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

Dear Sir/Madam

COMMENTS ON EXPOSURE DRAFT 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 EXPOSURE DRAFT)

Thank you for providing us with the opportunity to provide comment on the Exposure Draft.

It is our understanding that the Exposure Draft is primarily attempting to address two shortcomings in current practice – as follows:

1. That users might take unwarranted reliance:
   a. from other information contained in a document containing audited financial statements; or
   b. from other information accompanying audited financial statements.

2. That auditors may not be “reading and considering” all of the other information that they should be.

In our view, while attempting to address the above issues, some of the requirements in the Exposure Draft appear to extend audit scope with a consequential extension of work effort, a further widening of the audit expectation gap, increased audit risk and increased audit liability.

We are also concerned that the extension of the auditor’s responsibility to “read and consider” other information accompanying [emphasis added] the audited financial statements, and which has a [emphasis added] primary purpose of providing commentary to enhance the users’ understanding of the audited financial statements or the financial reporting process, whilst admirable, will be very difficult to apply in practice. The reasons for our view are twofold:

1. The other information accompanying the audited financial statements is often not available until after the audit report has been issued. The ability of an auditor to influence any change to other information made available after the issue of the audit report is significantly reduced, unless the auditor threatens to withdraw the audit report, which is a ‘big call’ for an auditor to make. Accordingly, the auditor’s level of tolerance for ‘material inconsistencies’ in other information made available after the issue of the audit report is going to be much higher than for other information made available before the audit report is issued. This is not an acceptable situation in which to place the users of ‘other information’, as they should expect the same level of “reading and consideration” of other information by the...
auditor, irrespective of whether the other information is made available to the auditor before or after the audit report is issued.

2. The other information accompanying the audited financial statements, particularly in a public sector environment, may consist of a wide range of documents ranging from press releases by elected representatives to documents that include (as part of their content) commentaries on the performance of an entity or group of entities. There is also a possibility that the other information, in a public sector context, may be provided by a government agency with oversight responsibility for the particular government entity that is subject to audit. The ability of the auditor to access other information in these circumstances may be subject to significant practical difficulties including, for example:

a. There may be a significant delay between the time the audit report is issued and when the other information becomes available.

b. In a political environment a press release by an elected representative may be regarded (by the elected representative) as part of their accountability to the electorate, and a matter that has nothing to do with the auditor. In some cases it may be that the auditor is refused access to this information.

At present, the auditing standards preserve the delicate balance of responsibilities between the auditor and those within, or associated with, the entity who are being held to account. In the situation referred to above, there is also a possibility that the Exposure Draft could bring the role of the auditor into direct conflict with the role of those who are directly accountable to users. This is undesirable because the requirements of the Exposure Draft have the potential to confuse users over the respective roles of the auditor and the accountable party.

In summary we recommend that the final standard:

1. Is limited to including requirements to clarify the auditor’s responsibility to “read and consider” the other information before the audit report is issued. However, the final standard should recognise that the auditor may not be able to gain access to all other information for various reasons, including the likelihood that an elected representative in the public sector may choose not to make the other information available to the auditor because they consider that information to be outside the auditor’s role. This risk is mitigated by the auditor disclosing in the audit report the documents they have “read and considered”.

2. For other information issued by the entity after the audit report is issued, the auditor’s work should be limited to assessing whether the other information indicates that the audit report remains appropriate.

We have provided responses to the questions accompanying the Exposure Draft in the attachment to this letter.
Should you have any questions concerning our submission, please do not hesitate to contact me.

Yours sincerely

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Submission of the Office of the Controller and Auditor-General (New Zealand)

Exposure Draft: 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

Our Comments on Specific Questions

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?*

We support the desire to clarify the auditor’s application of ISA 720 to remedy existing shortcomings, but we do not consider there is any need to strengthen or extend the auditor’s responsibilities with respect to the other information.

As noted in the covering letter, we have interpreted the shortcomings as follows:

- That users might take unwarranted reliance:
  - from other information contained in a document containing audited financial statements; or
  - from other information accompanying audited financial statements.
- That auditors may not be “reading and considering” all of the other information that they should be.

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?*

We support the clarification that the auditor also “reads and considers” certain documents that accompany the audited financial statements before the audit report is issued.

However, for other information issued by the entity after the audit report is issued, we believe that the auditor’s work should be limited to assessing if the other information indicates that the audit report remains appropriate.

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?*

We understand the concept of initial release, whilst noting that the distinction between ‘initial release’ and ‘date the financial statements are issued’ is subtle.

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?*
In our opinion, securities offering documents should be scoped out of the requirements of ISA 720. The reason for this is that in New Zealand the auditor’s responsibilities for securities offering documents is specified in legislation.

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 consider 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, and that the Exposure Draft helps the auditor in applying the requirement.

   (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 consider that it is clear that the auditor’s responsibilities include reading and considering the other information for consistency with the audited financial statements.

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?

   We agree that the definitions of terms of “inconsistency” including the concept of omissions and “a material inconsistency in the other information” are appropriate.

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 are of the view that a user will interpret ‘inconsistency’ in the context of their own particular interests and not in terms of users as a collective group. In other words, the audit expectation gap will remain.

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 agree with a principles based approach to determining the extent of work effort by the auditor.

   (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 agree that the categories of other information in paragraph A37, and the guidance about the nature and extent of the work effort for each category appears to be appropriate.
(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?

The work effort required of the auditor to “read and consider” other information before the audit report is issued seems reasonable.

However, for other information issued by the entity after the audit report has been issued, we believe that the auditor’s work should be limited to assessing if the other information indicates that the audit report remains appropriate.

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

The auditor will need to “read and consider” all other information. The Appendix in the Exposure Draft may assist an auditor identifying the particular aspects of the other information to be “read and considered”. However, the extent to which the auditor can “validate” some of the qualitative financial information such as “general descriptions of the business environment and outlook” will depend on how well the auditor understands the entity and its environment. This will be a matter of professional judgement.

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?

This matter is clearly specified in paragraph 15 of the Exposure Draft.

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 of the view that a user will interpret this terminology in the context of their own particular interests, and not in terms of users as a collective group. In other words, the audit expectation gap will remain.

(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?

We are of the view that users will take some form of assurance from the statement in the audit report based on our experience. Most readers do not understand the concepts of reasonable and limited assurance.
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?

No assurance is being provided technically, although users will take some form of assurance from the work the auditor has carried out on other information. However, we consider the example statement in paragraph A57 of the Exposure Draft adequately explains what an auditor has done, in a technical sense.

Our Comments on General Questions

In addition to the requests for specific comments above, the IAASB is also seeking comments on the matters set out below:

(a) **Preparers (including Small- and Medium-Sized Entities (SMEs)), and users (including Regulators)**—
The IAASB invites comments on the proposed ISA from preparers (particularly with respect to the practical impacts of the proposed ISA), and users (particularly with respect to the reporting aspects of the proposed ISA).

We know that SMEs will not want the proposed standard to lead to unnecessary hold-ups in the finalisation of the financial statements, nor in the audit incurring additional costs. However, these are matters that should be capable of being managed by the auditor when auditing a SME.

(b) **Developing Nations**—Recognizing that many developing nations have adopted or are in the process of adopting the International Standards, the IAASB invites respondents from these nations to comment on the proposed ISA, in particular, on any foreseeable difficulties in applying it in a developing nation environment.

Developing nations face difficulties in applying the ISAs where both auditing and financial reporting expertise is in short supply.

(c) **Translations**—Recognizing that many respondents may intend to translate the final ISA for adoption in their own environments, the IAASB welcomes comment on potential translation issues respondents may note in reviewing the proposed ISA.

We have no comments to make on potential translation issues.

(d) **Effective Date**—Recognizing that the proposed ISA is a substantive revision, and given the need for national due process and translation, as applicable, the IAASB believes that an appropriate effective date for the standard would be 12–15 months after issuance of the final standard. Earlier application would be permitted. The IAASB welcomes comment on whether this would provide a sufficient period to support effective implementation of the ISA.

An effective date of 12 to 15 months after the issuance of the final standard seems reasonable.