

July 17, 2014

Technical Director
International Auditing and Assurance Standards Board (IAASB)
529 5th Avenue 6th Floor
New York, New York 10017
USA

Dear Sir,

Re: Re-Exposure Draft – The Auditor’s Responsibility Relating to Other Information – Proposed International Standard on Auditing 720 (Revised)

Thank you for the opportunity to comment on the Re-Exposure Draft (“ED”). We have reviewed the ED and have provided our responses to the questions provided.

Overall, we are supportive of the efforts by the IAASB to clarify the auditor’s involvement with other information in annual reports, given the weight that users place on this other information. We believe that the re-exposure draft has addressed some significant concerns raised in response to the 2012 ED, particularly the restriction of the scope to information included in an entity’s annual report.

However, we remain concerned about the confusion that will be created by including in the auditor’s report on financial statements, references about disclosure that is not reported in the financial statements and that is not audited. We also do not believe that the proposals address the practical limitations that the auditor’s understanding of the business may be insufficient to facilitate effective or efficient review of information that may be forward-looking in nature or include technical disclosure for resource based issuers (i.e. involving engineering or geological expertise). In addition, the process to evaluate qualitative disclosure about management’s view of the business involves a significant degree of judgment. In some cases, it may be extremely difficult to conclude whether the disclosure is materially inconsistent with the auditor’s knowledge obtained during the course of the audit.

Our detailed responses to the specific questions are as follows:

- 1. Whether, in your view, the stated objectives, the scope and definitions, and the requirements addressing the auditor’s work effort (together with related introductory, application and other explanatory material) in the proposed ISA adequately describe and set forth appropriate responsibilities for the auditor in relation to other information.**

We believe that defining the scope of other information by reference to information included in an entity’s “annual report” significantly simplifies the auditor’s reporting obligations. The objectives set out in the ED adequately describe the requirements and responsibilities of the auditor in relation to other information; however, we have identified certain aspects of the scope, definitions and the requirements addressing the auditor’s work effort, that require further clarification. These are noted below.

Scope and definitions

Although the objectives in the proposed ISA are clear, we believe that these may be difficult to achieve in practice. Annual reports released in conjunction with the financial statements allow management to promote the affairs of the entity to current and potential investors by discussing historical results and current, as well as future, business prospects. The annual report includes technical, non-financial information as well as information that is

qualitative and forward-looking in nature. The process to evaluate qualitative disclosures about management's view of the business involves a significant degree of judgment and, in some cases, it may be extremely difficult to conclude whether the disclosure is materially inconsistent with the auditor's knowledge obtained during the course of the audit.

We understand that the intention of the proposed ISA is to "raise the bar" but the proposed auditor's responsibilities would extend to include many areas that fall outside the auditor's expertise. An auditor may obtain a broad but basic understanding of the business sufficient to complete the financial statement audit. However, this understanding is significantly less than the depth of knowledge possessed by management that is required to run the business and, in particular, to identify material inconsistencies on matters for which the auditor is not an expert.

Work effort

There is insufficient guidance regarding the procedures to be performed with respect to the other information, particularly where this relates to prospective or forward-looking information. The definition of an annual report per the ED notes that it usually contains "information about the entity's developments, its future outlook and risks and uncertainties." The ED (in the appendix) further suggests that the type of items that may be included in other information extends to the business outlook, market trends and other economic factors. However, the guidance in the ED does not specify the procedures to be performed on such information and states that this is a matter of professional judgment and, in certain cases, solely based on the auditor's recollection.

Financial statement users and preparers of the annual report will have to bear the costs of these procedures that could vary from entity to entity, while the end result is that no assurance is expressed with regards to the other information in the auditor's report. We recommend that the IAASB considers providing more specific guidance regarding the procedures to be performed in order to identify material inconsistencies, particularly where this relates to non-financial information. We also recommend that the IAASB consider whether such specific guidance could form the basis of a review or agreed-upon procedures opinion so as to provide entities and users of their financial statements with a report that is more commensurate with the additional work effort and cost that will be required to review the other information.

2. Whether, in your view, the proposals in the ISA are capable of being consistently interpreted and applied.

We believe that the proposals relating to the requirement to consider whether there is a material inconsistency between the other information and the financial statements is capable of being consistently interpreted and applied. However, we believe that the requirement to consider whether there is a material inconsistency between the other information and the auditor's knowledge obtained during the course of the audit, specifically where this relates to non-financial information, will result in inconsistent interpretation and application.

In evaluating qualitative disclosures, a wide range of subjective interpretations may exist based on examining the reporting issuer's choice of words and it may be difficult for the auditor to conclude on what is considered outside the realm of acceptability in all but the most extreme cases. We provide the example below to illustrate our concerns.

Entity X has developed a new product (product A) and tested it with 50 potential customers, 30 of the customers had positive feedback and 5 had neutral feedback and the remaining customers did not provide any feedback. Management did not follow up to find out why the remaining customers did not respond. Entity X is a development stage corporation and all of its products are in various stages of testing. Compared to the entity's other products,

A is in the most advanced stage of testing. Entity X does not yet generate revenue.

Management considers making the following statements in their annual report: “After the preliminary testing phase, management is excited about product A and its future potential” and “preliminary market tests indicate that customer feedback is positive for product A”.

Management does not wish to disclose the number of customers tested or the detailed test results due to proprietary concerns and there is no industry standard to suggest whether a test sample of 50 customers is an appropriate sample size. A is a new product and there are no comparable products that exist in the marketplace. The auditor performed very limited reviews of the product A customer market tests because the customer test results do not directly affect any amounts reported in the annual financial statements (i.e. all costs are expensed, there are no capitalized development assets and associated impairment testing). In this example, it would be very difficult for the auditor to evaluate if either of the two statements in the annual report are materially inconsistent with both the financial statements and the auditor’s knowledge obtained during the course of the audit.

As noted under question 1, we recommend that more specific guidance be provided regarding the procedures to be performed with respect to identifying material inconsistencies between other information and the auditor’s knowledge obtained during the course of the audit, as well as identifying material inconsistencies in non-financial information.

3. Whether, in your view, the proposed auditor reporting requirements result in effective communication to users about the auditor’s work relating to other information.

The proposed wording for reporting on other information is clear in conveying that the other information is not audited and that no opinion is expressed thereon. However, the proposed wording that describes the auditor’s procedures as having “read” the other information and “considered” whether there are material inconsistencies does not effectively communicate what work the auditor actually performed with respect to other information. While it is easier to infer the type of procedures performed to identify material inconsistencies between other information and the financial statements, this is more challenging with respect to non-financial information and inconsistencies with the auditor’s knowledge obtained during the course of the audit. Furthermore, the application and other explanatory material notes that “remaining alert for other indications” of material inconsistency implies that this may extend beyond the auditor’s knowledge obtained during the course of the audit. This will not be clear to users, based on the proposed wording of the auditor’s report.

The statement that “we have nothing to report” will create the perception of providing negative assurance. The proposed ISA is clearly requiring the auditor to perform certain procedures to identify material inconsistencies, which will require time and effort. As noted under question 1, financial statement users and preparers of the annual report will have to bear the costs of these procedures that could vary from entity to entity, while the end result is that no assurance is expressed with regards to the other information in the auditor’s report and users will still remain unclear as to what work the auditor has actually performed.

4. Whether you agree with the IAASB's conclusion to require the auditor to read and consider other information only obtained after the date of the auditor's report, but not to require identification of such other information in the auditor's report or subsequent reporting on such other information.

The proposed ISA will result in two types of auditor's reports. If the final version of the other information is obtained before the auditor's report date, the auditor's report will include a reference to the "other information." If the final version of the other information is obtained after the auditor's report date, the auditor's report will not address the "other information" (as per paragraph A47 of the proposed ISA).

This might create confusion to the users of the financial statements when they see two different types of auditor's reports as it is unlikely that they are familiar with all the requirements of ISA 720. When they see an auditor's report with the "other information" section, they might assume that procedures have been performed with respect to the other information and that no such procedures have been performed on other information when the auditor's report does not include such a reference. This may also create the perception that the quality of the audit where "other information" is referred to in the auditor's report is superior to an audit that does not include such reference in its report, or that audits are not performed consistently.

While the above scenario is far from ideal, we understand that mandating the re-issuance or amendment of the auditor's report may result in conflicts with local law and regulations and we also recognise that the auditor cannot refer to future actions in the auditor's report. Therefore, although we do not agree with the conclusion to not require identification of such other information in the auditor's report or subsequent reporting on such other information in principle, there does not seem to be a practical alternative.

MNP LLP is one of Canada's largest chartered accountancy and business advisory firms. Our clients include small to mid-size owner-managed businesses in agriculture, agribusiness, retail and manufacturing as well as credit unions, co-operatives, First Nations (i.e., Aboriginal peoples in Canada), medical and legal professionals, not-for-profit organizations, municipalities and government entities. In addition, our client base includes a sizable contingent of entities that are publicly traded in Canada and internationally, and which operate in all industries and sectors.

We are pleased to offer our assistance to the IAASB in further exploring issues raised in our response, in finding solutions to meet the needs of financial statement users.

Yours truly,

MNP LLP

Jody MacKenzie

Jody MacKenzie, CA
Director, Assurance Professional Standards

cc: AASB, Canada