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20 May 2013

Technical Director
International Auditing and Assurance Standards Board
529 Fifth Avenue, 6th Floor
New York, New York 10017 USA

Our Ref: 2013/JE/C1/IAASB/76

Subject: Proposed Revised International Standard on Auditing 720, *The Auditor's Responsibilities Relating to Other Information in Documents Containing or Accompanying Audited Financial Statements and the Auditor's Report Thereon*

Dear Sir:

The International Organization of Securities Commissions' Committee on Issuer Accounting, Audit and Disclosure (Committee 1) appreciates the opportunity to comment on the IAASB's Exposure Draft, *International Standard on Auditing 720 (Revised), The Auditor's Responsibilities Relating to Other Information in Documents Containing or Accompanying Audited Financial Statements and the Auditor's Report Thereon* (the ED). 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, other pronouncements and statements.

Members of Committee 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



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among the members of Committee 1; however, they are not intended to include all comments that might be provided by individual members on behalf of their respective jurisdictions.

Overall Comments

In general, we appreciate the Board's focus on improving audit quality by bringing greater consistency around the world regarding auditors' consideration of the diversity of information that accompanies audited financial statements. However, we believe that further consideration is needed to provide for a more robust standard that is practical for auditors and enforceable by regulators. Particularly, we would like to point out the following matters:

- The introduction of the concept of "initial release" into the scope has raised some concerns to us in terms of its implications and how it could be consistently applied.
- We have mixed views regarding whether securities offering documents should be within the scope. Some members believe securities offering documents should be a matter governed by securities law. Other members believe securities offering documents include the same risks of material inconsistency in other information that are being addressed by the proposal and as such should be within the scope.
- There is a need for clearer guidance in relation to "other information" that is not available at the date of the auditor's report.
- The auditor's required work effort to "...read and consider the other information..." may be prone to a variety of interpretations particularly with respect to other information beyond the directly reconcilable financial information.
- The definition and guidance proposed around the term "inconsistency" has raised some concerns particularly as users may have a different expectation than what is being proposed.

Scope

Under the existing ISA 720, all documents containing audited financial statements that are part of the company's annual reporting to owners or similar stakeholders are within the scope of the ISA. The existing ISA 720 also may be applied, adapted as necessary, to other documents such as those used in securities offerings. We note, however, that the ED introduces "...documents that are expected to be issued in connection with the *initial release*..." within the requirements section as a precursor to



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determining which documents would be within the scope of the proposed ISA. Further, the ED proposes to largely remove the possibility of its use with respect to the other information contained in securities offering documents, by removing them from its scope unless the securities offering is the reason for the company's initial release of its annual results. Among the Committee 1 members we have concerns about the implications of the revision of the scope, as described below. We recommend reconsidering the scope, especially the introduction of the terminology "initial release," in order to achieve the consistent application of the standard.

"Initial Release"

We believe that further clarification should be made in paragraph A5 as there are jurisdictions in which multiple financial reports prepared under different requirements – thereby producing different auditors' reports – are issued for the same period. It is not clear that the initial release concept covers all of those multiple documents, accordingly, the IAASB needs to clarify that the final standards actually cover all of those documents. For example, some companies voluntarily issue "glossy" annual reports containing audited financial statements and an auditor's report, subsequent to the official filing of "regulatory" annual reports to the regulator. The timing of the preparation for the "glossy" annual report and "regulatory" annual report are different; accordingly, it is not clear whether the "glossy" issued as of the same period but prepared under different requirements than the regulatory report can also qualify as "initial release". Regardless, as audited financial statements are bound in the reports, users would reasonably expect that auditors read and consider the other information in both reports. In addition, the "glossy" annual report and "regulatory" annual report contain different other information.

In addition, if the IAASB intends to introduce the initial release concept, it needs to clarify if the introduction of the initial release concept, in connection with the additional criteria stated in paragraph A5, would solve the concern for the open-ended obligation to auditors, as intended. Our members doubt if the initial release concept is sufficiently clear to avoid placing an open-ended obligation on auditors as there is no limit on which documents issued after, and in connection with, the initial release are to be included in the scope.

Securities Offering Documents

We noted that securities offering documents are excluded from the scope of the ED, in the manner summarized above.



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Some Committee 1 members believe that it is appropriate to scope out the securities offering documents from ISA 720, as the auditor's responsibility for such documents should be governed solely by securities law and therefore should not be left to the ISAs. Accordingly, these members suggest that the final standard eliminate the proposed provision which requires auditors to apply ISA 720 to prospectuses that meet the initial release timing requirements. The standard could, instead, note that auditors should look to applicable laws and regulations for all securities offering documents.

Our other Committee 1 members consider that the other information in all documents relating to public offerings of securities that include audited financial reports should come within the scope of ISA 720. The risks of material inconsistencies in other information and to the fair presentation of the financial statements that the proposed ISA is intended to address are risks that are resident in all public offering documents, not just those that are prepared as part of the initial release of annual results. Thus, from the perspective of investors in the public offering, these members cannot see why the auditor would be required to review the public offering document in some cases ("initial release") but not in others.

Turning to the practical implications of auditor involvement with securities offering documents, our members who support inclusion within the scope believe that, in many jurisdictions, auditors will need to confirm the inclusion of their audit reports in the offering document before they are published, accordingly, the auditors would be aware of the publication of the offering document. If this is the case, it seems operational to require the auditors to read and consider the information in the offering documents, before the offering documents are published. On the other hand, where the audited financial statements are included with no involvement of the auditors, the members would agree that it is not practical to expect the auditors to be responsible for the other information because there is no "trigger" for the company to engage them such that they could fulfill this responsibility. These members acknowledge that in some jurisdictions the obligations of auditors to review public offering documents are set out in other regulations. However, they do not consider that it can be assumed that such regulations are sufficiently pervasive internationally. These members do not consider clarifying that ISA 720 applies in connection with public offering documents would preclude compliance with any jurisdiction's requirements, especially if the ISA noted that in the case of conflicting provisions the applicable laws would apply.

"Other Information" Not Available at the Date of the Auditor's Report

In some jurisdictions, other information such as an MD&A is not available at the date of the auditor's report on the financial statements ("subsequently available document"), and thus is filed subsequent to the filing of the audited financial statements, in accordance with local regulations. These



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subsequently available documents are within the scope of the ED and we agree that the expected work effort for “other information” should be the same regardless of whether the other information is or is not available at the date of the auditor’s report. However, we believe the proposed auditors’ responses on these subsequently available documents is not clear and the lack of clarity causes at least the following two issues.

First, financial statement users are not able to determine if the subsequently available document (e.g., MD&A) is reviewed by an auditor or not. Although paragraph A59 recognizes that if other information was not available at the date of the auditor’s report then this does not obviate the need for the auditor to read and consider the subsequently available document, the ED does not, however, require any communication to users regarding whether or not the subsequently available document was read and considered by the auditor. Thus, although the same work is performed by the auditors, the transparency of the auditor’s work is different. We are concerned that the lack of transparency could confuse users. Although we recognize that there would not be a simple solution, the IAASB should further consider how to achieve the greater transparency of the auditor’s involvement on subsequently available documents. For example, would auditors be required to update the auditor’s report or communicate to users outside of the auditor’s report when the auditor completes reading and considering the subsequently available documents? We suggest that the IAASB seek investors’ input regarding how investors should be notified of the auditors’ responses on the subsequently available documents.

Secondly, it is not clear to us how auditors should respond to a material inconsistency (misstatement) in a subsequently available document. In jurisdictions where audited financial statements are issued first and other information such as MD&A are issued subsequently, the subsequently issued other information could contain a material inconsistency (misstatement), although the audited financial statements did not have any issue. A professional accountant shall not knowingly be associated with subsequently issued other information where the professional accountant believes that the information contains a materially false or misleading statement under paragraph 110.2 of the Code of Ethics. Although paragraph 14(b) of the ED may address the situation, it simply refers to ISA 560 paragraphs 10-16, which, we believe, deal with a material inconsistency (misstatement) in the financial statements, instead of in the subsequently available document. The current ISA 720 is relatively clearer on the point, although we question whether paragraph 13 of the existing ISA 720 is clear enough regarding how auditors should respond to the material inconsistency in the subsequently available document in relation to the needs of financial statement users.



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The Nature and Extent of the Auditor's Work Effort

The Objective as well as paragraph 11 of the ISA set out that the auditor is required to "...read and consider the other information...". We are concerned that this can lead to a variety of interpretations between auditors and jurisdictions, and that it therefore does not sufficiently guide the work effort required from the auditor. Further, we wonder whether reading and considering the other information in light of the understanding of the entity sufficiently meets with the expectations that financial statements users have of the role of the auditor. Based on our understanding, the expectation would be that auditors do some form of verification and reconciliation of the other information with the audited financial statements and other information gathered during the audit.

Paragraph A37 classifies the nature of the other information and states work efforts respectively. We believe that work efforts for the information categorized under A37 (a), (b) and (c) are prescriptive and clear; however, work efforts for the information categorized under A37 (d) is subjective, and thus ambiguous to us. We are concerned that the lack of clarity regarding paragraph A37 (d) will not only bring about divergence in practice but also negatively affect the enforceability of the standard.

The Definition of an "Inconsistency" in the Other Information

The existing ISA 720 defines an inconsistency as "*other information that contradicts information contained in the audited financial statements.*" On the other hand, paragraph 9 of the proposed ISA 720 expands the definition of an inconsistency to "*(i) Contains information that is incorrect, unreasonable or inappropriate; or (ii) Is presented in a way that omits or obscures information that is necessary to properly understand the matter being addressed in the other information.*" While we are supportive of the idea of asking the auditor to consider matters broadly, as there are no criteria to evaluate what would be "unreasonable or inappropriate", the new definition could be subjectively applied. Accordingly, we are concerned that the change in the definition could lead to divergence in practice, create difficulty for auditors to challenge management and cause enforceability issues.

The Auditor's Report Regarding Inconsistencies

We noted that an example of the statement that would be included in the auditor's report is stated under paragraph A57. We are concerned with the following sentence of the paragraph "*We have not identified material inconsistencies in the Other Information.*" As described in paragraph 9 (a), the term "inconsistency" has a particular meaning, which is different from an ordinary user's expectation. If the term "inconsistency" means "*(i) Contains information that is incorrect, unreasonable or inappropriate; or (ii) Is presented in a way that omits or obscures information that is necessary to*



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properly understand the matter being addressed in the other information,” the statement in the auditor’s report should present that, otherwise, it would widen the expectation gap, instead of narrowing it.

In addition, in case of material inconsistencies identified, the statement, on paragraph A58, should include a clear statement whether the identified material inconsistency has any effect on the true and fair view of the audited financial statements or not.

We noted that the example under paragraph A57 does not address any responsibility of management for the other information. Management would be responsible for the preparation and fair presentation of the other information under the scope of the proposed ISA and this should be stated in the auditor’s report.

Thank you for the opportunity to provide input on this project. If you have any questions or would like to further discuss the matters noted in this letter, please contact either Nigel James or me at 202-551-5300.

Sincerely,

Julie A. Erhardt
Chair
Committee on Issuer Accounting, Audit and Disclosure
International Organization of Securities Commissions