on or after December 15, 2023.

AU-C section	Examples of climate-related matters that may be relevant when applying the identified AU-C section
Communication with Those Charged with Governance and Auditor Reporting	
AU-C sec. 260, *The Auditor's Communication With Those Charged With Governance* This section addresses the auditor's responsibility to communicate with those charged with governance in an audit of financial statements.	One of the matters that AU-C sec. 260 requires the auditor to communicate to those charged with governance is the auditor's views about qualitative aspects of the entity's significant accounting practices, including accounting policies, accounting estimates, and financial statement disclosures. An example of a matter that the auditor may communicate to those charged with governance is the effect of climate-related matters on significant assumptions used in accounting estimates, such as the impairment of nonfinancial and financial assets, and the degree of subjectivity involved in the development of the assumptions.
AU-C sec. 700, *Forming an Opinion and Reporting on Financial Statements* This section addresses the auditor's responsibility to form an opinion on the financial statements. It also addresses the form and content of the auditor's report issued as a result of an audit of financial statements. In determining whether the financial statements are prepared, in all material respects, in accordance with the requirements of the applicable financial reporting framework, AU-C sec. 700 requires the auditor to evaluate the matters in paragraph 15 of AU-C sec. 700. One of those matters is whether the financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements.	An example is disclosure about an entity's strategy to transition from manufacturing vehicles that use fossil fuels to electric vehicles, a strategy that would have pervasive effects on the entity and its financial statements. The following are additional disclosures that may be needed in this circumstance: • Risks related to the uncertainty of the demand for electric vehicles because of the market's perceptions about the quality, safety, performance (the range over which electric vehicles may be driven on a single battery charge), existing infrastructure (access to charging facilities), and cost of these vehicles • Risks related to competition from other types of alternative fuel vehicles, plug-in hybrid electric vehicles, and high fuel-economy internal combustion engine vehicles • The entity's dependence on the continued supply of lithium-ion battery cells for its vehicles and the limited number of such suppliers at the date of the financial statements

AU-C section	Examples of climate-related matters that may be relevant when applying the identified AU-C section
Communication with Those Charged with Governance and Auditor Reporting	
AU-C sec. 701, *Communicating Key Audit Matters (KAMs) in the Independent Auditor's Report* Addresses the auditor's responsibility to communicate key audit matters in the auditor's report when the auditor is engaged to do so. It is intended to address both the auditor's judgment about what to communicate in the auditor's report and the form and content of such communication. AU-C section 701 does not require the communication of key audit matters. The purpose of communicating key audit matters is to provide report users with greater transparency about the audit that was performed. The communication of key audit matters in the auditor's report may also provide intended users of the financial statements with a basis to further engage with management and those charged with governance about certain matters relating to the entity, the audited financial statements, or the audit that was performed. When communicating KAMs, the auditor is required to identify those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. KAMs are selected from matters communicated with those charged with governance.	Auditing account balances and disclosures impacted by climate-related matters may involve especially challenging, subjective, or complex auditor judgment. Such matters may be communicated to those charged with governance. If so, and the auditor is engaged to communicate KAMs, such matters would be among the matters considered by the auditor as a potential KAM.

AU-C section	Examples of climate-related matters that may be relevant when applying the identified AU-C section
Communication with Those Charged with Governance and Auditor Reporting	
AU-C sec.720, *The Auditor's Responsibilities Relating to Other Information Included in Annual Reports*[25] Addresses the auditor's responsibility relating to other information, whether financial or nonfinancial (other than financial statements and the auditor's report thereon), including in an entity's annual report. When the auditor has obtained all of the other information at the date of the auditor's report, the auditor is required to include a separate section in the auditor's report with the heading "Other Information," or other appropriate heading. AU-C section 720 establishes the requirement for the auditor to read the other information and consider whether a material inconsistency exists between the other information and the financial statements, and to remain alert for indications that a material misstatement of fact exists. AU-C section 720 also requires the auditor to remain alert for indications that a material inconsistency exists between the other information and the auditor's knowledge obtained in the audit or the other information is otherwise misleading. The credibility of the audited financial statements may be undermined by material inconsistencies between the other information and the audited financial statements or the auditor's knowledge obtained in the audit.	The following are examples of other information about climate-related matters that might be included in a document containing the audited financial statements and the auditor's report, which the auditor would be required to read and consider in accordance with AU-C sec. 720: • A discussion of the entity's short and long-term strategy for managing and responding to climate-related risks • Disclosure of climate-related performance measures, such as carbon emissions attributable to activities that the entity is responsible for • Potential future effects of climate change on the entity's operations. If the auditor identifies that a material inconsistency appears to exist (or becomes aware that the other information appears to be materially misstated), between the other information and the audited financial statements, AU-C sec. 720 states that the auditor should discuss the matter with management and, if necessary, perform other procedures to conclude the following: • Whether a material misstatement of the other information exists • Whether a material misstatement of the financial statements exists • Whether the auditor's understanding of the entity and its environment needs to be updated

[25] SAS No. 137, *The Auditor's Responsibilities Relating to Other Information Included in Annual Reports*, has been codified in AU-C section 720, and is effective for audits of financial statements for periods ending on or after December 15, 2021.

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