



Mr. James Gunn
Technical Director
IAASB
545 Fifth Avenue, 14th Floor
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USA

10 October 2012

Ref.: AUD/PRJ/HBL/NRO/SHA

Dear Mr. Gunn,

Re: IAASB Invitation to Comment (ITC): Improving the Auditor's Report

FEE¹ is pleased to provide you with its comments on the IAASB Invitation to Comment (ITC) on Improving the Auditor's Report.

With the unfolding of the financial crisis, the audit profession is prepared to reassess its role and how it can enhance its contribution to the economy and to society. FEE fully supports initiatives that will lead to more user friendly, relevant and informative auditors' communication.

In this respect, we welcome this IAASB project as FEE believes that global solutions for auditor's reports are preferable and will benefit investors and other users. Furthermore, any such global solutions should be scalable to provide for the differing information needs of the users between different market segments.

Audit has become more complex over the recent years with the increase in the complexity of entities' business models and financial reporting. New solutions for auditor communication should be sufficiently flexible to allow for further developments in both of these areas. In this context, the auditor's reporting cannot be viewed in a vacuum; rather there is a strong link to financial reporting. In addition, care needs to be taken to ensure that the so called "expectation gap" is not increased, i.e. that exactly what the auditor is reporting (and what the auditor is not reporting) is capable of being properly understood. This would ensure that the core service of the audit profession, the audit, continues to be valued by its users. However, improvements should only be made that really do meet user needs and enhance audit quality, i.e. by providing better information as opposed to merely providing more information.

¹ FEE (Fédération des Experts comptables Européens - Federation of European Accountants) is an international non-profit organisation based in Brussels that represents 45 institutes of professional accountants and auditors from 33 European countries, including all of the 27 European Union (EU) Member States.

FEE has a combined membership of more than 700.000 professional accountants, working in different capacities in public practice, small and big accountancy firms, businesses of all sizes, government and education, who all contribute to a more efficient, transparent and sustainable European economy.

In the broader context of the European debate on audit policy, it has become even more urgent to review at an international level whether improvements can be made as to how auditors should best communicate with all relevant stakeholders. FEE would strongly encourage cooperation between the IAASB and the European Institutions in order to ensure that any proposed improvements are aligned on an international level: we seek a globally compatible solution that gives due credence to both the European Commission's (EC) Proposals and ISA 700 improvements. In the absence of such satisfactory cooperation, we might end up with two different auditor's reports, which would be very costly and diminish transparency for users.

Our main comments are summarised below:

1. The project of improving the auditor's report should be dealt together with a project on auditor's reporting as a whole. The auditor's reporting consists of reporting to the public in the auditor's report (ISA 700) and also of reporting to those charged with governance of the company (ISA 260). Therefore, due consideration should be given to how this reporting has to be inter-related. This IAASB ITC focuses almost solely on public auditor's reporting, but FEE strongly believes that more can be done in the area of auditor's reporting internally to those charged with governance and the interaction between the two types of reporting.
2. FEE agrees that specific information about the audit could be provided by the auditor, such as information on significant audit risks in the Auditor Commentary section. Indeed, the profession is willing to explain more about the work performed, but not to navigate the users through the complexities of the financial statements. We call for ISA compliant reporting on significant audit risks. FEE believes that details regarding audit work performed to address specific significant audit risks identified during the audit of the entity are more useful than generic information. Such an approach will enhance transparency and credibility of the auditor's work and will add value to the auditor's report. In this respect, it will be essential to set clear principles-based criteria in order to specify which and how identified significant audit risks could be reported.
3. It is strategically important for the future of the audit profession to respond to stakeholder's needs by reporting on the appropriateness of management's use of the going concern assumption, especially when there are significant risks in this regard. However, the key principle is that it is the responsibility of management and those charged with governance of an entity to provide the required underlying information. The auditor's report paragraph on going concern should relate to information provided by the audited entity itself. Having this principle in mind, FEE believes that there is an urgent need to reflect on expanding the financial reporting standards related to going concern reporting by management in order to meet, at least partly, the market needs. Therefore, we encourage the IAASB to initiate discussions with the relevant standard setters, such as the International Accounting Standards Board (IASB) in order to coordinate such financial reporting enhancements.
4. Regarding the auditor's statement on other information, FEE believes that the requirements included in ISA 720 could be further extended to make the auditor's report more informative and comprehensive. Therefore, we propose that the auditor should also report on the consistency of other information with the financial statements based on his or her knowledge

and understanding of the entity and its environment. FEE would also stress the importance of ensuring that no new expectation gaps arise in this area.

5. Any changes introduced in the auditor's report regarding clarifications and transparency should be carefully considered in order to guard the profession against the criticism of being too defensive and using boilerplate language. However, auditors should be able to use their professional judgment when necessary.
6. FEE fully supports global standardisation of the content order in the auditor's report for which we recommend the IAASB use a principles-based structure. This would help the users navigate through the auditor's report. It will also further enhance comparability underlying the "ISA-brand".

For further information on this FEE letter, please contact Hilde Blomme at +32 2 285 40 77 or via email at hilde.blomme@fee.be or Noémi Robert at +32 2 285 40 80 or via email at noemi.robert@fee.be from the FEE Secretariat.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Philip Johnson', with a long, sweeping horizontal stroke extending to the right.

Philip Johnson
FEE President

Appendix: Responses to Questions

Overall Considerations

Question 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?

FEE is in overall agreement with the project of the IAASB to enhance the relevance and informative value of auditor's reporting. FEE fully supports initiatives that will lead to having a more user-friendly auditor's report that is easier to understand and more informative.

The recent debate has highlighted that there is a need to provide the public with more information about what an audit is and what the output of an individual audit is. It is the role of the profession to respond to the concerns expressed. It remains an important role of today's profession to provide comfort on the reliability of financial reporting: the auditor's report accompanies the entity's financial statements and the additional auditor reporting will help to add more credibility to those financial statements as well as generating confidence in the audit.

But, the IAASB should be aware of the following considerations:

- Not to attribute management responsibilities to the auditor: management has primary responsibility for providing relevant information in the financial statements, in accordance with a specified financial reporting framework. The auditor has a responsibility to audit those financial statements. It is the responsibility of management to disclose all required information in the financial statements, and this should not be blurred by any requirement for the auditor to take over such responsibility. All disclosures that relate to the individual business model, business risks, choices of options for accounting policies, sensitivity analyses, etc., should therefore be disclosed by the entity itself.
- Issues encountered with the current financial reporting framework should not be transferred to the auditor. In relation to some specific topics, financial reporting has become difficult to understand for users over the last few years. Nevertheless, it should not be the role of the auditor to navigate users through the financial statements.
- There are risk management issues to address, such as the consequences for the auditor of an entity failure, where the auditor had not included the issue in his/her commentary. The new requirements might increase audit risk, and hence costs.
- Not to place an excessive burden and additional costs on companies if no or little benefit to meeting users' needs can reasonably be expected. Responding to users' needs for more information should be proportionate to the nature, size and complexity of the entity. We refer to our response to Question 7 in this matter.

The general support that FEE gives to the IAASB ITC is subject to our detailed comments below.

Question 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.

As explained in Question 1, the proposals on auditor's communication should be supported to make it more practicable and useful and thus FEE is in favour of the initiatives of the IAASB. However, FEE believes that the IAASB should also consider the following matters in further detail:

- There is an interaction between external and internal auditor reporting. Auditor's reporting consists of:
 - o Reporting to the public in the public external auditor's report (ISA 700); and
 - o Communication with, and/or reporting, to those charged with governance of the company in an internal capacity (ISA 260).

In this ITC, the IAASB focuses almost solely on the public reporting, but equal attention is needed to show how this impacts with the private auditor's reporting to those charged with governance, including the audit committee. FEE strongly believes that there is room for improvements in this area. We consider that the way forward is that the auditor provides additional information to the audit committee regarding significant findings from the statutory audit, including for instance any significant deficiencies in internal control, any significant difficulties encountered during the audit, any significant qualitative aspects of the entity's accounting practices and/or any significant matters arisen from the audit that were discussed with management.

- When discussing reporting, an important principle should be kept in mind: the auditor's reporting cannot be seen in a vacuum, there is a link to financial reporting. An auditor's responsibility is to express an opinion on the financial statements and other information as prepared by an entity's management and board(s) in accordance with the applicable financial reporting framework, being national or international accounting standards. Accordingly, when considering auditor's reports, any discussion about the auditor's role and reporting needs to start with the underlying financial reporting framework and its ability to meet the needs of users and other stakeholders. Therefore, FEE believes that a comprehensive evaluation of the whole financial reporting system may be needed. The IAASB can play an important role in initiating such discussions, especially with standard setters, such as the International Accounting Standards Board (IASB).
- In the European Union (EU), we currently have the European Commission (EC) proposals (reference is made to Article 22 in the EC Proposed Regulation on the auditor's report). These proposals include a number of matters that are perceived to be too prescriptive or too detailed. In particular, an assessment of the internal control system is being proposed, which could involve significantly increased (documentation) costs for companies with little added value and which should be avoided.

Moreover, as most of the additional matters are only proposed to be included in the public auditor's report of Public Interest Entities (PIEs), the comparability between the audit reports

worldwide and between different segments of the market will seriously diminish: for instance, comparable companies (one listed and one equally large non-listed entity) in the same or similar sectors might not be approached in the same manner in terms of public reporting by the auditor. In relation to this concern, FEE draws attention to the sensitivities surrounding the definition of PIEs, especially for supervisory purposes. Indeed, the definition varies by jurisdiction and, therefore, may not constitute a consistent and practical criterion. Extending this definition should be considered very carefully in order not to put additional burdens on low risk or low complexity entities with limited effect to the public interest.

FEE would like to invite the IAASB to reflect on how its proposals can alleviate some of these concerns, not in the least in the light of our next comment.

- Last but not least, it cannot be emphasised enough that the final revised ISA 700, which will eventually result from this IAASB ITC, might come too late to influence the final outcome of the EC Proposals on the auditor's report. FEE would encourage the IAASB to work with the EC to see whether this concern can be dealt with. Otherwise, we might end up with two different auditor's report, which would be very costly and diminish transparency for users.

We refer to our comments below regarding the different alternatives for improvement FEE would like to recommend to the auditor's report as proposed in the IAASB ITC.

Auditor Commentary

Question 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).

FEE is willing to respond to the call for auditors to provide more information to users through the auditor's report.

In order to enhance the auditor's report in an efficient way and to give added-value insights into the audit work, FEE is convinced that the information included in the auditor's report has to follow directly from the ISA framework. The ITC proposals are, in contrast, not sufficiently precise, in that they do not include appropriate criteria for determining matters to be reported. Under ISAs, auditors are required to undertake a risk assessment to identify the key areas that they should concentrate their audit upon. These are called "significant risks". As defined in ISA 315, a significant audit risk is "an identified and assessed risk of material misstatement that, in the auditor's judgment, requires special audit consideration", colloquially put "key matters of audit focus".

Having this in mind, FEE supports inclusion of information on the audit approach in the auditor's report, more specifically on the significant audit risks because:

- The auditor's report should focus on significant areas of audit work or key areas of audit focus, which are linked to accounting or financial reporting matters. This is linked to the principle that the auditor should ordinarily not report on matters that are the responsibility of management. We refer to our response to Questions 1 and 2 in this respect;
- Identifying and responding to significant audit risks are key and fundamental to the performance of the audit. ISA 315 already requires the auditor to identify and document significant risks and ISA 330 to perform audit procedures to respond to those risks, thus information on these risks is already available to the auditor;
- Explaining major significant risks identified will create the opportunity to include more company or entity specific information and less generic or boilerplate information in the auditor's report;
- The auditor has considerable experience of identifying significant risks on audits and thus this has led to a high level of consistency between entities with the same characteristics. This would, therefore, help to drive consistency in what is being included in the auditor commentary section;
- In addition, as significant risks are audit driven (and not management driven), it would ensure that management has low leverage on the content of the auditor's report. Management's influence would be largely reduced to matters of wording and style rather than content;
- Reporting on significant risks will enable auditors to give added-value information related to a large number of areas of the financial statements and could, for example be related to revenue recognition, use of fair value measurements including measurement of financial instruments, sovereign debt exposure etc. The number of significant risks identified varies from entity to entity depending on the risk profile, the industry and complexity of the business. However, FEE is convinced that this number normally falls in the range from zero

to ten. Therefore, reporting significant audit risks in the external auditor's report would be feasible from a quantitative perspective;

- Providing users with clear information about the work done on each of these specific areas, supporting the audit opinion on the financial statements as a whole, will maintain the clear pass/fail nature of the auditor's report. In this way, misconceptions about piecemeal audit opinions could be mitigated;
- However, users may be unfamiliar with the term significant audit risk, so FEE proposes this would be explained as the criteria the auditor uses during the risk assessment procedures in identifying the key areas that the auditor should concentrate his or her audit upon.

Further to the above, FEE is concerned about including "matters that are important to the users' understanding" of the audited financial statements for the following reasons:

- The auditor's report is not intended to navigate the user through the financial statements;
- Some of these matters should only be reported internally to those charged with governance, not publicly. We refer to our comments on the IAASB examples of Auditor Commentary to demonstrate the issues linked with reporting on this kind of information in the public auditor's report;
- Reporting on specific items in the financial statements might give the impression that the auditor expresses piecemeal audit opinions;
- There is a risk of inclusion of boilerplate information in the auditor's report.

To clarify our views on matters which should be reported on or not, FEE also believes that the use of Emphasis of Matter (EOM) paragraph as stipulated in ISA 706 should continue and not be replaced by Auditor Commentary. Further reference is made to this in our response to Question 5.

Question 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.)

The use of professional judgment to determine what should be included in the "Auditor Commentary" section is too high level and evasive. In fact, as proposed, the criteria to make such determination are too vague. This could result in significant variations and thus consistency will be lost.

As explained above, FEE recommends that the matters reported are, in principle, based on the "significant risks" identified during the audit, in accordance with ISA 315.

In line with what is stated in ISA 315, "in exercising judgment as to which risks are significant risks, the auditor shall consider at least the following:

- Whether the risk is a risk of fraud;
- Whether the risk is related to recent significant economic, accounting or other developments and, therefore, requires specific attention;
- The complexity of transactions;
- Whether the risk involves significant transactions with related parties;
- The degree of subjectivity in the measurement of financial information related to the risk, especially those measurements involving a wide range of measurement uncertainty; and
- Whether the risk involves significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual.”

In addition, FEE would like to draw attention to some different practical ways to use this section. For instance:

- The auditor could consider whether to group together a number of significant risks, for instance if related to the same account balance or disclosure;
- Links may exist between operational risks of the entity and significant audit risks. However, many operational risks identified by management are not risks related to financial reporting;
- Where management does not disclose a significant audit risk, which the auditor considers should be referred to in the financial statements, qualification or abstention of the opinion of the auditor might come in to play and help convince management to make the necessary disclosures;
- Reporting on significant risks should be proportionate in nature, as they would be most relevant where a high level of transparency is requested by users.

There is also a need for principles-based criteria to govern what should be reported for each significant risk identified. We refer to our response to Question 5.

Question 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.)

As explained in our response to Question 4, FEE believes that there is a need to give principles-based criteria explaining how information shall be provided in the auditor’s report on the identified significant risks. For each significant risk, added-value comments should be given on:

- The **nature** of each significant risk;
- The **audit approach** undertaken in response to this significant risk; and
- The **key findings** from that audit work.

Where relevant to the information provided in the auditor’s report on each significant risk, a clear **reference to the related disclosure in the financial statements** should be provided. This reference should be made to help the users to link the point raised by the auditor to the disclosures, but, as said before, the aim is not at navigating the users through the financial statements.

The comments should also include:

- Whether any significant deficiencies in internal financial controls have been identified by management and/or the auditor and have been resolved (or not) and whether they have impacted the audit work performed;
- Whether fraud risks have been identified and the impact of those fraud risks on the audit approach.

Audit work based on ISAs already addresses potential fraud risks. Such risks exist in all entities, can never be removed completely, but can be mitigated by performing audit procedures that respond to the fraud risks identified. Although fraud risks are always significant risks from an ISA audit perspective², the fraud risks in a particular entity might turn out to be low. Therefore, there needs to be careful consideration on whether to include them within the auditor commentary section or not.

There is a risk that Auditor Commentary could cover areas that are not disclosed in the financial statements; for example, providing detail on the implementation of a new computer system as illustrated in the IAASB's 4th Auditor Commentary example. As previously stated, the auditor should not provide new information on the audited entity. That is the role of management. Linked to this, the IAASB is invited to consider the possibility for the auditor to not disclose a significant audit risk if such a disclosure could be harmful to the audited entity (for example where the risk is related to a matter which is highly sensitive from a business perspective) or for the audit (for example where the risk relates to management override or other suspected fraudulent activities). In such cases, it should be considered by the IAASB whether it is possible for the auditor to not disclose the matter to the public but only to the board of directors and/or the audit committee.

As previously explained, FEE believes that the use of an Emphasis of Matter (EOM) paragraph should continue to be used as provided for in ISA 706. That standard states that "the Emphasis of Matter paragraph is a paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgment, is of such importance that it is fundamental to users' understanding of the financial statements." To provide for all contingencies, it is essential that this information is separate from the significant risk paragraph. Both paragraphs could have a common denominator but it may not be the case for all audits: a matter appropriately presented in the financial statements, which needs to be highlighted in the EOM paragraph, could be deemed not to be a significant risk. Moreover, FEE believes that it is crucial that the paragraph on significant risks remains concentrated on the audit approach. Finally, the IAASB may consider providing guidance on avoiding duplicative reporting, e.g. where an EOM is considered needed in the auditor's report, but which has already been reported as a significant risk.

² See ISA 240 paragraph 27 and ISA 315 paragraph 28.

Having these developments in mind, FEE has the following comments on the Auditor Commentary examples provided:

- *Introduction paragraph*

As explained above, FEE believes that the auditor report relates first and foremost to the audit and should not be a means to navigate users through the financial statements, which we consider to be the responsibility of management of the audited company. Therefore, we recommend deletion of the part of the sentence “likely to be most important to users’ understanding of the audited financial statements” and only refer to the audit.

- *1st example: Outstanding Litigation*

According to our analysis, the explanation in this paragraph does not provide any insights into the audit procedures and work performed. Therefore, we are not convinced that this example should be included for consideration in an auditor’s report nor of the value it would have for users, apart from duplicating what is already included in the financial statements.

- *2nd example: Goodwill*

As explained above, we are not supportive of reproducing substantial parts of the information already included in the financial statements in the auditor’s report. We believe that the auditor’s report should relate to the audit performed. Therefore, we do not support inclusion of such examples in the auditor’s report.

- *3rd example: Valuation of Financial Instruments*

In response to the market needs and expectations of stakeholders for the auditor’s report, this example seems appropriate.

The first sentence links the commentary to the company’s disclosure in the financial statements. Subsequently, information relevant to the audit is included where the following is explained:

- A significant risk has been identified during the audit;
- The work performed during the course of the audit to mitigate the risk;
- The conclusion on this matter, in the context of the financial statements as a whole.

This would be in line with the criteria for reporting on significant audit risks as we have explained above in the first part of our response to Question 5.

- *4th example: Audit Strategy Relating to the Recording of Revenue, Accounts Receivable, and Cash Receipts*

If identified as such, this paragraph would be expected to be covered as a significant risk.

- *5th example: Involvement of Other Auditors*

FEE does not support this example as, in the European Union, divided responsibility and referring to other auditors in the auditor's report is not allowed as there is only sole responsibility for auditors. Furthermore, including references to other audit firms may confuse users as to the nature of the auditor's responsibility.

Question 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.)

The new requirements are expected to result in a cost increase for the additional time needed and potential delays in finalising the auditor's report with regard to the following areas:

- Drafting the additional information to be included in the auditor's report;
- Discussing these matters internally within the audit firm, including with the engagement quality control reviewer as required by International Standard on Quality Control (ISQC) 1; and
- Discussions with management.

Management is likely to spend additional time reviewing and discussing wording and presentation with the auditor.

Nevertheless, the audit profession agrees that the benefits generally outweigh the costs, and is ready to enhance the communication process. However, this step forward has to be done in an appropriate manner. Therefore, the profession would like the IAASB to consider the fact that Auditor Commentary would be much more appropriate in entities where there are external shareholders who lack access to information. In comparison, benefits to entities who are owner managed are less evident.

Question 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.)

The IAASB proposes to mandate the inclusion of Auditor Commentary in the auditor's reporting for PIEs only. FEE believes that this is a worthwhile proposal to start considering the scope for application. Indeed, when considering the inclusion of such reporting on significant audit risks, we should avoid putting disproportionate burdens on non-PIEs and SMEs. The applicability of this requirement should be proportionate to the nature, size and complexity of the entity. Non-PIEs and SMEs would have disproportionate costs attached to such mandatory requirements with low effect on users' confidence and market needs. Equally, it could be argued that auditors of less

complex entities would be likely to identify fewer significant audit risks compared to large complex entities.

However, FEE has the following concerns about the voluntary approach for non-PIEs and for leaving the inclusion of Auditor Commentary for non-PIEs to the discretion of the auditor:

- There is a potential risk for inconsistencies by mandating Auditor Commentary for PIEs only. This could generate reporting discrepancies between comparable companies in terms of sector, business, size and complexity with one being a PIE (and therefore having an Auditor Commentary in the audit report) and another one that is not a PIE (and therefore might not have an Auditor Commentary in the audit report).
- Additionally, as mentioned in Question 2, it is foremost a matter of definition. What does the concept of PIE include? For instance, FEE does not believe that the extended definition proposed by the EC to amend the Statutory Audit Directive (2006/43/EC) is the right way forward. Some entities added in this extended definition may in reality be low risk or low complexity entities with limited impact on the public interest. In terms of size, many are likely to be SMEs. As all those entities will fall within the scope of the Proposed EC Regulation regarding statutory audit of PIEs, they will face considerably increased costs with limited available infrastructure to handle their extended obligations.
- There are potential perception issues by not mandating Auditor Commentary for all companies. At the very least, users might be confused and unsure as to how to interpret the role of Auditor Commentary: does the inclusion of Auditor Commentary suggest the entity is “more problematic” than the company for which no Auditor Commentary is provided? Has the auditor “done a better job” in audits where Auditor Commentary is provided?
- There are also risks leaving Auditor Commentary inclusion to the discretion of the auditor: the arguments to convince the client to include such information will not be as strong as if it were mandatory. As alternatives, FEE has considered whether:
 - o The audit client could decide on its inclusion;
 - o National standard setters could decide on its inclusion;
 - o Criteria other than PIEs/non PIEs differentiation could be used;
 - o A proportionate application of Auditor Commentary, as is built into the ISAs, could be developed.

FEE thought about such alternatives, but was not convinced that any one was the optimal solution. The IAASB is invited to further consider alternative options, which can be satisfactory for all parties, and to come up with more criteria to improve the consistency of the proposals.

Going Concern/Other Information

Question 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.)

FEE supports improved auditor communication in line with market needs. Additional information in the auditor's report regarding the appropriateness of management's use of the going concern assumption seems strategically important to respond, at least in part, to issues arising from the financial and economic crisis. However, as explained below, care will need to be taken to ensure that the auditor's role in this area is clear, such that users' expectations are not misplaced.

Certain work linked to "going concern" is already performed during the audit assignment as ISA 570 requires the auditor to obtain sufficient appropriate audit evidence regarding the appropriateness of management's use of the going concern assumption in the preparation of the financial statements and to conclude, in this matter, whether a material uncertainty exists as identified during the audit.

The expectation gap between what users desire and what the auditor can do in relation to "going concern" has to be addressed by the IAASB. Some users may actually wish the auditors to "guarantee" the going concern status of the audited company. But this is an entirely unrealistic expectation, which cannot be achieved.

FEE emphasises the fact that the auditor's report should not and cannot be by itself an opinion on the going concern of the audited entity, but should be taken as a whole with the analysis performed by the entity's management in the financial statements: the auditor report paragraph on going concern should be based on the quantitative and qualitative information given in the disclosures of the financial statements by management. Disclosures made by management need enhancement. As previously mentioned, the accounting framework may need to be substantially improved to address this matter.

In this respect, FEE believes that status quo is no longer an option: there is an urgent need to reflect on expanding the accounting and financial reporting standards related to going concern reporting by the company. As of today, International Accounting Standards (IAS) 1 is the only Standard dealing with the going concern issue. This Standard imposes on management the responsibility to assess whether its company is/will be able to continue as a going concern in the foreseeable future. There is no requirement on the level of disclosure to be made by management. As explained in our response to Question 2, a comprehensive evaluation should be performed of financial reporting as a whole in order to have a holistic approach on such matters. This would include initiating discussions with the IASB.

We call for more disclosures by management. With the growing demand from investors for additional information on going concern assessments, entities should be required to provide more information on the assumptions and other information used to support management's assertion that the entity would be able to continue its activities in the foreseeable future, currently

considered as a period of at least one year. This is especially important in situations where there may be concerns about the impact of future events. Additionally, the information provided should in general be proportionate to the size and complexity of the entity.

Disclosures in the financial statements could be analysed in three categories:

- No going concern issue: only brief disclosures;
- Potential going concern issue: more extensive disclosures;
- Clear going concern issue: significantly more details to be provided.

Based on the assumption that management's level of disclosures in the financial statements on the going concern issue is appropriate, the information in the auditor's report on the going concern issue should also be proportionate as follows:

- In respect of PIEs, where there is no going concern issue, a brief paragraph in the auditor's report should explain that the management's use of going concern is appropriate. In respect of non-PIEs, FEE considers that no information should be included in the auditor's report.
- Where there is a potential going concern issue, management and the auditor are expected to have done a significant amount of work in this area. A brief paragraph in the auditor's report should explain that the management's use of going concern is appropriate. In addition, in the "Auditor Commentary" section, more detail should be provided in respect of the work undertaken by the auditor.
- Where there are uncertainties on going concern assumptions, management should be asked to give more extensive disclosures. In parallel, a more detailed paragraph in the auditor's report should provide more detail on the material uncertainties that exist. In addition, in the "Auditor Commentary" section, more detail should be provided in respect of the work undertaken by the auditor.

These comments do not deal with the situations whereby:

- The auditor would need to issue a qualified or disclaimer opinion in relation to management's use of the going concern assumption in the preparation of the financial statements; or
- Management has prepared the company's financial statements on a liquidation or on a break-up basis.

As a general comment, the examples of auditor's paragraphs on going concern presented in the ITC have to be reassessed. In our opinion, these examples do not sufficiently differentiate between the categories encountered by the auditor on going concern. If there is a going concern issue, it should be more visible to users.

Moreover, FEE does not fully support the wording "is not a guarantee" presented in the IAASB ITC example on Page 9. Indeed, "guarantee" could evoke an incorrect association by the public resulting in an increase of the expectation gap.

Finally, we would like to support the fact that the disclosure in the auditor's report should be as entity specific as possible.

Question 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.)

As already explained in our response to Question 1, auditors should not provide information that management should ordinarily be required to provide. In addition, as further detailed in our response to Question 8, current accounting and financial reporting standards are not explicit in relation to requiring companies to disclose matters in relation to going concern issues and related material uncertainties.

Therefore, management will often be reluctant to disclose material uncertainties, pleading lack of a requirement in law, regulation or standards to do so. This would result in the need for auditors to put pressure on management in order to have them disclose more information in relation to material uncertainties in the financial statements.

Therefore, it seems preferable that material uncertainties should only be reported on in the context of going concern issues, both by management in the financial statement and by the auditor in the auditor's report.

However, as the EC Proposed Regulation on statutory audit for PIEs requires such reporting in the auditor's report, stating that there are or there are no material uncertainties appears important. Such reporting in the auditor's report could be linked to reporting on significant audit risks, in circumstances where material uncertainty would qualify as a significant audit risk.

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

According to ISA 720, the auditor should read the other information to identify, if any, material inconsistencies with the audited financial statements. FEE believes that the requirements included in ISA 720 could be further extended, as explained below.

In order to make the auditor's report more informative and comprehensive, FEE supports adding a paragraph clarifying the work performed on specific other information.

For example, the auditor should report on the consistency of the management report with the financial statement for the same financial year and whether the management report has been prepared in accordance with the applicable legal requirements. In addition, the auditor should also state that, based on his knowledge and understanding of the entity and its environment obtained during the course of the audit, the management report as a whole suitably presents the company's position, the opportunities and principal risks and uncertainties of its likely future developments.

This would ensure that auditors:

- Not only perform a consistency check between the management report and the financial statements; but
- Also state whether the management report as a whole is suitable in the context of the auditor's knowledge and understanding of the company's business obtained during such audit.

Similar proposals are currently being considered by the European Parliament Legal Affairs (JURI) Committee.

FEE expects to have the opportunity to comment further on this matter when the revised ISA 720 Exposure Draft is issued. In this respect, we anticipate that the IAASB will wish to take account of the IAASB's conclusion from this ITC, as well as the new requirements of the updated EC Directive when issued.

Clarifications and Transparency

Question 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.)

The paragraph on responsibilities of each party could be shortened: this would guard the profession against the criticism of the auditor's report being too defensive and using boilerplate language. Additionally, we are not convinced that adding enhanced descriptions of the responsibilities of management, TCWG and the auditor would be able to address the expectation gap.

As a result, only the basic information that management is responsible for the financial statements, the related internal controls and the disclosures related to the going concern assumption would need mandating.

The auditor could use professional judgment to determine which information to include in the auditor report in relation to his or her responsibilities and what would be dealt with by reference to an official website of the national or international standard setter, audit firms, etc. As far as the auditor responsibilities are concerned, FEE is not supportive of expanding the description beyond what is currently required to be included in the auditor's report.

As far as the description of the auditor's responsibilities is concerned in the example auditor's report as included on page 11 in the ITC, we are not convinced that the use of the word 'always' in relation to the detection of material misstatements is appropriately chosen. Instead, we would propose to use the words 'detect with a high probability'.

In addition, in relation to the description of the management responsibilities, we recommend to keep all reference to going concern and responsibilities in relation to going concern together in one place.

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

FEE has not identified any impediments against disclosing the name of the engagement partner in the auditor's report. This is already required in the European Union (EU) under the Statutory Audit Directive of 2006 (2006/43/EC).

Question 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.)

As mandated by Article 27 (a) of the Statutory Audit Directive (2006/43/EC), in case of a statutory audit of the consolidated accounts of a group of undertakings, the group auditor bears the full responsibility for the auditor's report on the consolidated accounts. Therefore, such disclosure should not be included.

Question 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.)

Audit firms should have the option to decide how to communicate information related to such responsibilities. Some are supportive of replacing the inclusion of such information in the auditor's report by a brief reference to the relevant laws and regulations or by a reference to a website where such information is given in greater detail. FEE supports giving the auditor the opportunity to decide where he/she prefers supplying the information. Websites, either of national or of international standard setters, or of the audit firm itself, could be suitable options.

Form and structure

Question 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.)

FEE is supportive of giving the opinion more prominence.

Indeed, in recent debates, users have explicitly requested to maintain the “pass/fail” nature of the auditor’s report: as they previously explained, the main message they seek from an auditor’s report is the opinion of the auditor on whether or not the financial statements give, in all material aspects, a true and fair view in accordance with the applicable financial reporting framework.

In case significant risks are included in the auditor’s report, the IAASB should consider proposing that the audit opinion includes a reference to the reporting on significant audit risks in order to make users aware of their existence, similar to what is currently included when referring to an emphasis of matter paragraph.

Question 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.)

FEE recommends the IAASB to propose a principles-based structure (including the order and placement of the different section in the auditor’s report) for the auditor’s report which should be possible to apply in virtually all circumstances – an exception being where laws and/or regulation prescribe otherwise. An ISA compliant auditor’s report is requested by the profession, and would be a hallmark of the ISA-brand. It will avoid difference in interpretation across industries.

However, as the revisions to the auditor’s report now being proposed and considered tend towards having more entity-specific information included in the auditor’s report, they will differ anyway from one company to another. Moreover, local circumstances should also be considered. Therefore, far reaching content-wise consistency between auditor’s reports might not be achievable.

Question 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.)

Consistent with our response to Question 16 using a similar structure for all auditors’ reports, FEE fully supports global standardisation of the content order in the auditor’s report. We believe this would help to navigate users through the auditor’s report as well as helping to provide a comparison between auditor’s reports.

Question 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 already discussed beforehand in our response to Question 7 and Question 8, FEE's view on the appropriateness of the application of the auditor's reporting improvements are the following:

- Auditor Commentary should ordinarily not be mandatory for non-PIEs but considered as optional for them. However, FEE has concerns about the consistency of the proposal to leave the inclusion of Auditor Commentary entirely to the discretion of the auditor for non-PIEs. Further consideration should be given to the practical consequences of such proposal. FEE agrees that Auditor Commentary be mandatory in the auditor's report of PIEs while due consideration should be given to the definition of a PIE;
- A going concern paragraph should be applicable for all entities, reporting on the appropriateness of the use of going concern assumptions by management as well as on the relevant disclosures made by management;
- Other minor improvements (especially on the form of the report) as proposed in the IAASB ITC should be applicable for all entities;
- The EOM paragraph should remain subject to the auditor's professional judgment, as prescribed in ISA 706.

FEE does not support the inclusion of all public sector entities in the definition of PIEs. National authorities will have to determine the applicability of the proposals to the public sector so as to balance costs and benefits in responding to the true needs of users. Authorities may for example have regard to the proportion of the population for which an entity provides public services.

For public sector entities, FEE suggests that the IAASB should take the following into account in its standard-setting proposals:

- With regard to information on the use of going concern:
 - o The IAASB will be aware of the matters included in paragraph A1 of ISA 570 concerning the issue of the ability of public sector entities to continue as going concerns.
 - o Within the EU, financial reporting of public sector entities can be based on many different financial reporting frameworks; they vary from those on an accruals basis through to a simple cash basis. In many instances, assets and liabilities are not included in the financial statements.
 - o The proposals would have to accommodate those circumstances where the going concern assumption remains relevant when a cash, cash modified or accruals basis is used, and also circumstances where a change in the appropriateness of the going concern assumption would not affect some or all asset and liability valuations.

- With regard to Auditor Commentary:
 - o Reporting requirements can currently be different and/or more extensive for auditors of public sector entities. Auditors may report on compliance, legality or regulatory purposes, i.e. whether funds have been spent appropriately. Moreover, a significant amount of information that could be in Auditor Commentary is already in the communication by the auditor on public sector entities, but not necessarily in the auditor's report. For instance, reporting by the European Court of Auditors includes not only an ISA based auditor's report, but also much additional audit-relevant information in annexes.
 - o Nevertheless, Auditor Commentary including information on significant audit risks arising during the audit could be useful for users if framed taking these reporting differences into account.