

CHARLES A. MCDONOUGH  
Vice President and Controller

October 5, 2012

Prof. Arnold Schilder  
Chairman  
International Auditing and Assurance Standards Board (IAASB)  
529 Fifth Avenue, 6<sup>th</sup> floor  
New York, NY 10017

Dear Arnold:

***Re: Comments on "Improving the Auditor's Report"***

The World Bank welcomes the opportunity to comment on the IAASB's proposals to improve the independent auditor's report. Rather than answering each of the 18 individual questions in the Invitation to Comment (ITC), for the sake of conciseness and because we do not feel able to provide a meaningful answer for all of them, we will focus our comments on a few major areas which in substance address the key issues raised in the ITC. Whenever applicable, we mention the specific question(s) to which our comments relate.

We commend the IAASB for the leadership it has shown in initiating this important project, and for setting forth a broad range of ideas and concrete proposals to improve the auditor reporting. In our view, the ITC makes a compelling case for improving auditor reporting and revising ISA 700, and we are confident that it will foster a meaningful discussion which in turn will lead to a better audit reporting model.

At the same time, we are not fully convinced that the proposals contained in the ITC would bring about a significant enhancement of the audit report's informational or decision-making usefulness. Specifically:

As regards the new section on Going Concern Information (Questions 1, 8 and 9):

- Including a conclusion on the appropriateness of the going concern assumption would simply confirm what is already implicit in the current format of the auditor's report; and
- The additional statement mentioning the existence of material uncertainty on the entity's ability to continue as a going concern (or the lack thereof) would be already included as an emphasis-of-matter paragraph in the current auditor's report.

As regards the new Auditor Commentary (Questions 1, 3 and 5):

- First, as the ITC acknowledges, the information provided would, to a large extent, be similar in nature to the one currently included in an emphasis-of-matter paragraph, albeit in an expanded form; and we are not convinced that the wording “likely to be the most important” (as opposed to the current “fundamental to users”) would in effect amount to a lower threshold.
- Second, it is unclear to us whether the readers of the financial statements would be able to interpret meaningfully and accurately the additional information describing the way the auditor has addressed identified risks of material misstatement. We are of the view that a minimum of competence in the field of auditing would be required on the part of readers, and we do not believe that shareholders and other financial statement users possess such competence.

Instead, we suggest that such information could be conveyed to an audit committee or other bodies charged with the reporting entity’s governance (see below). It would be useful, as part of the continued outreach envisaged before the issuance of an exposure draft as noted on Page 2, to analyze further the experience of jurisdictions who introduced similar arrangements, including France as noted in paragraph 59.

Conversely, we see two potential risks in the proposed approach for an expanded audit report (Questions 6 and 10):

- (i) We are concerned that the Auditor Commentary and Going Concern Information could lead to excessive disclosure and that the auditor’s report evolve into a “boiler-plate” document, which would create an additional burden for auditors, TCWG and financial statements users, without genuine corresponding benefits. In some jurisdictions, especially developing economies, we see a risk of high variability in the quality of such Commentaries or Information; this would most likely require audit professional bodies to develop additional technical guidance for auditors.
- (ii) We also fear that the inclusion of detailed information on the financial statements in the audit report might blur the boundaries between the roles of preparers and auditors, thereby compounding one of the key challenges for the audit profession at present. We believe that management’s responsibility to provide appropriate and sufficient information in the financial statements, and the independent auditor’s role to provide assurance in that respect, should continue to be affirmed.

An alternative, and in our view more effective, approach to improving auditor reporting would focus on the auditor's communication with the audit committee or other bodies charged with governance ("TCWG"). Indeed, the "private" nature of the communication between auditors and TCWG creates a more appropriate environment for a discussion on sensitive issues relating to the use of professional judgment and key uncertainties affecting the financial statements. Moreover, TCWG include persons with sufficient "audit literacy" and competence in the area of corporate financial reporting who thus represent a more suitable audience for such discussions involving complex issues.

We do recognize that users of financial statements have expressed the need to receive more information about the work of auditors and the basis upon which they draw their conclusions on the financial statements. We see two possible important steps to address these needs:

- First, we understand that users would like to understand more about the risks inherent in the business and gain insights on the independent auditors' perspective as to where key risks reside in the financial statement information. To that end, we would encourage the audit community to work closely with the accounting standard-setters in order to develop proposals to provide this information.
- Second, TCWG could be required to provide assurances in their own report to the effect that they have gained a proper understanding of the work of auditors and the basis upon which they have developed their conclusions.

Furthermore, we welcome the ongoing efforts to (a) reduce excessive disclosure in the financial statements and eliminate the unnecessary information that dilutes the quality of the financial reporting and (b) enhance risk disclosures in areas such as financial instruments and contingencies. In parallel, we encourage a continued emphasis on investor education in order to foster a better understanding—and use—of financial statements, especially the explanatory notes. The IASB, IFRS Foundation and national accounting standard-setters will continue to play a critical role in that respect.

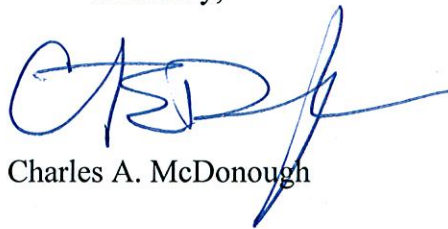
Lastly, on the other questions in the ITC:

- We see great merit in disclosing the name of the engagement partner (Question 12), given the critical role that individual plays in the direction of the audit and in the formulation of its conclusions, and as a matter of transparency. To address the concern regarding a possible perception of dilution of the audit firm's responsibility, an approach could be to include appropriate language in the report affirming that the ultimate responsibility for the conduct of the audit lies with the audit firm.
- We do not believe that adding information on the work of other auditors would be of value to the users of the financial statements (Question 13). We see in fact a risk of confusion and dilution of the responsibility of the group auditor which is clearly stated in ISA 600. Again, we are of the view that matters relating to the group auditors' reliance on the work of others are best left to a discussion between the auditors and TCWG.

- We are generally supportive of the proposed changes to the structure of the report (Question 15), especially the reordering of paragraphs to present the audit opinion at the beginning of the report.

We hope these inputs will be useful to the IAASB and look forward to contributing further to this important project.

Sincerely,

A handwritten signature in blue ink, appearing to read 'C.A. McDonough', with a long horizontal flourish extending to the right.

Charles A. McDonough