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Organización Internacional de Comisiones de Valores
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February 29, 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 705 “*Modifications to the Opinion in the Independent Auditor’s Report*” and Proposed Redrafted International Standard on Auditing 706 “*Emphasis of Matter Paragraphs and Other Matter(s) Paragraphs in the Independent Auditor’s Report*”

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 Drafts of proposed redrafted international standard on auditing ISA 705, *Modifications to the Opinion in the Independent Auditor’s Report* (ISA 705) and proposed redrafted international standard on auditing ISA 706, *Emphasis of Matter Paragraphs and Other Matter(s) Paragraphs in the Independent Auditor’s Report* (ISA 706). 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.

In general, we welcome a number of the changes that have been made in clarifying and redrafting ISA 705 and 706. We are particularly pleased with the changes that the International Auditing and

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Assurance Standards Board (IAASB) made to these standards that address the concerns that we expressed in our comment letter on the March 2005 Exposure Drafts (ED). Specifically, we note that the IAASB:

- Eliminated the use of the caveat “ordinarily” in describing the circumstances when a modification to the auditor’s reports is appropriate;
- Added a statement that multiple uncertainties leading to a disclaimer of opinion are not necessarily related to the inability of the auditor to obtain sufficient appropriate audit evidence;
- Clarified that a modification to the auditor’s report is appropriate when there is a material misstatement of the financial statements related to specific amounts or disclosures, even when it is impracticable to quantify the effects of the misstatement;
- Included a reference to the financial reporting framework in the “Basis for Qualified Opinion” section of the illustrative qualified opinion in Illustration 1 of the Appendix; and
- Clarified that an Emphasis of Matter paragraph is only permitted when the auditor has obtained sufficient appropriate audit evidence that the matter is not materially misstated in the financial statements.

In the following sections we outline certain matters that we believe should be considered before finalizing the proposed standards. Within our recommendations for editorial changes, additions are noted in “bold underline” and deletions in “bold strike-through.” The appendix to this letter outlines our responses to the IAASB’s request for specific comments.

ISA 705

Disclaimer “opinion” vs. “report”

The ISA establishes three types of modified opinions, namely a qualified opinion, an adverse opinion and a disclaimer of opinion. However, we do not believe that a disclaimer of opinion is a type of *opinion* because in this type of report the auditor has not expressed an opinion but has rather disclaimed the ability to form an opinion. We therefore believe the standard would be clearer and translation into other languages would be facilitated if the ISA consistently referred to modifications to the auditor’s *report* rather than modifications to the auditor’s *opinion*.

We also believe that this ISA needs to clarify further and emphasize that multiple uncertainties in and of themselves do not make it necessary to issue a disclaimer.

Definition of “pervasive”

ED-ISA 705 proposed guidance to assist the auditor in determining the pervasiveness of a matter giving rise to an adverse opinion or a disclaimer of opinion, which has been subsequently revised and incorporated into a definition in ISA 705 based on comments that the IAASB received on the ED. While we agree that an explanation of what is meant by “pervasive” will result in greater clarity, we believe that the current definition is confusing because it incorporates two distinct concepts – diffuseness and significance, and two distinct issues – misstatements and the inability to obtain sufficient appropriate audit evidence. We believe that the definition would be clearer if these distinct concepts and issues were described in a manner more consistent with paragraphs 9-11 of the close-off document¹.

Other matters requiring a modification to the auditor’s report when the auditor disclaims an opinion

We believe that the content in paragraph 23 in the close off document of ISA 705 should be retained in the requirements of the ISA rather than presented in the Application Material section. This paragraph, which reads, in part, "An inability to perform a specific procedure does not constitute a scope limitation if the auditor is able to obtain sufficient appropriate audit evidence by performing alternative procedures..." is essential to understanding the requirements of ISA 705.

Piecemeal Opinion

The Exposure Draft's discussion of the term "Piecemeal Opinion" in paragraph 17 and related paragraphs in the application material section is unclear and difficult to follow. It is unclear if the term had the same meaning as "split opinion", or if "split opinion" would only refer to cases where a modified opinion, not an adverse opinion or disclaimer, is expressed on the financial statements as a whole. Furthermore, the term "Piecemeal" is an English term that is difficult to translate into other languages. Using this term does not contribute to clarity, especially in the context of an auditor's opinion. We suggest that the board come up with a more generic term that is easy to translate and also provide a clear explanation of the intended usage and limits involved.

ISA 706

Clarification of circumstances requiring an Emphasis of Matter

Paragraphs 1(a) and 7 each indicate that an Emphasis of Matter paragraph is used to draw users' attention to a matter presented or disclosed in the financial statements that the auditor *judges* important to their understanding of the financial statements. However, as noted in paragraph A1, in certain circumstances described in Proposed ISA 560 (Redrafted), *Subsequent Events*, and [Proposed] ISA 570 (Redrafted), *Going Concern*, the auditor is *required* to include an Emphasis of Matter paragraph (i.e., inclusion of such a paragraph is not a matter of auditor judgment). Consequently, we recommend that these paragraphs be revised as follows:

1.(a)...An Emphasis of Matter paragraph to draw user's attention to a matter presented or disclosed in the financial statements that the auditor **is required to include by other International Standards on Auditing or that the auditor** judges important to a user's understanding of the financial statements.

7. When **required by other International Standards on Auditing, or when** the auditor considers it appropriate to draw users' attention to a matter presented or disclosed in the financial statements that, in the auditor's judgment, is of such importance that it is fundamental to the users' understanding of the financial statements, the auditor shall include an Emphasis of Matter paragraph in the auditor's report.

We also would like to see one or more examples of the specific type of condition described in paragraph 1 (a) of the ED. Showing examples of cases where such emphasis of matter is *required* is not really helpful in clarifying and illustrating when such emphasis of matter would be helpful although discretionary, and not specifically required.

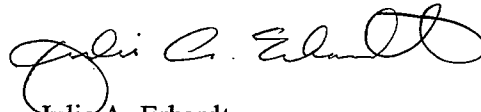
Other Matters Paragraphs

In regard to the discussion of "Other Matters" in paragraphs 4, 9 and A6 to A8, we believe that the intended use of such paragraphs needs to be clarified. As now written, these paragraphs raise the issue

but do not really make clear what type of usage would be appropriate. We recommend the standard should distinguish clearly the situations where the auditor is required by law or regulation to include an "Other Matters" paragraph from those situations in which an auditor, based on his/her professional judgment, decides to make use of an "Other Matters" paragraph to draw users' attention. There is also no indication of whether use of an "Other Matters" paragraph is expected to occur only in rare circumstances, or not. We also note that a statement should be added regarding the auditor's need to have sufficient and appropriate audit evidence to support an Other Matters paragraph if one is used, similar to what is said in the ISA regarding an Emphasis of Matter paragraph.

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: Responses to Request for Specific Comments

ISA 705

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

We believe that the objectives as stated in the proposed redrafted ISA are appropriate.

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?

We believe that the criteria identified by the IAASB for determining whether a requirement should be specified have been applied appropriately and consistently.

ISA 706

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

We believe that the objectives as stated in the proposed redrafted ISA are appropriate.

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?

We believe that the criteria identified by the IAASB for determining whether a requirement should be specified have been applied appropriately and consistently except that we believe that clarification is needed regarding what is intended in paragraph 9 regarding "other matters". We also believe the ISA should communicate in paragraph 9 or paragraphs A 6 to A 8, whether the use of an other matters paragraph is intended to take place only in rare circumstances or not, and provide the appropriate rationale.

ⁱ Excerpts from the close-off document for ISA 705:

9. The auditor may judge misstatements that are material individually or in the aggregate to be pervasive to the financial statements when such misstatements are not confined to specific elements, accounts or items in the financial statements or, if confined, the misstatements represent or could represent a substantial proportion of the financial statements.
10. Further, in relation to disclosures, the auditor may judge misstatements that are material individually or in the aggregate to be pervasive to the financial statements when the misstated disclosures are fundamental to users' understanding of the financial statements.
11. The auditor may judge an inability to obtain sufficient appropriate audit evidence about one or more matters pertaining to the financial statements to be both material and pervasive when the possible effects of the inability cannot be confined to specific elements, accounts or items in the financial statements or, if confined, those possible effects could represent a substantial proportion of the financial statements.