

IAASB CAG PAPER

IAASB CAG Agenda (March 2010)

Agenda Item N.2

Other Information in Documents Containing Audited Financial Statements—ISA 720—Preliminary Issues

The Auditor's Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements—ISA 720—Preliminary Issues

Papers to Be Referred to during Discussion

1. The discussion of this agenda item will follow the structure of this Preliminary Issues Paper.
2. Since the IAASB's approval of the proposal in December 2009, the Task Force has focused its considerations on issues to be addressed in the revision of ISA 720¹ that it considers to have implications for the scope of the revised ISA. Apart from the preliminary issues outlined in this paper, it is the Task Force's intention that the other matters that will need to be addressed in the revision of ISA 720 be discussed at the next CAG meeting in September.
3. Hyperlinks presented at the end of this Preliminary Issues Paper to the Issues Paper for the March 2010 IAASB meeting are for reference only.

Project Status and Timeline

4. The proposal for this project was considered and approved at the December 2009 IAASB meeting.
5. The IAASB will be considering similar issues to those contained in this Preliminary Issues Paper at its upcoming March meeting and a further issues paper at its June meeting.

Matters for CAG Consideration

Documents Containing Audited Financial Statements Addressed by ISA 720

6. Extant ISA 720² applies to "annual reports (or similar documents), that are issued to owners (or similar stakeholders), containing audited financial statements and the auditor's report thereon." The ISA also recognizes that it may be applied, adapted as necessary in the circumstances, to other documents containing audited financial statements, such as documents used in securities offerings.
7. The corporate reporting environment has evolved significantly over the last decade. Entities have embraced a variety of mechanisms with the aim of communicating more effectively with their stakeholders. In addition to the annual report which is traditionally relied on by entities for the purpose of reporting their activities and performance, other documents which may also contain audited financial statements have taken on a heightened level of importance. Examples of such documents include interim reports, summary financial reports, shelf registration documents and prospectuses.

¹ ISA 720, "The Auditor's Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements."

² ISA 720, paragraph 2.

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8. In assessing whether the scope of extant ISA 720 is fit for purpose in the present corporate reporting environment, the Task Force considered the reason for the ISA's focus on documents like the annual report that are issued to owners (or similar stakeholders). In this regard, the Task Force believes that the considerations outlined below are of relevance.
9. ISA 560³ states that the auditor has no responsibility to perform any procedures regarding the financial statements after the date of the auditor's report. Extending this to the context of the auditor's responsibilities under ISA 720, the documents containing the audited financial statements which the auditor needs to read the other information contained therein would, accordingly, need to be prepared within the same timeframe as the financial statements and with the intention of being made available to the auditor prior to the date of the auditor's report.
10. Furthermore, the rationale behind ISA 720 is that the auditor reads the other information in documents containing the audited financial statements, not only for avoidance of being associated with other misleading information, but also, in serving directly the interest of the audit, to identify material inconsistencies that may have an effect on the audited financial statements and the auditor's report. This provides further support for ISA 720 to deal with documents which are intended to be prepared within the same timeframe as the financial statements, and with the intention of being made available to the auditor prior to the date of the auditor's report.
11. The Task Force recognizes that there are other documents which may contain the audited financial statements and the auditor's report, such as a prospectus, however, requiring the auditor to read these documents as part of the auditor's responsibilities under the ISAs would not be consistent with the requirements of ISA 560 as explained.
12. Accordingly, the Task Force believes that the extant focus of ISA 720 on annual reports continues to be appropriate and should not be expanded to address these other documents. Notwithstanding this, the Task Force proposes to clarify and explain the reason for ISA 720's inclusion (and exclusion) of the documents that are currently within its scope.
13. Related, the Task Force further identified that, in certain cases, local laws and regulations may dictate the auditor's responsibilities in regard to documents that are most commonly employed by entities for reporting purposes, for instance, in the case of prospectuses, the Prospectus Directive in the European Union (EU) and Section 7110⁴ in Canada. For some of these documents, local laws and regulations may prescribe the application of the requirements and guidance in ISA 720 although some may argue that these documents do not fall within the scope of the ISA which extends to "annual reports." The Task Force is of the view that it should be clarified that such responsibilities are outside of the obligations of the auditor under

³ ISA 560, "Subsequent Events," paragraph 10.

⁴ The Canadian Auditing and Assurance Standards Board's Assurance Section 7110, "Auditor Involvement with Offering Documents of Public and Private Entities."

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the ISAs.

Matter for CAG Consideration

1. Do Representatives agree that the extant focus of ISA 720 on annual reports continues to be appropriate?

The Auditor's Responsibilities with Regard to Other Information

14. In considering the nature and extent of the auditor's responsibilities in connection with the other information as set out in the project proposal, the Task Force discussed the procedure required of the auditor to "read the other information."⁵ The Task Force concluded that the intention of the ISA is not just to require the auditor to *read* the other information but for the auditor to *read* the other information and *consider* whether such information is materially inconsistent with the audited financial information (emphasis-added). The Task Force is of the view that the latter more fully expresses the intent of the requirement since auditors are unlikely to merely read the other information without applying an appropriate thought process because otherwise, performance of the procedure is unlikely to result in the achievement of the objective as stated ISA 720.
15. As extant ISA 720 does not contain guidance in support of the requirement for the auditor to read the other information, the Task Force recommends that the ISA be revised as follows:
 - Revising the requirement to include, in addition to reading the other information, the responsibility for the auditor to consider whether such information is materially inconsistent with the audited financial statements and the auditor's report. In this regard, the Task Force also discussed the use of the words "assess" and "evaluate" but concluded that usage of such words may seem to imply that a greater level of work effort is necessary than that envisaged for achieving the objective of ISA 720. Further, usage of such words may be perceived to denote an implied documentation requirement.
 - Providing application material in support of the proposed requirement to clarify the following:
 - The consideration given by the auditor in reading the other information is performed in light of the auditor's knowledge of the entity and information acquired during the course of the audit or in performing procedures on the audit; and
 - The matters the auditor may consider in reading the other information. For example, in cases where the other information is derived from the audited

⁵ ISA 720, paragraph 6.

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financial statements, auditors typically will perform a cross-check of the relevant other information with the audited financial statements.

Matter for CAG Consideration

2. Do Representatives agree with the Task Force's proposal to require the auditor, in reading the other information, to consider whether such information is materially inconsistent with the audited financial statements in light of the auditor's knowledge of the entity and information acquired during the audit?

Electronic Dissemination of the Audited Financial Statements and the Auditor's Report

16. Extant ISA 720 does not address the method of dissemination of annual reports. Since the standard was last revised in 1993,⁶ it is likely that traditional printed hard-copy was, at that time, the method most commonly employed by entities for distributing annual reports although electronic formats of annual reports were likely to have been employed to some extent. With improvements both to the state and cost of technology, and developments in local laws and regulations, preparers have increasingly taken to disseminating electronic formats of their annual reports through their websites for reporting purposes.
17. In discussing the matter of electronic dissemination, the Task Force was of the view that the starting points of such considerations are the audited financial statements and the auditor's report *rather than* the other information which accompanies these statements (emphasis-added). Although there are undoubtedly specific considerations which the auditor may need to give in regard to the other information when electronically disseminated, in the context of the ISAs, the Task Force felt that the initial focus should appropriately be on the audited financial statements and the auditor's report. The other information, amongst other matters, should be taken into account by the auditor but on the basis that it could undermine the credibility of those financial statements and the auditor's report.
18. Further, the Task Force drew parallels between the electronic dissemination of audited financial information and circumstances involving: i) the reproduction of audited financial information in electronic formats for example, HTML, PDF, XBRL, and video; and ii) the translation of the audited financial statements and the auditor's report into other languages.
19. When documents containing the audited financial statements and the auditor's report are disseminated electronically, the auditor may be perceived to be associated with these electronic documents even though the auditor has little, if any, control over the circumstances under which the audited financial information has been disseminated. Similar consideration may be extended to instances involving the reproduction and translation of audited financial statements and the

⁶ Conforming amendments were made to the extant ISA 720 when the IAASB issued its audit risk standards in October 2003. Subsequently, as part of the IAASB's Clarity project, extant ISA 720 was redrafted (but not revised) and clarified ISA 720 was released in March 2009.

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auditor's report. Specifically, such information may not be correctly reproduced or accurately translated but with which the auditor may nevertheless be seen to be associated. Accordingly, for completeness, when considering whether to address the matter of electronic dissemination of the audited financial statements and the auditor's report, it is felt that consideration will similarly need to be given to the matters of reproduction and translation.

20. With consideration for the above, the Task Force is of the view the extant scope of ISA 720 should be retained, and clarifying guidance introduced in the ISA, to indicate that the standard does not deal with matters relating to the dissemination, reproduction, and translation of the audited financial statements and the auditor's report. Notwithstanding this, the Task Force believes that such matters should be addressed and that further discussions be had with the IAASB as to how this may best be achieved.

Matter for CAG Consideration

3. Do Representatives agree that the extant scope of ISA 720 should be retained and further clarified in regard to the matters of electronic distribution, reproduction and translation of the audited financial statements and the auditor's report?

Action Requested

21. The CAG is asked to review and comment on the preliminary issues highlighted in this issues paper, or any other matters which may be of relevance to the project.

Material Presented – FOR IAASB CAG REFERENCE PURPOSES ONLY

Agenda Item 5-A of the March 2010 IAASB Meeting – Other Information in Documents Containing Audited Financial Information – Issues and IAASB Task Force Proposals

[Link to follow](#)