



14 March 2013

Our Ref.: C/AASC

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

Dear Sirs,

IAASB's Exposure Draft (ED) on International Standard on Auditing (ISA) 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 Hong Kong Institute of Certified Public Accountants (HKICPA) is the only statutory licensing body of accountants in Hong Kong responsible for the professional training, development and regulation of the accountancy profession. The HKICPA sets auditing and assurance standards, ethical standards and financial reporting standards in Hong Kong.

We welcome the opportunity to provide you with our comments on the IAASB's ED. We support in principle the IAASB's continuing efforts to improve audit quality, increase the value of the auditor's report and narrow expectation gaps. We are concerned with the proposed expansion of the auditor's responsibilities in respect of other information, embedded within the audit of financial statements, in order to meet the perceived expectations of users. This would widen the expectation gap. Under the revised ISA 720 there would be more than extant "assurance" due to the increased responsibilities and proposed statement to be included in the auditor's report. The proposed nature and scope of work surrounding other information is ill-defined. We are concerned that the proposals in ED/ISA 720 are not entirely an appropriate response to issues that users of financial statements have expressed in related to other information. We recommend the IAASB to reconsider the proposals in ISA 720 and to undertake a separate project of studying whether a separate assurance engagement on other information would serve the needs of the market. Our responses to the specific questions in the ED are included in the attachment.

We trust that our comments are of assistance to you. If you require any clarification on our comments, please contact me at simonriley@hkicpa.org.hk.

Yours faithfully,

Simon Riley
Director, Standard Setting

SR/SH/jn

Encl.



ATTACHMENT

HONG KONG INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS' COMMENTS ON THE IAASB'S EXPOSURE DRAFT ON ISA 720 (REVISED)

Request for Specific Comments

Question 1:

Do respondents agree that there is a need to strengthen the auditor's responsibilities with respect to other information? In particular do respondents believe that extending the auditor's responsibilities with respect to the other information reflects costs and benefits appropriately and is in the public interest?

In principle, we are supportive of strengthening the auditor's responsibilities with respect to other information given the increased volume of information to meet stakeholders' expectation in recent years. . We are concerned that the proposals would act to broaden the scope of an auditor's work in an ill-defined way and would result in widening the expectation gap, contrary to what we believe would be the IAASB's intention behind the proposals. We are of the view that the proposals are unwarranted and the framework is not clear to achieve the desired effect. The IAASB is recommended to consider developing a separate assurance engagement on how to meet users' needs in this area instead of embedding it within ISA 720.

Question 2:

Do respondents agree that broadening the scope of the proposed ISA to include documents that accompany the audited financial statements and the auditor's report thereon is appropriate?

In principle, we agree to include documents that accompany the audited financial statements and the auditor's report if they have the primary purpose of providing commentary to enhance the user's understanding of the audited financial statements. However, it is unclear how practical it is to identify all other information that may be made available at the time of the initial release of the financial statements e.g. as there may be large quantities of information made available to regulators and other users at that time, including information being disseminated through electronic means. There should be agreement with management on what "other information" comprises and when that information would be made available to the auditor prior to the commencement of the audit engagement.

Question 3:

Do respondents find the concept of initial release clear and understandable? In particular, is it clear that initial release may be different from the date the financial statements are issued as defined in ISA 560?

The difference between initial release and the date of authorisation of financial statements is not clearly explained in A4 of ISA 720. We would recommend the IAASB to further clarify whether there would be circumstances where the "initial release date" and the "date the statements are issued" are not the same and hence further clarify the distinction between the two. We believe the coverage and requirements contained in ISA 560 by contrast, continues to be appropriate.

Question 4:

Do respondents agree that the limited circumstances in which a securities offering document would be in scope (e.g., initial release of the audited financial statements in an initial public offering) are appropriate or should securities offering documents simply be scoped out? If other information in a securities offering document is scoped into the requirements of the proposed ISA in these circumstances, would this be duplicating or conflicting with procedures the auditor may otherwise be required to perform pursuant to national requirements?

We are of the view that a securities offering document should be scoped out of ISA 720. In Hong Kong, for example, an Initial Public Offering engagement is carried out in accordance with another standard other than an ISA equivalent.

Question 5:

Do respondents consider that the objectives of the proposed ISA are appropriate and clear? In particular:

- (a) Do respondents believe that the phrase "in light of the auditor's understanding of the entity and its environment acquired during the audit" is understandable for the auditor? In particular, do the requirements and guidance in the proposed ISA help the auditor to understand what it means to read and consider in light of the auditor's understanding of the entity and its environment acquired during the course of the audit?**

We do not believe the objectives are appropriate and clear. There is lack of clarity in the phrase "in light of the auditor's understanding of the entity and its environment acquired during the course of the audit". As currently drafted, there is no clear understanding of the objectives and how the work should be carried out to meet the objectives. The objectives should not be referenced against the auditor's understanding which can be judgemental. In addition, the term "auditor" is unclear as to whose knowledge is being referenced against for "reading and considering" the other information. It can be expected that the work would be carried out by the members of the engagement team with the engagement partner being responsible overall. In practice, it would be difficult to gauge how much knowledge the engagement team has in totality. Further clarification should be made to the term "auditor" to clarify if it includes "the firm" which may have an implication on the extent of the auditor's understanding – e.g. would the audit engagement team be expected to have information obtained by other teams while performing other non-audit engagements?

- (b) Do respondents believe it is clear that the auditor's responsibilities include reading and considering the other information for consistency with the audited financial statements?**

We support in principle that the auditor's responsibilities include reading and considering the other information for consistency with the audited financial statements as in the extant ISA 720. However, the extensive application guidance seems to go beyond the work effort normally expected of "considering" and expand the auditor's responsibilities to add credibility of the other information.

Question 6:

Do respondents agree that the definitions of terms of "inconsistency" including the concept of omissions and "a material inconsistency in the other information are appropriate?

The proposed definition of "inconsistency" causes confusion as it is different from common usage and what is ordinarily understood from a dictionary. In the extant ISA 720, the definition of "inconsistency" is made with reference to audited financial statements. However in the proposed revised definition, the inconsistency is in reference to the omission of information that is necessary to properly understand the matter being addressed in the other information which is wider in scope. The auditor may not be in a position to identify such inconsistencies or omission unless the matter has been included in the financial statements. There is a need to apply judgement in determining what is "unreasonable", "inappropriate" and "material inconsistency". There is no clear benchmark for the auditor in applying this ISA and would result in inconsistencies in the work performed. Use of "material" differs from audit materiality elsewhere in ISAs and, as a result, this has the potential to be applied by auditors in a way that differs from the standard setters intentions absent of these intentions being adequately explained in the proposed standard.

Question 7:

Do respondents believe that users of auditors' reports will understand that an inconsistency relates to an inaccuracy in the other information as described in (a) and (b) of the definition, based on reading and considering the other information in light of the auditor's understanding of the entity and its environment acquired during the course of the audit?

We do not believe that users of auditors' reports would fully understand the definition of "inconsistency" as intended in the proposed ISA 720 given that as explained in our response to Question 6 above that it differs from ordinary usage and the definition found in the dictionary. We believe that it should be clarified to the users that the inconsistency is between the other information and the audited financial statements. As currently drafted, the users would incorrectly consider they derive some form of "assurance" on the other information even though it clearly states that there is no audit or review opinion issued in respect of this other information and hence a widening of the expectation gap.

Question 8:

Do respondents agree with the approach taken in the proposed ISA regarding the nature and extent of the auditor's work with respect to the other information? In particular:

(a) Do respondents believe the principles-based approach for determining the extent of work the auditor is expected to undertake when reading and considering the other information is appropriate?

We are supportive of the IAASB using the principles-based approach.

(b) Do respondents believe the categories of other information in paragraph A37 and the guidance for the nature and extent of the work effort for each category are appropriate?

We are of the view that the procedures are practically difficult to apply. Even though the procedures are drafted as application guidance, we are of the view that the procedures would be interpreted as "required" procedures. There is no clear guidance as to the level of work to be performed which would result in inconsistencies in practice and hence interpreted and applied by auditors in significantly different a manner from that as expected by users of audited financial statements.

(c) Do respondents agree that the work effort is at the expected level and does not extend the scope of the audit beyond that necessary for the auditor to express an opinion on the financial statements?

From the detailed procedures in paragraphs A28 to A43, we are not sure how the scope of the audit would not be extended if the auditor is to fulfil the requirements of the proposed ISA 720 and to meet the expectations of users given the express statement the auditor is required to make in the auditor's report.

Question 9:

Do respondents believe that the examples of qualitative and quantitative information included in the Appendix in the proposed ISA are helpful?

We believe further guidance should be provided on the expected work done to be helpful. We consider that appendix serves its apparent purpose of providing a link between the expectation of work to be performed and the nature of other information. In addition, we note from the Appendix that some examples include forward looking information and hence it seems that there is intention to expand the auditor's responsibility in this connection. The IAASB is recommended to clarify the responsibilities of the auditor.

Question 10:

Do respondents believe it is clear in the proposed requirements what the auditor's response should be if the auditor discovers that the auditor's prior understanding of the entity and its environment acquired during the audit was incorrect or incomplete?

The IAASB is recommended to consider adding guidance for situations where modification of the auditor's report is contemplated and in doing so, we would hope that the extent of work required to be performed becomes less open-ended and more commensurate with the nature of other information in relation to the financial statements as a whole.

Question 11:

With respect to reporting:

- (a) Do respondents believe that the terminology (in particular, "read and consider," "in light of our understanding of the entity and its environment acquired during our audit," and "material inconsistencies") used in the statement to be included in the auditor's report under the proposed ISA is clear and understandable for users of the auditor's report?**

We are concerned that the statement would widen the expectation gap. Although it is not the intention of the IAASB for auditors to provide "assurance" on the statement, the fact that the auditor's report contains such a statement on other information, users would likely derive some level of "comfort" or "assurance". We question whether it is reasonable to impose a requirement on the auditor to make a positive statement that no material inconsistencies are identified. The responsibility of preparing other information lies with the management and there is no such requirement on management as to the accuracy and completeness of the other information in most jurisdictions. There is also no corresponding statement under the description of the management's responsibility section of the auditor's report or revision to ISA 580 "Written Representations". We recommend the IAASB reconsider the proposal.

- (b) Do respondents believe it is clear that the conclusion that states "no audit opinion or review conclusion" properly conveys that there is no assurance being expressed with respect to the other information?**

As mentioned in (a) above, we believe users would derive some level of comfort from the statement. Clarification should be made in the statement with reference to the purpose of the procedures carried out.

Question 12:

Do respondents believe that the level of assurance being provided with respect to other information is appropriate? If not, what type of engagement would provide such assurance?

We recommend the IAASB to re-consider the proposals in the ED as a separate limited assurance engagement if the intention of the proposals is to add credibility to the other information which, from a comparison of the proposals in the ED compared to extant requirements, appears to be intention of the IAASB.

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