



OICV-IOSCO

Organización Internacional de Comisiones de Valores
International Organisation of Securities Commissions
Organisation internationale des commissions de valeurs
Organizaçào Internacional das Comissões de Valore

June 12, 2008

Mr. James M. Sylph
Executive Director, Professional Standards
International Auditing and Assurance Standards Board
International Federation of Accountants
545 Fifth Avenue, 14th Floor
New York, NY 10017

Email address: Edcomments@ifac.org

Re: Proposed Redrafted International Standard on Auditing 210 "Agreeing the Terms of Audit Engagements" and Related Conforming Amendments to Other ISAs

Dear Mr. Sylph:

The International Organization of Securities Commissions (IOSCO) Standing Committee No. 1 on Multinational Disclosure and Accounting (SC 1) appreciates the opportunity to comment on the Exposure Draft of proposed redrafted international standard on auditing ISA 210, *Agreeing the Terms of Audit Engagements* (ISA 210) and Related Conforming Amendments to Other ISAs. As an international organization of securities regulators representing the public interest, IOSCO is committed to enhancing the integrity of international markets through promotion of high quality accounting, auditing, and professional standards.

Members of SC 1 seek to further IOSCO's mission through thoughtful consideration of accounting, auditing and disclosure concerns, and pursuit of improved global financial reporting. As we review proposed auditing standards, our concerns focus on whether the standards are sufficient in scope and adequately cover all relevant aspects of the area of audit being addressed, whether the standards are clear and understandable, and whether the standards are written in such a way as to be enforceable.

Our comments in this letter reflect those matters on which we have achieved a consensus among the members of SC 1; however, they are not intended to include all comments that might be provided by individual members on behalf of their respective jurisdictions.

Scope (paragraph 1)

As written, paragraph 1 suggests that the ISA applies only to the initial agreement between the auditor and the entity and to the auditor's response to a request *by the entity* to change those terms. In practice, however, we understand that auditors often request changes to the terms of the audit engagement (e.g., because of changes in the planned scope of the engagement as a result of the

Calle Oquendo 12
28006 Madrid
ESPAÑA
Tel.: (34.91) 417.55.49 • Fax:
(34.91) 555.93.68
mail@oicv.iosco.org
• www.iosco.org

auditor's testing or new auditing or accounting standards that become effective after the initial agreement has been reached). We believe that the requirements and guidance in the ISA are sufficient to address auditor-requested changes, but suggest that paragraph 1 be modified as follows so that it is clearer that these changes are within the scope of the ISA (our suggested addition indicated in bold type and underlined):

1. This International Standard on Auditing (ISA) deals with the auditor's responsibilities in:

- (a) agreeing **or modifying** the terms of the audit engagement with the entity; and
- (b) responding to a request by an entity to change the terms of an audit engagement

for an audit of financial statements. It is to be adapted in the circumstances when applied to audits of other historical financial information.

Objective

In paragraph 3, we believe it would be clearer if the beginning of the first sentence were to read:

The objective of the auditor is to accept an audit engagement only when the basis upon which it is to be performed has been **specified and** agreed, through:

- (a) Establishing whether necessary preconditions for an audit are present; and
- (b) Confirming that there is a common understanding between the auditor and the entity, **including those charged with governance and shareholders as appropriate**, of the terms of the audit engagement and of the respective responsibilities of the auditor, management, and those charged with governance.

Preconditions for an Audit (paragraphs 4 and A1)

We note that this ISA introduces a new term "preconditions" for an audit, while other recently developed or proposed ISAs use a term "premises on which an audit is conducted". Use of a term such as "preconditions" for an audit would seem to imply that auditor-related preconditions should be included in the ISA in addition to the client-related preconditions now described in paragraph 4b.

If the term "preconditions" is retained, we believe that paragraph 4 should also reference the auditor's client acceptance and continuance responsibilities as outlined in the ISAs, as well as the auditor's need to consider both his or her competence and independence before agreeing to undertake an engagement. These auditor-related requirements must also be met for an audit engagement to be performed. Therefore, they do not merely "complement" the preconditions for an audit as now stated in paragraph A1, but are themselves preconditions as well.

As a further comment on paragraph 4, we think the use of words such as "all" and "any" in paragraph 4 (b) (ii) a. and b. result in statements regarding management responsibilities that are too broad to be included in an ISA. For example, as these paragraphs now read, the auditor is required to obtain the agreement of management for a statement that management is responsible to provide the auditor with:

(ii) a. All information, such as records and documentation, and other matters that are relevant to the preparation and presentation of the financial statements (*whether the auditor judges the information necessary or requests the information or not*) (*italics ours*)

Finally, we recommend that paragraph 4 be modified to clarify that obtaining agreement from management and, where appropriate, those charged with governance, as to their responsibilities does not in any way diminish the responsibilities of the auditor.

We provide a suggested revision below that we believe could help to clarify the responsibilities of management and the auditor. We also believe that conforming changes are necessary elsewhere where the preconditions for an audit are described, for example in paragraph A1, the example engagement letter in Appendix 1 and in Proposed ISA 200 (Revised and Redrafted).

To address these various matters, we suggest that paragraph 4 be reworded as follows with the footnote shown, or clarified in some comparable manner:

4. **In addition to the client acceptance and continuation requirements of the ISAs¹, and in order to establish whether the necessary preconditions for an audit are present, the auditor shall:**
- (a) Determine whether the financial reporting framework to be applied in the preparation and presentation of the financial statements is acceptable; and
 - (b) Obtain the agreement of management and, where applicable, those charged with governance that they acknowledge and understand their responsibility:
 - (i) For the preparation and presentation of the financial statements in accordance with the applicable financial reporting framework; this includes the design, implementation and maintenance of internal control relevant to the preparation and presentation of financial statements that are free from material misstatement, whether due to fraud or error; and
 - (ii) To ~~provide~~ **make available to the auditor with:**
 - (a) ~~All~~ Information, such as records and documentation, and other matters that the auditor judges is relevant to the preparation and presentation of the financial statements; and
 - (b) ~~Any~~ **Additional** information that the auditor may request from management, and where appropriate, those charged with governance; and
 - (c) ~~Unrestricted~~ **Unconditional** access to those within the entity from whom the auditor determines it necessary to obtain audit evidence.
 - (d) **This acknowledgment of management responsibilities does not in any way reduce the responsibilities of the auditor to plan and conduct the audit to obtain sufficient appropriate audit evidence to support the auditor's opinion.**

¹ **[Proposed] ISA 220 (Redrafted), "Quality Control for an Audit of Financial Statements", paragraphs 11-12 and ISA 300 (Redrafted), "Planning an Audit of Financial Statements", paragraph 5.**

Agreement of the Responsibilities of Management and, where appropriate, Those Charged with Governance (paragraphs 4(b), A12 and A13)

As now written, paragraphs A12 and A13, which describe actions that the auditor *may* take in seeking to reach agreement of the responsibilities of management and those charged with governance, introduce ambiguity as to whether the actions involved are requirements or merely helpful guidance. Paragraph A12 indicates that the auditor is required by ISA 580 to obtain written representations that management and those charged with governance have fulfilled their responsibilities (as described in paragraph 4(b) above) and that "it *may* therefore be appropriate to make them aware that receipt of

such written representations will be *expected...*" (emphasis added). Paragraph A13 describes the consequences of not obtaining these representations: "Where management and, where appropriate, those charged with governance will not agree...to provide the written representations, the auditor *will* be unable to obtain sufficient appropriate audit evidence" and consequently, unless prohibited by law or regulation from declining the engagement, "it *may* not be appropriate for the auditor to accept the engagement" (emphasis added).

Because the auditor is required to obtain appropriate representations pursuant to ISA580, it would seem that the use of "may" in these paragraphs is inappropriate. We request that the Board clarify what is required as opposed to what is suggested or being illustrated. We also request that the last sentence specify clearly the intended implications for the auditor's report and/or cross reference the appropriate text in the ISAs on management representations and auditor reporting.

Agreement on Audit Engagement Terms (paragraphs 8, 16 and A22)

In addition to the required terms of the audit engagement outlined in paragraph 8 (i.e., the objective and scope of the audit, the responsibilities of the auditor and management, the identification of the financial reporting framework and the expected form of any reports to be issued by the auditor), we believe that the terms should include the basis on which the auditor's fees are computed. In our view, the basis on which audit fees are computed is fundamental to "confirming that there is a common understanding between the auditor and the entity of the terms of the audit engagement", as described in the objective of the ED. We therefore recommend moving "the basis on which fees are computed" from paragraph A22 to paragraph 8.

Paragraph 16 describes the auditor's responsibilities "if the auditor is unable to agree to a change of the terms of the audit engagement and is not permitted to continue the original audit engagement." It is unclear to us who, in these circumstances, are not permitting the auditor to continue the original audit engagement. We request that the Board clarify its intent. Also, in paragraph 16(b), we recommend adding "regulatory bodies" to the list of parties that the auditor might need to notify about the auditor's withdrawal from the audit engagement.

Financial Reporting Framework Prescribed by Law or Regulation – Determined as Unacceptable (paragraphs 19 and 20)

We believe the content of paragraph 20 would more appropriately be presented as a subparagraph (c) in paragraph 19. Otherwise, paragraphs 19 and 20 are logically in conflict.

Objective (paragraph A2)

We recommend changing the reference from "legislation" to "laws and regulations" so as to accommodate jurisdictional differences in how the terms of audit engagements might be established. For completeness of coverage, we also suggest adding the following sentence: "In some instances, relevant laws and regulations may also prescribe responsibilities for shareholders."

Form and Content of the Audit Engagement Letter (paragraph A22)

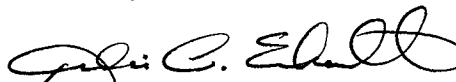
Paragraph A22 indicates that an audit engagement letter may make reference to: "The fact that because of the test nature and other inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that even some material misstatement may remain unresolved." We have previously expressed our concern with terms such as "unavoidable risk", which we believe are excessively negative and inappropriately convey the auditor's responsibilities. We request that paragraph A22 be reworded to more appropriately convey the inherent limitations of an audit, for example by using the language in paragraph A39 of Proposed ISA 200 (Revised and Redrafted), which states:

The auditor is not expected to, and cannot, reduce audit risk to zero and cannot therefore obtain absolute assurance that the financial statements are free from material misstatement due to fraud or error. This is because there are inherent limitations of an audit, which result in the audit evidence on which the auditor bases the auditor's opinion often being persuasive rather than conclusive.

In addition to the general comments we have made above, Appendix A contains our responses to the questions in the Explanatory Memorandum accompanying the ED.

Thank you for the opportunity to comment on this ED. If you have any questions or need additional information regarding this comment letter, you may contact me or Susan Koski-Grafer at 202-551-5300, or any member of the IOSCO Standing Committee No. 1 Auditing Subcommittee.

Sincerely,



Julie A. Erhardt
Chair

IOSCO Standing Committee No. 1

Appendix A: Responses to Request for Comments

Responses to Request for Specific Comments

1. Do you agree with the proposed description of management’s responsibilities in the ISAs?

Please see our comments in the main body of our letter on how the description of both management and auditor responsibilities could be improved.

2. Do you agree that the description of management’s responsibilities in the terms of the audit engagement, written representations and auditor’s report may use the wording of the law or regulation if the auditor has determined that the law or regulation includes responsibilities that are equivalent in effect to those described in the ISAs?

While we agree in principle that the auditor should be able to use the wording of the law or regulation in such circumstances, we are concerned that the ISA does not provide adequate guidance to auditors to determine whether the descriptions are “equivalent”. Determining “equivalence” is not a simple matter. We note that paragraph A20 indicates that the accounting profession or national standard setter in a jurisdiction may provide guidance in this area, but believe some reference is needed as to how the auditor should make a determination in the absence of such institutional guidance. If what is intended is for the auditor to use professional judgment, we believe this should be stated.

3. Do you agree with the proposed conforming amendment to proposed ISA 700 (Redrafted)?

The amendment to paragraph 23(a) of ISA 700 indicates that the auditor’s report shall describe management’s responsibility for the financial statements in the manner that they are described in the terms of the audit engagement¹. To avoid confusion as to the responsibilities that are required to be described in the auditor’s report, we recommend modifying paragraph 23(a) to cite the specific paragraphs in ISA 210 in which those responsibilities are enumerated. Otherwise, one might interpret paragraph 23(a) to require the auditor’s report to describe the responsibilities outlined in paragraph 4(b)(ii) of ISA 210². As noted earlier in this letter, we have also commented on the need to revise this description of responsibilities.

4. Are there any residual concerns about the way in which management’s responsibilities are dealt with that may cause difficulty in any particular jurisdiction?

Please see our comments in the main body of this letter.

Responses to Request for Comments on the Application of the Clarity Drafting Conventions

1. Are the objectives to be achieved by the auditor, stated in the proposed redrafted ISA, appropriate?

¹ Paragraph 23(a) states of ISA 700, “The auditor’s report shall describe management’s responsibility for the financial statements in the manner that responsibility is described in the terms of the audit engagement.”

² Paragraph 4(b)(ii) of ISA 210 now states, “...the auditor shall...(b) Obtain the agreement of management and, where appropriate, those charged with governance that they acknowledge and understand their responsibility...(ii) To provide the auditor with: a. All information, such as records and documentation, and other matters that are relevant to the preparation and presentation of the financial statements; b. Any additional information that the auditor may request from management and, where appropriate, those charged with governance; and c. Unrestricted access to those within the entity from whom the auditor determines it necessary to obtain audit evidence.”

We believe the objectives are largely appropriate. Please see our comments in the main body of this letter for additional comment regarding the objectives.

2. **Have the criteria identified by the IAASB for determining whether a requirement should be specified been applied appropriately and consistently, such that the resulting requirements promote consistency in performance and reporting, and the use of professional judgment by auditors?**

Except as described in the main body of our letter, we believe that the criteria for determining whether a requirement should be specified have been applied appropriately and consistently.