

International Auditing and Assurance Standards Board
International Federation of Accountants
545 Fifth Avenue, 14th Floor
New York, New York 10017 USA

8 October 2012

Dear Sir/Madam

Re: Invitation to Comment on Improving the Auditor's Report

On behalf of RSM International Limited, a global network of independent accounting and consulting firms, we are pleased to have the opportunity to respond to your invitation to comment on Improving the Auditor's Report.

The financial crisis has intensified concerns about the effectiveness and public understanding of the audit process. Key stakeholders and legislators, including the US Public Company Accounting Oversight Board (PCAOB), the European Commission and other financial statement users, have expressed a desire for more information with regard to certain aspects of the financial reporting process, including the significant risks impacting businesses and the basis for the going concern assumption. It is important that the profession seeks to address those concerns in a measured and timely manner, to enhance confidence in the audit process and ultimately the capital markets.

As many stakeholders in this effort have acknowledged, a holistic approach is necessary to achieve desired results. In addition to potential changes to the auditor's report, changes should be considered and addressed relative to relief from the complexity of financial reporting and allow a financial statement preparer to focus the users' attention on the most important matters facing the entity. Additionally, those charged with governance should be encouraged (or required) to provide more transparency into the processes they employ in their responsibilities for overseeing financial reporting and the external audit.

In forming our responses to this Invitation to Comment, we focused our responses on major themes we believe to be pervasive and important. Management, first and foremost, has the responsibility for communicating information about the entity to users of its financial statements; auditors should not be the original source of this information. It is important that any changes to the auditor reporting model result in enhancing audit quality and thus care needs to be given to reporting information about the audit that is subjective in nature and prone to varying interpretation. And lastly, any changes to the auditor reporting model should serve to lessen the expectations gap, not widen it.

The analysis provided by the International Auditing and Assurance Standards Board (IAASB) in the Invitation to Comment thoroughly describes the key drivers of value, whilst acknowledging many of the impediments to this process. We agree with the overall vision proposed by the IAASB in this Invitation to Comment.

1. Overall, do you believe the IAASB's suggested improvements sufficiently enhance the relevance and informational value of the auditor's report, in view of possible impediments (including costs)? Why or why not?

Overall, we believe the IAASB's suggested improvements enhance the relevance and informational

value of the auditor's report; however, we do have concerns about the relevance and informational value of some specific improvements addressed later in our letter. Importantly, we believe that the key aspect of the auditor's report is the binary 'pass/fail' true and fair opinion. We believe that this feature needs to be retained in the auditor's report as it is one of the most important matters for investors.

We believe the most important driver for these proposals is the demand from financial statement users for more information to be provided in the auditor's report. These proposals address that demand, providing value to those stakeholders that is difficult to achieve by other means, but that is also mindful of additional costs and impediments, which rightly need to be considered as part of this process.

These proposals will significantly impact the nature of the auditor's report and therefore the relationship between the auditor, management and those charged with governance (TCWG). However, the financial crisis has highlighted the need for more information and greater transparency in the financial reporting process.

Ultimately, it will be for these stakeholders and auditors to find an appropriate balance in the level of detail that is appropriate, through public dialogue. It is therefore important that the standard is not too prescriptive and allows that balance be found.

2. Are there other alternatives to improve the auditor's report, or auditor reporting more broadly, that should be further considered by the IAASB, either alone or in coordination with others? Please explain your answer.

An alternative reporting model could be to require the auditor to report on the fairness of the presentation of information provided by management and/or TCWG, whom in-turn would be required by the applicable accounting framework, to report in greater detail than is currently required on significant matters, including going concern and internal control.

Additionally, an alternative to Auditor Commentary that should be explored further is expanded use of required emphasis of matter paragraphs, with the benefit being that the auditor provides a road map to users of where important information disclosed by management is located in the financial statements.

3. Do you believe the concept of Auditor Commentary is an appropriate response to the call for auditors to provide more information to users through the auditor's report? Why or why not? (See paragraphs 35–64.)

The financial reporting process needs to reflect the information needed by the users of the financial statements and as such, the IAASB should consider how best to reflect the demand for more information in the auditor's report.

The concept of an Auditor Commentary is a significant expansion of the auditor's report. In addition to our basic belief that management, first and foremost, has the responsibility for communicating information about the entity to users of its financial statements and that auditors should not be the original source of this information, we have concerns about the following aspects that should be considered:

- The auditor will be expected to provide a commentary on significant matters, which may require the auditor to obtain and validate evidence more precisely than is required under existing auditing standards. Auditors will need to demonstrate knowledge of matters to be reported equal to that of management, in order for the auditor's commentary to have equal informational value to disclosures and reports made by management.
- Obtaining and auditing more information will increase the cost of conducting an audit. Management and shareholders will need to be willing to pay for these additional costs and will need to understand the value derived from the auditor's commentary.

- In addition, because the auditor's commentary will be publically available, there is likely to be more contentious discussion between the auditor and management regarding the disclosures made. This tension in discussions between the auditor and management could possibly result in management not discussing sensitive information with their auditors. In some cases legal advice may be necessary, to determine whether the auditor has a legal right to disclose relevant information, also increasing cost of the audit.
- Auditor's responsibilities will be increased by the introduction of the auditor's commentary. As a result auditor's potential liability will also increase, which will need to be managed in a variety of ways, including internal training and insurance. It may be more difficult in certain jurisdictions to extend or obtain professional liability insurance for this, which will increase audit costs further.

4. Do you agree that the matters to be addressed in Auditor Commentary should be left to the judgment of the auditor, with guidance in the standards to inform the auditor's judgment? Why or why not? If not, what do you believe should be done to further facilitate the auditor's decision-making process in selecting the matters to include in Auditor Commentary? (See paragraphs 43–50.)

It will be difficult to develop more specific criteria (paragraph 47) because the range of applicable facts and circumstances is wide, creating an unacceptable risk that specific criteria exclude a significant matter that would be more likely to be reported under a guidance/judgment regime. Auditors should be permitted to use judgment to determine which matters should be included in the Auditor Commentary. Further, if matters to be addressed in Auditor Commentary are not left to auditor judgment but rather would be required, a significant risk is created that the Auditor Commentary becomes boilerplate with little real informational value added.

5. Do the illustrative examples of Auditor Commentary have the informational or decision-making value users seek? Why or why not? If not, what aspects are not valuable, or what is missing? Specifically, what are your views about including a description of audit procedures and related results in Auditor Commentary? (See paragraphs 58–61.)

Yes, we believe the illustrative examples of the Auditor Commentary have the informational or decision-making value users seek. However, we do not believe that providing detailed descriptions of audit procedures and related results in the Auditor Commentary will provide value and would give rise to significant impediments, including widening the expectations gap.

In complex areas of an audit many interrelated procedures are performed, which together provide sufficient and appropriate audit evidence with regard to the audit area under consideration. Most audit areas are subject to a preliminary analytical review, risk assessments, fraud risk assessments, tests of controls and substantive testing, including substantive analytical review and tests of details. Each of these audit procedures can be complex and therefore it may be impractical to describe those procedures fully, which they would need to be, in order to obtain a complete understanding of the audit procedures applied. Very often there may be a number of audit procedures applied to individual items selected for testing that together provide sufficient and appropriate evidence, but individually do not. Describing each audit procedure in sufficient detail may be impractical or result in an unduly cumbersome audit report.

6. What are the implications for the financial reporting process of including Auditor Commentary in the auditor's report, including implications for the roles of management and those charged with governance (TCWG), the timing of financial statements, and costs? (See paragraphs 38 and 62–64.)

An audit compliant with International Standards on Auditing should address all of the areas included in these proposals. Auditors already conduct audit procedures on significant matters, document their findings, discuss their conclusions with management and TCWG and document those conclusions on the audit file. The key change with these proposals is that a further step is introduced to publically disclose the auditor's findings and conclusions for significant matters in the Auditor Commentary. The

respective roles of the auditor, management and TCWG are unchanged by that new requirement, but their interactions during the audit and particularly at the conclusion of the audit, may be more intense and critical if those findings and conclusions are not mutually agreed or if disclosure could harm the entity in some manner. In all but the most straight-forward and simple of situations, this will lead to an increase in the time and costs to prepare the auditor's report and in some cases, to prepare the supporting documentation because auditors are likely to take even more care over their findings and conclusions, if they expect them to be publically disclosed. Finally, we are concerned that the auditor's public reporting of certain of the information in the Auditor Commentary may actually serve to undermine the role of management and TCWG.

7. Do you agree that providing Auditor Commentary for certain audits (e.g., audits of public interest entities (PIEs)), and leaving its inclusion to the discretion of the auditor for other audits is appropriate? Why or why not? If not, what other criteria might be used for determining the audits for which Auditor Commentary should be provided? (See paragraphs 51–56.)

Yes, we agree because investment decisions based on the auditor's report will be made with respect to listed companies and as such, the Auditor Commentary is likely to add incremental informational value to investors in and regulators of, listed companies. Further, we believe that additional audit costs will be proportionately higher for non-PIEs and the overall benefits to a smaller group of stakeholders will be considerably lower.

8. What are your views on the value and impediments of the suggested auditor statements related to going concern, which address the appropriateness of management's use of the going concern assumption and whether material uncertainties have been identified? Do you believe these statements provide useful information and are appropriate? Why or why not? (See paragraphs 24–34.)

The going concern assumption underpins the basis upon which the financial statements are prepared by management. The addition of a positive statement in the auditor's report affirming the appropriateness of management's use of going concern as the basis for preparation of the financial statements would be of value to the users of the financial statements. However, we believe that the auditor should not be required to provide such positive statements, unless management has disclosed the basis upon which they prepared the financial statements in the notes to the financial statements.

With respect to the auditor's report addressing whether material uncertainties have been identified, care needs to be exercised so as to not create confusion and a widening of the expectations gap, on the part of users of the financial statements. A positive statement from the auditor with respect to the appropriate use of the going concern assumption in the preparation of the financial statements combined with another statement by the auditor that there were material uncertainties that may affect the use of going concern, likely would be confusing to users of the financial statements.

9. What are your views on the value and impediments of including additional information in the auditor's report about the auditor's judgments and processes to support the auditor's statement that no material uncertainties have been identified? (See paragraphs 30–31.)

Paragraphs 18 to 20 of ISA 570 require auditors to disclose material uncertainties in the auditor's report as an Emphasis of Matter paragraph, if adequate disclosure is made in the financial statements and if adequate disclosure is not made, to express a qualified opinion or adverse opinion. Without amendment to ISA 570, we believe that a statement made by the auditor in the auditor's report indicating that no material uncertainties were identified may very well mislead a user of the financial statements into thinking that the auditor had obtained a greater degree of assurance regarding that statement than would be appropriate. As such, we believe that the current construct of ISA 570 with respect to addressing material uncertainties in the auditor's report is appropriate.

10. What are your views on the value and impediments of the suggested auditor statement in relation to other information? (See paragraphs 65–71.)

We support the addition of clarifications to the auditor’s report relative to the auditor’s responsibility with respect to other information. We believe that it would be an appropriate requirement for the auditor to state whether the auditor is aware of any unresolved material inconsistencies between such information and the audited financial statements. This statement would be based on a reading of the other information and this section of the auditors’ report should contain a brief description of the auditor’s responsibility with respect to other information so as to not widen the expectations gap.

11. Do you believe the enhanced descriptions of the responsibilities of management, TCWG, and the auditor in the illustrative auditor’s report are helpful to users’ understanding of the nature and scope of an audit? Why or why not? Do you have suggestions for other improvements to the description of the auditor’s responsibilities? (See paragraphs 81–86.)

We are supportive of clarifying language being added to the auditor’s report related to the auditor’s responsibility for auditing the financial statement footnote disclosures and for fraud, the responsibilities of TCWG, and the meanings of “reasonable assurance,” “material misstatement” and “fairly presented” (or “true and fair view”). All of this additional clarifying language should be added with the aim of lessening the expectations gap. To that end, we encourage the IAASB to continue outreach to users of the financial statements and auditor’s report to determine whether the proposed descriptions of auditor’s responsibilities truly result in users have an appropriate understanding of the auditor’s responsibilities (i.e., written in plain, non-technical English).

12. What are your views on the value and impediments of disclosing the name of the engagement partner? (See paragraphs 72–73.)

We acknowledge the right of national standard-setters and regulators to require disclosing the name of the engagement partner and that this is already required in certain jurisdictions. However, careful consideration should be given to liability considerations that could result in other jurisdictions, due to regulatory requirements as well as national statutes and local laws. As such, we believe that any such requirement should be left to the decision of national standard-setters and regulators rather, than establishing an international requirement.

13. What are your views on the value and impediments of the suggested disclosure regarding the involvement of other auditors? Do you believe that such a disclosure should be included in all relevant circumstances, or left to the auditor’s judgment as part of Auditor Commentary? (See paragraphs 77–80.)

With respect to group audits, more value to users could be achieved by describing the scope of work performed at key components, rather than disclosing the names of other auditors or seeking to place reliance on their work. Users of the financial statements may be more interested in understanding the nature and extent of audit work performed on a key component, rather than the name of the audit firm performing that work. Any additional disclosure regarding the involvement of other auditors should not detract from the “sole responsibility” concept and as such, it may be necessary to add clarifying language regarding the responsibilities of the auditor and other auditors should this disclosure be required.

14. What are your views on explicitly allowing the standardized material describing the auditor’s responsibilities to be relocated to a website of the appropriate authority, or to an appendix to the auditor’s report? (See paragraphs 83–84.)

We believe the value of clarifying the auditor’s responsibilities outweighs the impediments of providing the additional material in the auditor’s report. Moving this clarifying material to a website lessens the likelihood of it being considered by users of the financial statements and thereby decreases its informational value.

15. What are your views on whether the IAASB's suggested structure of the illustrative report, including placement of the auditor's opinion and the Auditor Commentary section towards the beginning of the report, gives appropriate emphasis to matters of most importance to users? (See paragraphs 17–20.)

We agree with the proposed structure and believe that the auditor's opinion should be at the start of the report as it will help to put any subsequent comments in the Auditor Commentary in context of the overall 'pass/fail' opinion. We also believe that consideration should be given to placing all paragraphs in the auditor's report addressing going concern in closer proximity to one another (i.e., management's responsibilities, auditor responsibilities and conclusions). While we support the proposed structure of the illustrative report, a concern should be acknowledged about moving the auditor's opinion and the Auditor Commentary section to the beginning of the report. If it is true that there is informational value in more clearly explaining the roles and responsibilities of preparers, TCWG, auditors, etc., then a risk exists that at least some users of the financial statements would read no further than the auditor's opinion or perhaps Auditor Commentary and therefore would not understand the full context in which the auditor's opinion was issued.

16. What are your views regarding the need for global consistency in auditors' reports when ISAs, or national auditing standards that incorporate or are otherwise based on ISAs, are used? (See paragraphs 21–23 and 87–90.)

There is a need for national legal and regulatory requirements to be accommodated within the Auditor's Report. However, as the recognised international auditing standard setter, the IAASB should develop and promulgate a high quality minimum standard for auditor reports and work with national bodies to encourage the consistent application of ISA 700. Outside the core elements of the report, there should be sufficient flexibility to allow individual jurisdictions to include their relevant legal requirements that may not be required in other jurisdictions.

17. What are your views as to whether the IAASB should mandate the ordering of items in a manner similar to that shown in the illustrative report, unless law or regulation require otherwise? Would this provide sufficient flexibility to accommodate national reporting requirements or practices? (See paragraph 17 and Appendix 4.)

Please refer to our response to Question 16 above.

18. In your view, are the IAASB's suggested improvements appropriate for entities of all sizes and in both the public and private sectors? What considerations specific to audits of small- and medium-sized entities (SMEs) and public sector entities should the IAASB further take into account in approaching its standard-setting proposals? (See paragraphs 91–95.)

As explained above, we do not believe that the value of IAASB's suggested improvements exceeds the costs or impediments in the case of SMEs. However, we believe that there is a need for consistency between the audit reports of all entities audited in accordance with ISAs. Therefore we encourage the IAASB to develop an auditor report with minimum requirements applicable to all entities including SMEs, comprising:

- Opinion
- Basis for opinion
- Going Concern
- Respective Responsibilities of Management and the Auditor
- Report on Other Legal and Regulatory Requirements

And additional requirements for PIEs, comprising:

- Auditor Commentary
- Other information



We would be pleased to discuss our comments further with members of the IAASB or its staff. If you wish to do so, please contact Robert Dohrer (tel: +44 207 601 1080; email: robert.dohrer@rsmi.com).

Yours sincerely

A handwritten signature in black ink that reads "Jean M Stephens".

Jean M Stephens
Chief Executive Officer
RSM International

A handwritten signature in black ink that reads "Robert Dohrer".

Robert Dohrer
Global Leader - Quality and Risk
RSM International