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- please always indicate -

**Request for Comments:**

**ED 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**

Dear Mr. Gunn,

Dear Ladies and Gentlemen,

We are pleased to take this opportunity to comment on the IAASB 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.

Please find below a short summary of our position on ED ISA 720 (rev.) before we comment on selected questions.

**Summary of our position on ED ISA 720 (revised):**

Basically, we welcome and support the intention of the IAASB, to take into account the latest developments in the corporate reporting environment in the standard setting process. However due to the following reasons we do not approve to the proposed ISA 720:

- Without compelling reason the draft extends the scope of duties of the auditor beyond – at least in Germany – legal requirements.

- The draft increases the expectation gap through the use of ambiguous terminology and vague provisions.
- The draft may lead to increased liability risks for auditors.
- Within the auditor's report Information about the (audited) financial statement and the (non-audited) other information are put together in a possibly misleading relationship.

### **Selected questions in detail:**

#### ***Scope of the Proposed ISA***

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

and

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?*

In principle, we agree with the IAASB that the amount of information from and about a company is growing steadily. External third parties do not always see what information is reliable and which is not.

Under the assumption that the assessment of 'other information' belongs to the remit of the auditor, we also agree with the IAASB that it does not matter whether the information is securely connected to the published annual financial statements (e.g. in the form of an annual report) or is published as stand-alone documents (accompanying documents) to the financial statements.

However, the answer to the question whether it is the responsibility of the auditor to assess "other information" should be left to the legislators or should be dealt with on a contractual basis between client and auditor. Our understanding is that the evaluation of other information in the sense of proposed ISA 720 is not a matter of a statutory audit, and should therefore not be dealt with in an ISA.

The concept of 'other information' in the proposed ISA is misleading. Due to the phrases "...in connection with the initial release..." in ISA 720.9 (c), and in ISA 720.9 (c) ii: "...and has a primary purpose of providing commentary to enhance the users' understanding of the audited financial statements and the auditor's report thereon." it is not sufficiently understandable what documents are within the scope of the ISA and which are not. Also the explanations in the application and other explanatory material help only to a limited degree.

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?*

With regard to the extent of work and a limitation of liability of the auditor we basically welcome the intention of the proposed ISA to introduce a temporal component (initial release) to limit the scope of the documents to be assessed. Unfortunately the definition in ED ISA 720.9 (b) and section A4-A6 of 'initial release' are misleading.

However the idea of initial release is not conceptually convincing. Documents to be published at a later date than the initial release may for the purposes of ISA 720.9 (c) ii also 'have a primary purpose of providing commentary to enhance the users' understanding of the audited financial statements and the auditor's report thereon' and may be used by addressees for their economic choices.

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?*

We refrain from an answer.

## **Objectives**

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?

An auditor does understand the meaning of the terminology "in light of the auditor's understanding of the entity and its environment acquired during the audit".

Nevertheless the terminology is misleading for external parties. An external party may have only a limited understanding of the subjective "auditor understanding". This may result in misinterpretations and thus in an increase of the expectation gap; in the context of civil proceedings possibly to increased liability risks.

The extant ISA 720 refers to the financial statements as reference base. This concept is much clearer, more understandable and distinguishable. Also under the extant ISA, the auditor has to consider his/her understanding of the business and its environment when assessing other information - even though this is derived implicitly from the professional duty of the auditor.

(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. A reference to the financial statement is not sufficiently clear (see our reply to question 6).

## **Definition of an Inconsistency in the Other Information**

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?

and

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?*

The definition of inconsistency in ISA 720.9 (a) does not make it sufficiently clear that a reference to the audited financial statements has to be made. This is also true for the other explanations in the proposed ISA. Rather, the standard prominently stresses the understanding of the auditor of the company and its environment.

The provisions in ISA 720.8 and .11 in connection with the definition in ISA 720.9 (a), however, might lead to the conclusion that the auditor has to assess the different documents of the other information against each other and the completeness of them overall. This should be explicitly negated.

#### ***Nature and Extent of Work Effort***

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?*

(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?*

(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?*

We prefer a principles-based approach to a case-based approach. We consider a categorization of the other information in accordance with A37 as ponderous. Rather it should be at the discretion of the auditor to determine his/her audit approach.

The proposed ISA imposes disproportional obligations in relation to other information. This is caused by an unclear delimitation of the relevant documents (see our comments on questions 1-3) in combination with the very far-reaching definition of inconsistency (see our comments

on questions 6-7) and the use of the phrase "in light of the auditor's understanding of the entity and its environment acquired during the audit "(see our answer to question 5).

Overall we do not see the need for the revision of the definition of inconsistency and the use of the 'auditor understanding' as the reference base. Both provisions do not lead to a relevant increase of the quality of the audit. Rather, there is a risk of enlarging the expectation gap and thus the risk of liability due ambiguous terminology and delimitation issues.

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

Yes

### ***Responding When the Auditor Identifies That the Audited Financial Statements May Be Materially Misstated***

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

### ***Reporting***

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?*

(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?*

and

*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?*

The terms "read and consider," and "in light of our understanding of the entity and its environment acquired during our audit," are not sufficiently clear and unambiguous, and in particular from the perspective of third parties misleading.

Overall, we believe that it is not appropriate to combine statements about the audited financial statements and statements about the non-audited other information in the auditor's report - unless explicitly required by national law. Otherwise third parties might get confused about the degree of assurance on the financial statements and the other information. Rather there is the possibility that the listing of the other information in the auditor's report creates alleged evidence of extensive assurance of these other information. This can result in an increase in the expectation gap and in the risk of liability of the auditor. The statement "no audit opinion or review conclusion" in relation to other information is only partly suited to reduce this risk.

We hope that our remarks will be taken into consideration in the subsequent course of the proceedings, and we would be delighted to answer any questions you may have.

Kind regards

RA Peter Maxl  
Executive Director

RA Dr. Volker Schnepel  
Head of professional law, accounting & auditing