



15 September 2011

Ref: 11/136

Prof. Arnold Schilder
Chair
International Auditing and Assurance Standards Board
International Federation of Accountants
545 Fifth Avenue
14th Floor
New York
New York 10017 USA

Dear Prof. Schilder,

The International Association of Insurance Supervisors (IAIS) welcomes the opportunity to comment on the International Auditing and Assurance Standards Board's (IAASB) Consultation Paper, *Enhancing the Value of Auditor Reporting: Exploring Options for Change* ('the paper').

As insurance supervisors, members of the IAIS may have the ability to request individual reports from auditors of regulated entities or additional assurance work on specific areas, for example, on solvency returns. Therefore, this letter expresses IAIS views on how changes to auditor reports addressed to the public may enhance audit quality through enhanced disclosures about the audit itself.

The IAIS believes that issues related to the information gap pertaining to the entity cannot be solved by the auditor. It is the responsibility of management, and not that of the auditor, to provide users with information about the entity. As the International Accounting Standards Board sets the standards for financial statements disclosure, and the IAASB for the auditor's report, we ask whether the two bodies should work together to promote better disclosure.

Where the auditor provides additional information about the audit, it should be made clear that this information is provided to reduce the expectation and information gaps relative to the conduct of the audit and to explain how the auditor arrives at his audit opinion. It is essential that this additional information about the context and the conduct of the audit is not seen by the auditor, management and users as an easy way of expressing an implicit qualified opinion.

The appendix provides the IAIS' responses to the questions set out in the paper.

If you have questions regarding this letter, please contact Aina Liepins at the IAIS Secretariat (tel: +41 61 280 8199; email: aina.liepins@bis.org) or Richard Thorpe, Chair of the IAIS Accounting and Auditing Issues Subcommittee (tel: +44 (0) 20 7066 3160; email: richard.thorpe@fsa.gov.uk).

Yours faithfully

Handwritten signatures in blue ink. The first signature is 'P. Braumüller' and the second is 'M. Mächler'.

Peter Braumüller
Chairman, Executive Committee

Monica Mächler
Chair, Technical Committee

Appendix: responses to questions raised in the paper

Issues Identified

1. Do respondents have any comments about the issues identified in Section II regarding the perceptions of auditor reporting today?

We agree with the presentation of the various issues raised by the main users of the audit report.

We believe that some issues related to the information gap cannot be solved by auditors providing additional information. It is the responsibility of management, and not that of the auditor, to provide users with information about the entity. The importance of the division of responsibility between management and the auditor should not be undermined.

2. If respondents believe changes in auditor reporting are needed, what are the most critical issues to be addressed to narrow the information gap perceived by users or to improve the communicative value of auditor reporting? Which classes of users are, in the view of respondents, most affected by these issues? Are there any classes of users that respondents believe are unaffected by these issues?

We believe that the audit report could be changed to narrow the information gap perceived by users. It would be helpful to explore options that provide more information about how the audit is undertaken, in particular in relation to areas of significant risks.

In addition to investors, lenders and analysts, policyholders are important users of audited financial statements for the insurance industry and may be particularly affected by expectation and/or information gaps. As supervisors, IAIS members pay particular attention to the auditor's report and place reliance on the work carried out by the auditors in forming an audit opinion.

3. Do respondents believe that changes are needed for audits of all types of entities, or only for audits of listed entities?

We believe that any changes forthcoming should be adaptable to all audits.

Exploring Options for Change

A. Format and Structure of the Standard Auditor's Report

4. Respondents are asked for their reactions to the options for change regarding the format and structure of the standard auditor's report described in Part A. Do respondents have comments about how the options might be reflected in the standard auditor's report in the way outlined in Appendix 1 of this Consultation Paper?

As the auditor's opinion is the key output from the audit, it should be the focus of the report. It is helpful to have context for the audit process, and as such, the report should retain descriptions of the respective responsibilities of management and the auditors.

We agree that it would be useful to explore the possibility of explaining some technical concepts (e.g., materiality, level of assurance...) in an appendix to the report.

5. If the paragraphs in the current standard auditor's report dealing with management and the auditor's responsibilities were removed or re-positioned, might that have the unintended consequence of widening the expectations gap? Do respondents have a view regarding whether the content of these paragraphs should be expanded?

We believe that the descriptions of the responsibilities of management and the auditor should remain in the audit report so that the opinion can be read with the appropriate context.

These paragraphs could be expanded to describe more fully the auditor's responsibilities with respect to fraud, going concern and other disclosures within the annual report. A statement could be added to reinforce the fact that the auditor's responsibility does not include developing and providing financial information about the entity.

B. Other Information in Documents Containing Audited Financial Statements

6. Respondents are asked for their reactions to the possibility that the standard auditor's report could include a statement about the auditor's responsibilities regarding other information in documents containing audited financial statements. Do respondents believe that such a change would be of benefit to users?

We fully agree that the standard auditor's report should include:

- a statement about the auditor's responsibilities relating to other information in documents containing audited financial statements. For example, the auditor's responsibilities with regard to the MD&A should be clearly set out.
- a conclusion regarding such other information.

7. If yes, what form should that statement take? Is it sufficient for the auditor to describe the auditor's responsibilities for other information in documents containing audited financial statements? Should there be an explicit statement as to whether the auditor has anything to report with respect to the other information?

We believe that the auditor should describe his responsibilities related to other information in documents containing audited financial statements and should make an explicit statement as to whether the auditor has anything to report. Much information is often included in the other information contained in the document including audited financial statements e.g. further financial analysis or prudential information. This other information may be analysed by users as part of their decision making and therefore it is important that users are clear about the role of the auditor in respect of this information.

C. Auditor Commentary on Matters Significant to Users' Understanding of the Audited Financial Statements, or of the Audit

8. Respondents are asked for their views regarding the auditor providing additional information about the audit in the auditor's report on the financial statements.

We believe that there is benefit in exploring whether further information can be provided about the audit. However, the auditor must be careful not to provide information about the entity that the entity has not disclosed itself. For example, it would not be appropriate for the auditor to disclose where measurement uncertainty exists within the financial statements, or key assumptions and judgments used for valuations, where management has not already disclosed these. In other words, auditor reporting should not be a substitute for adequate

disclosure in the financial statements. However, the auditor should be encouraged to discuss the disclosures he intends to make in the auditor's report with the entity's management and audit committee and, in particular, how these disclosures are linked to disclosures made in the audited financial statements. This may create the right level of tension between the auditor and management, potentially leading to improved disclosure where the auditor feels there are shortcomings. In the absence of appropriate disclosure, the auditor should qualify his opinion. In these circumstances, it may be appropriate for the auditor to provide the required information in the audit report.

The auditor is required to use judgment, especially when gathering evidence is difficult. In this context, we believe that it would be useful to explore options for changing the audit reporting model in order to have the auditor provide more information about:

- what was done
- nature of evidence was obtained and how judgement was exercised in assessing management choices regarding critical accounting estimates or policies
- approach to areas of measurement uncertainty and key assumptions

Moreover, it should be made clear that the additional information is provided to reduce the expectation and information gaps relative to the conduct of the audit and to explain how the auditor arrives at his audit opinion. It is essential that any additional information about the context and the conduct of the audit is not seen by the auditor, management and users as an easy way of expressing an implicit qualified opinion.

9. Respondents are asked for their reactions to the example of use of "justification of assessments" in France, as a way to provide additional auditor commentary.

The French Commercial Code requires the auditors to provide a "justification of assessment" in their report on the annual accounts. This includes their assessment of a company's choices, use of accounting methods, material or sensitive accounting estimates, and also, if necessary, elements of internal control.

We believe that it would be useful to further explore the "justification of assessment" as a means of providing more information about the audit process in key areas. However, we must point out that any trend to resort to boilerplate or standardised explanations would fail to provide valuable additional information about the audit.

10. Respondents are asked for their reactions to the prospect of the auditor providing insights about the entity or the quality of its financial reporting in the auditor's report.

As expressed above, clarity is needed about the respective roles and responsibilities of management, those charged with governance and the auditors. We believe that the responsibility to disclose information about the entity to users of the audited financial statement must remain with management and with those charged with governance.

D. An Enhanced Corporate Governance Model: Role of Those Charged with Governance regarding Financial Reporting and the External Audit

11. Respondents are asked for their reactions to the options for change relating to an enhanced model of corporate governance reporting, as described in Section III, Part D.

We agree that there is merit in enhancing corporate governance reporting. We believe that the proposals of the Financial Reporting Council in the UK have some merits and should be explored. In particular, the concept of an enhanced audit committee report, setting out, inter

alia, key matters discussed with auditors and their resolution could be a useful mechanism to provide additional information about the audit. However, this would need to be carefully considered alongside any proposal for enhanced reporting by auditors.

12. To the extent that respondents support this model, what challenges may be faced in promoting its acceptance? Also, what actions may be necessary to influence acceptance or adoption of this model, for example, by those responsible for regulating the financial reporting process?

The implementation of this model would require modifications to national laws and to requirements set by authorities regulating the financial reporting process across different jurisdictions. To promote harmonisation and adoption of an audit committee report across different jurisdictions and by the relevant international associations will be challenging and time consuming. We believe that the IAASB should promote consistency in auditor reporting across all jurisdictions. If this initiative would not be acceptable in all jurisdictions, then the proposal should be pursued separately and not as part of the standard auditor opinion.

13. Do respondents believe assurance by the auditor on a report issued by those charged with governance would be appropriate?

We believe that there is merit in having the auditor provide assurance on the reasonableness and completeness of the audit committee report. However, in order to avoid confusion, this assurance should not be included in the report on the financial statements. Also, since the auditor's report on the financial statements and the audit committee report are related, there is a need for the auditor to explain the impact, if any, of the findings raised in the report on the audit committee report on the opinion regarding the financial statements considered as a whole.

E. Other Assurance or Related Services on Information Not Within the Current Scope of the Financial Statement Audit

14. Respondents are asked for their reactions to the need for, or potential value of, assurance or related services on the type of information discussed in Section III, Part E.

The role of the auditor should not be extended to provide comfort on information on the financial health or future solvency of companies, the quality of the management or strategic choices.

However, we support the aim of improving the communication of the auditor with stakeholders and consider that it is desirable for auditors to provide assurance on a greater range of information that is relevant for shareholders.

In the context of the audit of insurers, we see considerable merit in discussing further with the IAASB how an international practice statement on the audit of insurance contracts could be developed. This could cover such areas as:

- the role of the auditor in relation to public reporting relating to solvency and how this relates to the ISA audit
- the extent to which internal controls at an insurer are assessed as part of the ISA audit
- the role of the auditor in the assessment of the embedded value calculations used to provide sensitivity information in the disclosures required by accounting standards

In this context, we are not opposed to extending the auditors' review to risk-related information, risk management procedures, internal control and financial reporting processes, key performance indicators and public reporting relative to solvency. However, we consider that it is essential to define the respective responsibilities of the governance bodies and the auditors regarding various types of information.

15. What actions are necessary to influence further development of such assurance or related services?
--

Given existing audit guidance for banks, and the complexity of insurance contracts, we see merit in developing an international audit practice standard on the audit of insurance contracts. This was previously in letters dated 11 February 2011 and 5 April 2011.