



Organización Internacional de Comisiones de Valores
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May 3, 2004

Mr. James Sylph
Technical Director
International Auditing and Assurance Standards Board
545 Fifth Avenue, 14th Floor
New York, NY 10017

Re: Proposed Revised International Standard on Auditing 700 (Revised), "The Independent Auditor's Report on a Complete Set of General Purpose Financial Statements", also Amendment to ISA 200, "Objective and General Principles Governing an Audit of Financial Statements", ISA 210, "Terms of Audit Engagements" and Conforming Amendments

Dear Mr. Sylph:

IOSCO's Standing Committee No. 1 on Multinational Disclosure and Accounting is writing to comment on the Exposure Draft ("ED"), "The Auditor's Report on a Complete Set of General Purpose Financial Statements" and the other proposed changes noted above.

We appreciate the opportunity to comment on this proposed standard and provide our perspectives as securities regulators charged with protecting the interests of investors in the global capital markets.

IOSCO is committed to promoting the integrity of international markets through promotion of high quality accounting, auditing, and professional standards. This letter provides comments on which we have achieved a consensus among members of Standing Committee No. 1 and is not intended to include all the comments that might be provided by individual members on behalf of their respective jurisdictions in the future.

Phased Approach for Addressing Auditor Reports Issues

We understand that the Board is seeking to address the overall subject of auditor's reports in a series of steps or phases, beginning with the issuance of an ED addressing only the unmodified auditor's opinion. We further understand that the goals in this project include providing more clarity to investors regarding the audit and working toward making audit reports more similar and more understandable around the world. These are appropriate and useful objectives. We also understand that the Board is seeking to develop and issue updated

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guidance as promptly as possible, in order to respond to the desire to provide coverage of a common form of auditor report in ISAs for anticipated use in the European Union in 2005.

We understand the rationale for using a phased approach to provide guidance on the most frequent report condition as quickly as possible. The tradeoff, however, is that it is difficult to anticipate how a later IAASB project on modified reports might affect the decisions made in this first ED. In principle, we would not object to a phased approach if the remaining work on other aspects of auditor's reports is done promptly and further changes that may need to be made to this ISA as a result of that work are appropriately coordinated. However, we are aware that the work proposed for ISA 701 already has introduced the possibility that coverage of "emphasis of matter" conditions, while deliberated in the later project, will be inserted into ISA 700 after its issuance as conforming changes.

We believe that significant changes to ISAs should not be handled as conforming changes. We therefore urge the Board to consider whether the project on ISA 700 should be extended to take into account impacts from the project to develop proposed ISA 701.

In addition to the expected impact of ISA 701, we are aware that evolving national requirements already have touched on matters that need to be addressed in auditor reports in some jurisdictions in North America and Europe. Other jurisdictions also may have changes that have been made recently or are currently under consideration. We believe the IAASB should take stock of these recent developments and ascertain the impact on the current projects on Auditor Reports, both ISA 700 and 701.

Clarity of the Standard

We have written you a number of times expressing concern regarding the need to clarify the requirements in ISAs. Required actions of the auditor are now expressed in ISAs through a combination of bold and gray lettering and use of drafting conventions, but we are concerned that the existing approaches are not consistently understood by auditors and others who use the standards. We have observed differences in interpretation of the present formats and conventions even among members of the IAASB in Board meeting discussions. It is also not always clear to us what is intended to be the requirement in a standard. For these and other reasons, we urge the Board to address the clarity of standards issue as a matter of priority.

The Auditor's Responsibilities

We support a requirement for a clear statement of the auditor's responsibilities in the audit report; however, we are not sure that the language suggested or required in this proposed standard will accomplish this. We note the introduction of a new phrase "reasonable but not absolute assurance" to replace the previous phrase "reasonable assurance". This conveys an impression of a further qualification or weakening of the intended assurance provided by the auditor - in the past when such terminology was used, it was in the context of an audit being intended to provide a "high, but not absolute level of assurance". Furthermore, reasonableness cannot be closely related to the concept of the "absolute" - if something is reasonable, it is reasonable and is in any case the result of a judgment. We object to introducing the new terminology "reasonable but not absolute assurance" to the auditor's report.

Later in the auditor's report the term "reasonable" is used again in the phrase "reasonable basis for our opinion". Reasonable is also used when describing management's responsibility "to make estimates that are reasonable in the circumstances" and the auditor evaluating "...the reasonableness of significant estimates made by management".

While we recognize that not all of the usage of the word "reasonable" is new to this standard on auditor reports, we are concerned that the word reasonable is being used frequently, now sometimes with a new modifying phrase, and possibly with different intended meanings. This will not contribute to understanding of the audit and audit report. In light of this, some of our members have expressed a preference for new wording of the last sentence in the Auditor's Responsibility section, to say instead "we believe that the audit evidence we have obtained is sufficient and appropriate to support our opinion on the financial statements."

We understand that the Board may be seeking a means to improve understanding as to what is involved in an audit and what an audit can accomplish, but we do not find it acceptable to do this by introducing new language in the auditor's report that appears to weaken the assurance provided by an audit or by overemphasizing what an audit does not do.

Requirements for the Auditor's Report

In this ED, it is unclear if the requirements for certain statements to appear in the auditor's report are requirements for the exact wording shown in certain bold type paragraphs (for example, where terms such as "should state that" are used and followed by text in bold paragraphs 25, 28, 33, 34, 37) – or whether the standard is only stating that these subjects or elements must be included in a statement made. Although paragraphs 14 and 57 seem to indicate that the wording used in the ISA is to be adopted in the absence of any national requirements to the contrary, or that the ISA is really prescribing "elements" to be included in auditor reports rather than exact wording, these statements are presented in gray lettering which some might take to be non-mandatory guidance.

If it were intended by the ISA that only the exact wording shown should be used in auditor's reports, our members would be concerned that this is too high a level of prescription.

ISA 200 and Auditor Accountability

In paragraph 19 of ISA 200, language needs to be added to note the auditor's accountability for his or her use of judgment. For example, the auditor must be able to demonstrate that the judgments were appropriate in the circumstances. In Paragraph 21, for balanced coverage, something needs to be said in this paragraph about what the audit does, as well as what it does not. A positive statement should be made as to the level of assurance obtained through conducting an audit and conveyed to users in an unqualified audit opinion, as opposed to only negative statements.

Timetable for the Project

We believe that the IAASB should consider whether evolving national changes affecting auditor reports, subsequent changes to ISA 700 that may be expected to arise in the project on ISA 701, the need to settle on a satisfactory approach to improve clarity in auditing standards, or other matters warrant a change to the present workplan or timetable for this proposed ISA. The issue of consistency and suitability of the auditor's report from an investor perspective is

obviously a very fundamental issue that would benefit from thorough debate from both an investor and an auditor perspective.

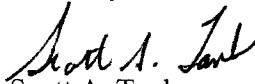
In light of the importance of the auditor's report as the visible product of the audit, we believe that the Board should give consideration to extending this project. This would provide additional time to seek and consider the other factors affecting the auditor's report, beginning with the comment letters to the ED, but not limited to such input. We suggest that the Board could undertake to specifically seek user inputs through a meeting or roundtable or otherwise, and also review auditor report changes being made or contemplated in jurisdictions around the world. A significant extension of this project might also enable the Board to consider modified as well as unmodified auditor reports at the same time.

If due consideration of all issues impacting this project is not feasible in the short term, and the decision is made nonetheless to finalize the ISA 700 standard in time for 2005, we urge the Board to manage the work on ISA 701 to include reconsideration of ISA 700 impacts more broadly, rather than just as conforming change activity.

In addition to our broad, overarching comments regarding this project, we have a number of comments that are focused on specific provisions in the ED for ISAs 700, 200, and 210, and the conforming amendments. These are described in the attachment to this letter.

Please do not hesitate to contact me or Susan Koski-Grafer or any member of IOSCO Standing Committee No. 1 if you would like to discuss any of our comments further.

Sincerely,



Scott A. Taub

Chairman

IOSCO Standing Committee No. 1

On Multinational Disclosure and

Accounting

ATTACHMENT

IOSCO SC 1 Comments on Specific Provisions in the ED

These comments do not repeat the comments already made in the main body of our SC 1 letter

ISA 700 The Independent Auditor's Report on a Complete Set of Financial Statements

Paragraph 10 – The first sentence explaining “scope of an audit” should also refer to ISAs, as follows (italics ours) “The term “scope of an audit” refers to the audit procedures deemed appropriate in the circumstances, in the auditor’s judgment *and in accordance with ISAs*, to achieve the objective of the audit”.

Paragraphs 10 and 11 - It should be made clear in the ISA that the use of a "true and fair view override" is limited to jurisdictions where such a concept is in the accounting standard/applicable financial reporting framework and it is permitted by law or regulation for the auditors to exercise such override.

Paragraph 39 –There is scope for confusion as to when national legal requirements should be deemed to form part of the financial reporting framework and when they should instead be categorised as "other reporting responsibilities". In Europe, for example, entities not applying IFRS will typically be subject to both national accounting standards and accounting requirements under national legislation (implementing the EU Accounting Directives). The auditor may be required, in addition to giving a true and fair view opinion on the financial statements, to report in specific terms on compliance with the legal requirements (e.g. that the financial statements have been "properly prepared" in accordance with the relevant statute).

Paragraph 53 - there is a need to clarify that the auditor may refer in his report to both ISAs and national standards where he has complied with both. (Moving the word “only” to follow “conducted in accordance with ISAs” would make the necessary clarification.)

Paragraph 55 appears to implicitly acknowledge that an auditor may refer to both a national framework and ISAs if both are complied with in performing the audit. We would prefer to see this wording amended to explicitly state this.

ISA 200 “Objective and General Principles Governing an Audit of Financial Statements

Paragraph 5 - while the engagement team certainly utilizes the firm’s “policies, procedures, and systems” in complying with ethical requirements, we think it an overstatement to say that “the engagement team *relies* on a firm’s systems in meeting its responsibilities with respect to quality control procedures applicable to the individual audit engagement”. (Italics ours) The engagement team and in particular the engagement partner also have specific responsibilities for individual actions. We refer you to our letter of October 21, 2003, on the Exposure Draft for the quality control standard and related ISQC.

Paragraph 7 - this paragraph inserts the “basic principles and essential procedures” type of language that we have previously objected to in our IOSCO SC 1 comment letters and

meetings with representatives of the Board on the clarity of ISAs. Given that much of the bold lettered material in ISA 700 consists of neither basic principles nor essential procedures (but rather mandated statements for inclusion in the audit report), this type of language seems inconsistent with the approach actually adopted in revising ISA 700. The Board is therefore open to criticism for failing to adopt a coherent approach to standard setting.

Paragraph 16 - this paragraph is useful in emphasizing the importance of professional skepticism. It also needs to mention the need for professional skepticism when considering representations from those charged with governance of the entity, as we have commented in our earlier letter on the Auditor's Responsibility to Consider Fraud in an Audit of Financial Statements.

Paragraph 18 – the phrase “inherent limitations of internal control” seems too negative and should be replaced with a reference to “factors which may undermine the effectiveness of internal control”. We also refer you to our letter of comments on the Exposure Draft on The Auditor's Responsibility to Consider Fraud in an Audit of Financial Statements, regarding the need to avoid language that is unreasonably negative about the ability of the auditor to detect fraud.

Paragraph 36 - this definition of an “applicable financial reporting framework” in this paragraph should begin by mentioning legal and regulatory requirements that are applicable in many jurisdictions, and then proceed to guidance on what to do when no such framework exists (or a choice of frameworks is allowed by the jurisdiction). Guidance should also be provided for when there are doubts about the suitability of a framework because the framework is not of a quality that is acceptable for cross border usage.

Paragraph 37 - Suggest that this statement be revised to read “The auditor should determine whether the financial reporting framework identified by management is acceptable in the case where the legal framework in the jurisdiction provides for the possibility to choose between different financial reporting frameworks, as well as when the legal framework in a jurisdiction does not specify any financial reporting framework. In the case where a jurisdiction has an established framework developed and issued by a national standards setter, the auditor would ordinarily presume such a framework to be suitable, unless it appears that application of the framework would produce results that are misleading to investors.

Paragraph 41 - the qualifying phrase “provided the standards setting organizations follow an established process involving deliberation and exposure of proposals for comment to a wide range of stakeholders” seems inappropriate in that there may be cases where duly-authorized regulators and standards-setters that do not expose all decisions for comment. We would suggest that the phrase be revised to state something similar to “provided the standards issued are duly authorized in the jurisdiction and are accepted by securities regulators having responsibility for oversight and investor protection.”

ISA 210 Terms of Audit Engagements

We believe paragraphs 15-17 need further clarification. First, there is an issue of “suitable” versus “acceptable” - from the text in the current ED, it seems that “suitable” or “appropriate” is really what is intended, rather than merely “acceptable”. More consistent use of language and additional guidance seems to be needed here. We think that it will be

difficult for the auditor to judge what constitutes a significant difference without some criteria with which to make such judgments.