Dear James

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 - Proposed Consequential and Conforming Amendments to Other ISAs”

Thank you for the opportunity to comment on the IAASB’s ISA 720 proposals.

Our responses to the specific questions raised by the IAASB in their Invitation to Comment are included in the Appendix. Our main comments are summarised below:

- Whilst we may accept that strengthening the auditor’s responsibilities with regard to other information is a good idea in the light of recent developments in corporate reporting we question where the “need” for change in this area is coming from and the benefits that might arise when compared to the increase in auditor costs and the pressure put on clients to provide the other information at an earlier stage. We also question whether ISA 720 is the right place to deal with the challenges that this proliferation of other information places on an auditor and recommend that the IAASB considers whether this might be better met by an ISAE 3000 assurance engagement rather than as part of an audit engagement.

- We disagree with the definition of “inconsistency” used in the IAASB exposure draft and believe the inclusion of inaccuracies and omissions or information that is unreasonable, inappropiate or obscures something else, extends the term ‘inconsistency’ far beyond its accepted meaning and would require a significant increase in auditor workload and associated costs. In our view, the phrase “in light of the auditor’s understanding of the entity and its environment acquired during the audit” is too widely construed and it is impracticable for the auditor to consider inconsistencies between a narrow clearly defined set of other information accompanying the financial statements and the far wider auditor’s understanding of the entity and its environment however that may be understood.
- We do not find the concept of "initial release" clear and understandable in a UK context where the date of an auditor's report on a reporting entity's financial statements is regarded as the date on which the auditor signed the report expressing an opinion on those financial statements.

Please contact me should you wish to discuss any of the points raised in this response.

Yours sincerely

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Appendix

Response to specific questions asked by the IAASB

1. Do respondents agree that there is a need to strengthen the auditor’s responsibilities with respect to other information?

NO

Whilst we may accept that strengthening the auditor’s responsibilities with regard to other information is a good idea in the light of recent developments in corporate reporting we question where the “need” for change in this area is coming from. ISA 720 was recently subject to the clarification process and it was not felt necessary at the time to revise the ISA despite many of the same issues with other information existing at that time. In our opinion, ISA 720 was not a “broken” standard and whilst improvements can always be made we do not see that that there is a great demand for IAASB to “fix it”.

We accept that developments in financial reporting and in particular changes to the other information that is now issued with audited financial statements mean that the auditor’s traditional “read” responsibility articulated in ISA 720 is not designed to meet the challenges faced when presented with a modern set of listed company financial statements where, not only does the quantity of the other information far outweigh the audited financial information but, in many cases, the other information contains information that is far more qualitative, complex and judgemental than the audited information in the financial statements. We question whether ISA 720 is the right place to deal with the challenges that this proliferation of other information places on an auditor.

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?

NO

Whilst we recognise that auditors’ responsibilities with regard to other information are important in practice to prevent inappropriate information being associated with and undermining audited financial statements. We do not believe that the changes proposed in the IAASB exposure draft which effectively just increase the amount of work that the auditor is expected to do by widening the definition of “inconsistency” to include incorrect, unreasonable and inappropriate and asking the auditor to consider the other information “in light of the auditor’s understanding of the entity and its environment” are appropriate. As noted above we question whether there really is a “need” for these changes and before progressing any further we suggest that the IAASB performs a cost benefit analysis on the proposed changes.

The IAASB should not underestimate the impact of these proposed changes on audit costs, or on the expectation gap.

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In our opinion, the proposed changes will require a substantial increase in the work that an auditor will be expected to undertake to meet the new requirements. The reasons for this are as follows:

- Auditor’s understanding of the entity and its environment – in our opinion, the requirement in paragraph 10(a) for the auditor to “read and consider the other information in light of the auditor’s understanding of the entity and its environment acquired during the course of the audit” is very open ended and almost impossible to comply with.

Even if this requirement is interpreted very narrowly and it is assumed that the auditor’s understanding of the entity and its environment are documented on the audit file this ignores the fact that the electronic audit files used in today’s audit contain far more information than it is possible for one auditor to have reviewed and understood and there may well be points buried in the detail of files which are inconsistent with the other information but it would be unreasonable for the auditor performing the review of the other information to know this.

If it is accepted that an auditor’s understanding of the entity and its environment goes wider than that which has merely been documented on the audit file, then this could be interpreted as the collective knowledge of the whole audit team, office or even the entire audit firm. Typically, a review of the other information will be performed at partner and manager level with detailed ticking of numbers left to a more junior member of staff. It would be impracticable for the whole audit team to review the other information in the light of their own personal understanding and it would be virtually impossible to get any meaningful review done on an office or firm-wide basis.

- Definition of “inconsistency” – as noted in our detailed response to question 6 below, the revised IAASB definition of “inconsistency” now includes inaccuracies and omissions or information that is unreasonable, inappropriate or obscures something else. In our opinion, this extends the term ‘inconsistency’ far beyond the extant meaning of “other information that contradicts information contained in the audited financial statements” (Extant ISA 720.5(b) and would inevitably end up with a large increase in the amount of audit work necessary to comply with these additional requirements.

- Composition of other information – as noted above, in recent years there has been a proliferation of other information far in excess of the traditional director’s report and now other information, although ostensibly tied to the financial statements, in practice includes increasingly specialised technical documents that cover areas outside those that the auditor would be expected to consider during the course of their audit work. While auditors do already look at these documents as part of their reading of the other information and whilst many of the procedures suggested in these proposals are already being applied, we believe that including this as requirements in the ISA will create an expectation gap in the level of technical expertise that auditors will be expected to apply to the other
information and it will be impossible for auditors to meet this expectation without a great increase in the audit costs incurred.

- Timing of other information – in our view the increase in the work that the auditors are expected to perform on the other information will inevitably mean that auditors will require this other information to be provided to them at an earlier stage of the audit to give them sufficient time to complete their procedures. Currently, other information is typically provided to the auditors at a late stage of the completion of the audit of the financial statements but this will have to change if auditors are expected to do more work on it. If IAASB intends to increase the scope of the auditors work in this area they should consult with companies to gain their agreement to an accelerated timetable for the provision of other information.

It is important that IAASB does not create unrealistic expectations about what auditors can reasonably be expected to do with other information as part of the audit of the financial statements. In our opinion, extending the definition of “inconsistency” and asking auditors to “read and consider the other information in light of the auditor’s understanding of the entity and its environment” has created an unrealistic expectation particularly when it is considered against the growth in the other information that is now typically provided.

We question whether there is a “need” for the changes to ISA 720 and strongly recommend that the IAASB conduct a cost benefit exercise to determine whether change is required. If users of the other information really do need auditor’s to provide assurance on the completeness, accuracy and reliability of other information, not assurance on its consistency with the audited financial statements, then we would recommend that the IAASB considers whether this might be better met by an ISAE 3000 assurance report rather than an ISA 700 auditor’s report. In our opinion, much of the other information that is now included in an annual report is not, and probably never has been issued to support, enhance or supplement the audited financial statements. Other information often stands on its own and can be read independently of the information in the audited financial statements and therefore could be reported on separately to the financial statements. This would help to manage the audit expectation gap and yet still provide users with the assurance it is perceived they “need”.

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?

YES

We agree that broadening the scope of the proposed ISA to include documents that accompany the audited financial statements and the auditors’ report thereon is appropriate. We do not envisage this to cause problems for UK auditors where the contents of an annual report and the division between the audited financial statements

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and other information is clearly defined and auditors already read the other information that accompanies the audited financial statements.

However, we recommend that the IAASB clearly define what is meant by “documents that accompany the audited financial statements” because this is a potentially grey area where differing practices abound. It is important that the exclusions in paragraph 3 of the ISA clearly define the accompanying information that the ISA does not apply to. Companies increasingly provide electronic information with, and directly relevant to, audited financial statements, which can range from PowerPoint presentations, video clips, webinars and other forms of communication that are not strictly “documents” in the accepted sense. As a minimum we believe that the exclusion in paragraph 3 should be widened to include any such electronic information and any information associated with preliminary announcements, such as information provided at analysts briefings.

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?

NO

We do not find the concept of “initial release” clear and understandable in a UK context where the date of an auditor’s report on a reporting entity’s financial statements is regarded as the date on which the auditor signed the report expressing an opinion on those financial statements (ISA (UK&I) 700.23). In the UK the auditor will only sign the auditor’s report when all other information contained in a report of which the audited financial statements form a part has been approved by those charged with governance and the auditor has considered all necessary available evidence.

Paragraph A4 of the exposure draft identifies a situation where in the case of a private entity, the audited financial statements and the auditor’s report thereon are first issued to the entity’s bank, in accordance with a contractual provision and then later released to the shareholders with the annual report. In this case the exposure draft states that the initial release occurs on the date of the release to the shareholders not when it is first issued to the bank. In our opinion this does not work in a UK context where the bank would not have been issued with an auditor’s report unless the auditor had completed their audit work, including the ISA 720 work on the other information, and signed their opinion.

The closest we can envisage to the IAASB concept of an initial release is a UK preliminary announcement which is a means by which a listed company results are released to the market in a controlled manner prior to the full annual report being sent to shareholders and in some cases prior to the date the auditor’s report is signed. In the UK where a preliminary announcement is made of “audited” results this is usually dated the same date that the auditor signs the opinion on the financial statement and requires that the auditor completed their audit of the financial statements including the ISA 720 work on the other information issued with those

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financial statements. In contrast a preliminary announcement of “unaudited” results contains no such audit assurance and takes place prior to the date that the auditor signs the audit opinion on the financial statements and could very well be at a stage when the other information is not available for review. In this case we could accept that the date of an unaudited preliminary announcement of the company’s results may be earlier than the date the financial statements are issued as defined in ISA 560.

In our view, where the IAASB’s “initial release” contains an auditor’s report it is more akin to a UK “audited” preliminary announcement and should follow the same controls that the FRC introduced in Bulletin 2008/2 which would require the auditor to have completed their work on the other information. Whilst this is manageable in the UK where other information is provided prior to the signature of the auditor’s report this may not work in other jurisdictions where there is no such requirement.

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?

NO

In our opinion, because securities offerings are subject to extensive and detailed regulations of their own which vary between jurisdictions, they should be scoped out of the requirements of ISA 720.

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?

NO

We do not believe that the phrase “in light of the auditor’s understanding of the entity and its environment acquired during the audit” is understandable for an auditor. In our view, the auditor’s understanding of the entity and its environment is too widely construed and could in practice incorporate the auditors’ knowledge of the industry within which the entity operates, the economic environment, events going on in other
parts of the world that may impact the client as well as knowledge gained from prior audits and in other parts of the auditing firm not just the engagement team.

We do not believe that the IAASB can seek to limit this by adding “acquired during the course of the audit” because the expectation will be that the results of prior year’s audits and knowledge and experience gained outside the narrow confines of the audit will be considered. In our view it is impracticable for the auditor to search for inconsistencies between the narrow set of other information accompanying the financial statements and the far wider auditor’s understanding of the entity and its environment.

(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?

NO

We do not believe the objective is clear that the auditor’s responsibilities include reading and considering the other information for consistency with the audited financial statements. Paragraph 8 states that the objectives of the auditor, having read and considered the other information, is to respond appropriately when, in light of the auditor’s understanding of the entity and its environment acquired during the course of the audit, the auditor identifies that there may be a material inconsistency in the other information. As stated above, this can be interpreted very widely and does not refer to the much narrower requirement to consider whether the other information is consistent 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”?

NO

We do not believe that the IAASB’s use of the term “inconsistency” is in accordance with what is the commonly accepted use of the term when comparing two or more clearly defined and discrete items, for example the other information and the audited financial statements. The Oxford English dictionary defines consistent as “compatible or in agreement with something” and gives as an example “the injuries are consistent with falling from a great height”. This is not in accordance with the IAASB’s definition of “inconsistency”.

In paragraph 9(a) of the draft ISA and page 20 of the consultation document the IAASB has tried to introduce into the definition of “inconsistency” the terms “incorrect”, “unreasonable”, inappropriate” and “omits or obscures” and we do not believe that this is appropriate. The terms “incorrect”, “unreasonable” “inappropriate” and “omits” or “obscures” are absolute concepts that can be taken in isolation whereas the term “inconsistency” is by definition a relative concept that involves a comparison between two or more things. Whilst the IAASB may see the

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merit in extending the scope of the auditor’s work on other information by the use of these terms we believe that it is a considerable “raising of the bar” and in our opinion the work effort required by the auditor to report in these terms far exceeds any benefit that might be gained.

It is difficult to see the justification for asking the auditor to consider whether the other information was “incorrect” when the responsibility for the financial statements is limited to “true and fair”. Similarly unless clearly grounded in the financial statements requiring the auditor to consider whether the other information is “unreasonable” or “inappropriate” requires a level of judgement that far exceeds the previous requirement to consider a much more narrow definition of inconsistency.

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?

NO

As stated above in our response to question 6, we do not believe that the IAASB’s use of the term “inconsistency” is in accordance with what is the commonly accepted use of the term when comparing two or more clearly defined and discrete items. As a result, we do not consider that users of auditors’ reports will understand that an inconsistency relates to an inaccuracy in the other information as described in the definition.

Furthermore, we do not believe that users will understand that it is based on reading and considering the other information in light of the auditors’ understanding of the entity and its environment acquired during the course of the audit. The illustrative wording for the auditor’s opinion include the sentence “We have not identified material inconsistencies in the Other Information” which implies that the inconsistencies are between different items of other information, rather than between the other information and the auditors’ knowledge of the entity and its environment.

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?

YES
We believe that a principles-based approach for determining the extent of work the auditor is expected to undertake when reading and considering the other information is appropriate.

(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?

NO

Whilst we believe that the procedures in paragraphs A37(a), (b) and (c) for quantitative financial information that is intended to be the same as information in the audited financial statements, qualitative financial information intended to convey the same meaning as qualitative disclosures in the audited financial statements, and directly reconcilable financial information represent a codification of what is currently performed in practice we do not agree with the procedures included in paragraph A37(d) for the remaining other information.

We are concerned that considering the remaining other information, whether financial or non-financial, relative to the auditor’s understanding of the entity and its environment acquired during the course of the audit is a significant extension of the auditor’s responsibilities and the scope of the audit. We recommend that the procedures relating to the “remaining other information” in paragraph A37 should be limited to reading the other information and dealing with any apparent inconsistencies with the audited financial statements if they come to the auditors’ attention.

(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?

NO

As stated in our response to previous questions we believe that the exposure draft does increase the scope of the audit and will require the auditor to undertake a considerable amount of additional work.

We have suggested that if there is a need for additional assurance in this area then it may be better served by a separate ISAE 3000 type engagement rather than by trying to add to what were the very straightforward and understandable requirements of ISA 720.

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

YES
We believe that the examples of qualitative and quantitative information included in the Appendix in the proposed ISA are helpful.

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?

YES

The proposed requirements are clear regarding the auditors’ response if it becomes apparent that the auditors’ prior understanding was incorrect or incomplete.

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?

NO

As stated above in our response to question 7 above we do not believe that the terminology 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.

(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?

NO

We do not believe that including a statement that “the auditor has not audited or reviewed the other information and accordingly does not express an audit opinion or a review conclusion on it” properly conveys that no assurance is being expressed on the other information.

In our opinion, this statement conflicts with the requirement in paragraph 16(c) of the exposure draft for the auditor to include a statement whether the auditor has identified material inconsistencies and, if so, a statement describing them. The illustrative wording in paragraph A57 of the exposure draft states that “We have not identified material inconsistencies in the Other Information” and it is clear that some assurance is being given albeit only negative 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

We do not believe that the level of assurance being provided with respect to other information is appropriate.

As stated in our response to question 1 above in our opinion the changes proposed in the exposure draft will require a considerable increase in the amount of work performed by the auditor over and above that required to audit the financial statements. As stated above the increased work effort and assurance given may be better suited to a separate limited assurance engagement and we recommend that the IAASB consider developing such an engagement based on ISAE 3000.