

## Mark-up from May 2006 IAASB Draft

### Proposed Amended ISA 210, “Terms of Audit Engagements”

#### Introduction

[No changes are proposed to extant paragraphs 1-4. These paragraphs are also not necessary to provide context to the proposed changes. As a result, they have not been reproduced here.]

#### Audit Engagement Letters

[No changes are proposed to extant paragraphs 5-9. As a result, they have not been reproduced here.]

#### Agreement on the Applicable Financial Reporting Framework

10. The terms of the engagement should identify the applicable financial reporting framework.

~~1311.~~ The auditor should accept an engagement ~~for an~~ to audit ~~of~~ financial statements only when the auditor concludes that the applicable financial reporting framework is acceptable or subject to paragraph 20, ~~when it is required by law or regulation prescribes the use of the financial reporting framework. Where law or regulation prohibits an auditor from refusing an engagement to audit financial statements, the auditor should consider the effect of any deficiencies in the applicable financial reporting framework on the audit opinion in accordance with [proposed] ISA 705, “Modifications to the Opinion in the Independent Auditor’s Report.” [Part of paragraph moved to 14a]~~

~~11.~~ As stated in ISA 200 the acceptability of the applicable financial reporting framework will depend on the nature of the entity, the objective and nature of the financial statements, and whether applicable legislative and regulatory requirements prescribe the financial reporting framework. The financial statements may be prepared and presented in accordance with a financial reporting framework designed to meet the common financial information needs of a wide range of users or a financial reporting framework designed to meet the financial information needs of specific users.

~~200.36a~~12. A condition for acceptance of an assurance engagement is that the criteria referred to in the definition of an assurance engagement are suitable and available to intended users ~~(see paragraph 48i)~~. Criteria are the benchmarks used to evaluate or measure the subject matter including, where relevant, benchmarks for presentation and disclosure. Suitable criteria are required for reasonably consistent evaluation or measurement of a subject matter within the context of professional judgment. ~~[From extant ISA 200.3]~~

~~200.36b.~~ For purposes of the ISAs, the applicable financial reporting framework provides the criteria the auditor uses to evaluate or measure the preparation and presentation of the financial statements. ~~The applicable financial reporting framework may encompass financial reporting standards established by an authorized or recognized standards setting organization, legislative and regulatory requirements or, in the case of special purpose~~

~~financial statements, financial reporting provisions established by a regulator or by a contract. [From ED-ISA 701.10]~~

- ~~1413.~~ Without an acceptable financial reporting framework management does not have an appropriate basis for preparing and presenting the financial statements and the auditor does not have suitable criteria for evaluating the entity's financial statements. In many cases the auditor may presume that the financial reporting framework is acceptable, as described in paragraphs 18 and 19 of this ISA. ~~In these circumstances, unless use of the financial reporting framework is required by law or regulation, the auditor encourages management to address the deficiencies in the financial reporting framework or to adopt another financial reporting framework that is acceptable. [Part of paragraph moved to 14b]~~
- ~~12.~~ ~~ISA 200 describes the financial reporting frameworks that are presumed to be acceptable, and how the auditor determines the acceptability of other financial reporting frameworks.~~
- ~~14.~~ Deficiencies in the applicable financial reporting framework that indicate that the framework is not acceptable may be encountered after the engagement has been accepted. If application of this framework may result in financial statements that are misleading in the circumstances of the entity, management adopts another framework that is acceptable, and the auditor agrees this change in framework in new terms of engagement. If management does not adopt another financial reporting framework, the auditor considers the effect of the misleading nature of the financial statements on the auditor's report in accordance with ISA 705, "Modifications to the Opinion in the Independent Auditor's Report" or ISA 706, "Emphasis of Matter Paragraphs or Other Matter(s) Paragraphs in the Independent Auditor's Report." (See paragraph 22 for financial reporting frameworks the use of which is prescribed by law or regulation.)

#### **Determining the Acceptability of the Applicable Financial Reporting Framework [From ISA 200]**

~~200.37.~~ ~~The auditor should determine whether the applicable financial reporting framework is acceptable. The auditor ordinarily makes this determination when considering whether to accept the audit engagement, as discussed in ISA 210, "Terms of Audit Engagements."~~

~~200.38~~15. Factors that may affect the auditor's determination of the acceptability of the applicable financial reporting framework include:

- The nature of the entity (for example, whether it is a business enterprise, a public sector entity or a not for profit organization);
- The objective of the financial statements (for example, whether they are prepared and presented in accordance with ~~a financial reporting framework designed to meet the financial information needs of specific users~~ or a financial reporting framework designed to meet the common financial information needs of a wide range of users or a financial reporting framework designed to meet the financial information needs of specific users);

- The nature of the financial statements (for example, whether the financial statements are a complete set of financial statements or a single financial statement); and
- Whether applicable legislative and regulatory requirements prescribe the applicable financial reporting framework.

~~200.38a. When the auditor concludes that the applicable financial reporting framework is not acceptable, the auditor considers the implications in relation to engagement acceptance (see ISA 210) and the auditor’s report. [From extant ISA 200.48]~~

~~200.39. [Moved to ISA 200.48a b]~~

~~200.40~~16. Many users of financial statements are not in a position to demand financial statements tailored to meet their specific information needs. While all the information needs of specific users cannot be met, there are financial information needs that are common to a wide range of users. Financial statements prepared and presented in accordance with a financial reporting framework designed to meet the common financial information needs of a wide range of users are referred to as “general purpose financial statements;” ~~unless they have been prepared to meet the financial information needs of specific users. For purposes of the ISAs, financial statements prepared to meet the financial information needs of specific users are considered to be special purpose financial statements, even though they may have been prepared and presented in accordance with a financial reporting framework designed to meet the common financial information needs of a wide range of users (see paragraph 48c).~~

~~200.48a~~17. In some cases, the financial statements will be prepared and presented in accordance with a financial reporting framework designed to meet the financial information needs of specific users. Such financial statements are referred to as “special purpose financial statements.” The financial information needs of the intended users will determine the applicable financial reporting framework in these circumstances. ISA 800, “Special Considerations—Audits of Special Purpose Financial Statements and Specific Elements Accounts or Items of a Financial Statement” discusses the acceptability of financial reporting frameworks designed to meet the financial information needs of specific users.

*Financial Reporting Frameworks Designed to Meet the Common Financial Information Needs of a Wide Range of Users [From ISA 200]*

~~Financial Reporting Standards Established by Authorized or Recognized Standards Setting Organizations [From ISA 200]~~

~~200.41~~18. At present, there is no objective and authoritative basis that has been generally recognized globally for judging the acceptability of financial reporting frameworks designed to meet the common financial information needs of a wide range of users. ~~Until~~ In the absence of such a basis ~~exists~~, financial reporting standards established by organizations that are authorized or recognized to promulgate standards to be used by certain types of entities are presumed to be acceptable for general purpose financial statements prepared and presented by such entities provided the organizations follow an

established and transparent process involving deliberation and consideration of the views of a wide range of stakeholders. Examples of such financial reporting standards include:

- IFRSs promulgated by the International Accounting Standards Board;
- IPSASs promulgated by the International Public Sector Accounting Standards Board; and
- Accounting principles promulgated by an authorized or recognized standards setting organization in a particular jurisdiction.

These financial reporting standards are often identified as the applicable financial reporting framework in legislative and regulatory requirements governing the preparation and presentation of general purpose financial statements.

Legislative and Regulatory Requirements Financial Reporting Frameworks Prescribed by Law or Regulation [From ISA 200]

~~200.41a19.~~ In some jurisdictions, the financial reporting framework comprises primarily legislative and regulatory requirements for preparing and presenting general purpose financial statements. ISA 210 recognizes that deficiencies may exist in such frameworks and explains the effect that these may have on the auditor's decision to accept the engagement and on the auditor's report. In some jurisdictions, law or regulation may prescribe the financial reporting framework to be used by management in preparing and presenting general purpose financial statements for certain types of entity. In the absence of indications to the contrary, such a financial reporting framework is presumed to be acceptable for general purpose financial statements prepared and presented by such entities.

~~14a20.~~ When law or regulation requires use of a financial reporting framework that the auditor would otherwise consider to be unacceptable, the auditor should accept the engagement only if any deficiencies in the framework can be adequately disclosed in the financial statements to avoid misleading users. When law or regulation prescribes the use of a financial reporting framework that the auditor concludes is unacceptable pursuant to paragraph 11, and the auditor concludes that application of the framework may result in financial statements that are misleading in the circumstances of the entity, the auditor should accept the engagement only if management agrees to provide disclosures in the financial statements beyond the specific requirements of the framework to avoid misleading users of the financial statements. If management refuses to do so and law or regulation prohibits the auditor from refusing the engagement, the auditor should consider the effect of the misleading nature of the financial statements on the auditor's report in accordance with ISA 705 or ISA 706.

~~14b21.~~ When the financial reporting framework is required by law or regulation and management has no choice but to adopt this may have to use a financial reporting framework prescribed by law or regulation even though it may result in financial statements that are misleading in the circumstances of the entity. In these circumstances, the auditor accepts the engagement only if any deficiencies can be adequately disclosed

management agrees to provide disclosures in the financial statements beyond the specific requirements of the framework to avoid misleading users of the financial statements. In addition, the auditor includes an eEmphasis of mMatter paragraph in the auditor's report in accordance with ~~[proposed] ISA 706, "Emphasis of Matter Paragraphs and Other Matters Paragraphs in the Independent Auditor's Report."~~ Unless required by law or regulation to do so, the auditor does not express the opinion on the financial statements using the phrases "give a true and fair view" or "are presented fairly, in all material respects," in accordance with the applicable financial reporting framework. **If the financial statements do not adequately disclose the deficiencies in the financial reporting framework to avoid misleading users, the auditor should consider the effect of the deficiencies the audit opinion in accordance with [proposed] ISA 705.**

~~1522.~~ The auditor may encounter dDeficiencies in the applicable a financial reporting framework the use of which is prescribed by law or regulation that were not anticipated when the engagement was initially accepted and that indicate that the framework is not acceptable may be encountered after the engagement has been accepted. In these circumstances, the auditor discusses the deficiencies with management and the ways in which such deficiencies may be addressed. If the deficiencies application of this framework may result in financial statements that are misleading in the circumstances of the entity, and there is agreement that management will adopt another financial reporting framework that is acceptable, the change in the financial reporting framework is agreed in new terms of engagement. If management refuses to adopt another financial reporting framework, or where the financial reporting framework is required by law or regulation, the auditor considers the effect of the deficiencies in the framework on the audit opinion in accordance with [proposed] ISA 705. management provides disclosures in the financial statements beyond the specific requirements of the framework to avoid misleading users of the financial statements. If management does not provide such disclosures, the auditor considers the effect of the misleading nature of the financial statements on the auditor's report in accordance with ISA 705 or ISA 706.

#### Financial Reporting Standards Supplemented by Law or Regulation

~~200.4223.~~ In some jurisdictions, legislative ~~and or~~ regulatory requirements may supplement the financial reporting standards established by an authorized or recognized standards setting organization with additional requirements relating to preparing and presenting financial statements. This may, for example, be the case when legislative ~~and or~~ regulatory requirements prescribe disclosures in addition to those required by the financial reporting standards or when they narrow the range of acceptable choices that can be made within the financial reporting standards.

24. Where financial reporting standards established by an authorized or recognized standards setting organization are supplemented by legislative or regulatory requirements, the auditor determines whether ~~If the additional requirements any~~ conflicts ~~with between~~ the financial reporting standards and the additional requirements exist. Where such conflicts exist, the auditor discusses the nature of the additional requirements with management and whether (a) the additional requirements can be met through additional disclosures in the financial statements, or (b) the description of the applicable financial reporting framework in the

financial statements can be amended accordingly ~~(see paragraph 48i)~~. If this is not possible, the auditor considers whether it is necessary to modify the auditor's ~~report opinion, see in accordance with [proposed] ISA 705, "Modifications to the Opinion in the Independent Auditor's Report" and ISA 706, "Emphasis of Matter Paragraphs and Other Matters Paragraphs in the Independent Auditor's Report."~~

### Jurisdictions that Do Not Have Authorized or Recognized Standards Setting Organizations or Financial Reporting Frameworks Prescribed by Law or Regulation

25. Appendix 2 contains guidance on determining the acceptability of financial reporting frameworks in jurisdictions that do not have authorized or recognized standards setting organizations or financial reporting frameworks the use of which is not prescribed by law or regulation.

### **Form of Wording Used to Express the Opinion**

~~15a~~26. ~~ISA 200 discusses the form of opinion to be expressed as a result of an audit of financial statements.~~ When wording prescribed by law or regulation differs significantly from the phrases described in the ISAs 200, the auditor considers whether there may be a risk that users might misunderstand the assurance obtained in the audit of the financial statements. In such circumstances, the auditor considers whether the risk of misunderstanding can be mitigated through appropriate explanation in the auditor's report (see ~~[proposed] ISA 706~~).

~~15b.~~ ~~When wording prescribed by law or regulation implies or requires a level of assurance different from that ordinarily obtained in an audit of financial statements (for example, when it requires a certification of fact), the auditor confirms the required level of assurance with management, and considers whether the required level of assurance can be obtained, for example, by amending the scope of the audit.~~ **If the auditor concludes that the required level of assurance cannot be obtained risk of misunderstanding cannot be mitigated through appropriate explanation in the auditor's report, the auditor should not accept the engagement.**

~~15e~~26. Law or regulation, however, may prohibit ~~an the~~ auditor from refusing ~~such an the~~ engagement ~~to audit financial statements~~. An audit conducted in accordance with such law or regulation ~~will does~~ not comply with the ISAs.

### **Recurring Audits**

[No changes are proposed to extant paragraphs 16-17. As a result, they have not been reproduced here.]

### **Acceptance of a Change in Engagement**

[No changes are proposed to extant paragraphs 18-25. As a result, they have not been reproduced here.]

### **Effective Date**

2628. This ISA is effective for audits of financial statements for periods beginning on or after [date].

## **Public Sector Perspective**

[No changes are proposed to the PSP. As a result, it has not been reproduced here.]

## **Appendix [1](#): Example of an Engagement Letter**

[No changes are proposed to the Appendix. As a result, it has not been reproduced here.]

## Appendix 2

### Determining the Acceptability of Financial Reporting Frameworks Designed to Meet the Common Financial Information Needs of a Wide Range of Users

#### Jurisdictions that Do Not Have Authorized or Recognized Standards Setting Organizations or Financial Reporting Frameworks Prescribed by Law or Regulation

200.431. When an entity is registered or operating in a jurisdiction that ~~has neither does not~~ have an authorized or recognized standards setting organization, ~~nor where use of a the~~ financial reporting framework ~~established is not prescribed~~ by law or regulation, management identifies an applicable financial reporting framework. Practice in such jurisdictions is often to use the financial reporting standards established by one of the organizations described in paragraph ~~41~~ 21 of this ISA. Alternatively, there may be established accounting conventions in a particular jurisdiction that are generally recognized as the financial reporting framework for general purpose financial statements prepared by certain specified entities operating in that jurisdiction. When such a financial reporting framework is adopted by management, the auditor determines whether the accounting conventions collectively can be considered to constitute an acceptable financial reporting framework for general purpose financial statements. When the accounting conventions are widely used in a particular jurisdiction, the accounting profession in that jurisdiction may have considered the acceptability of the financial reporting framework on behalf of the auditors. Alternatively, the auditor makes this determination by considering whether the accounting conventions exhibit attributes normally exhibited by acceptable financial reporting frameworks (see paragraph ~~44~~ 2), or by comparing the accounting conventions to the requirements of an existing financial reporting framework considered to be acceptable (see paragraph ~~44a~~ 3).

200.442. Acceptable financial reporting frameworks normally exhibit the following attributes that result in information provided in financial statements that is useful to the intended users:

- (a) Relevance, in that the information provided in the financial statements is relevant to the nature of the entity and the objective of the financial statements. (For example, in the case of a business enterprise that prepares general purpose financial statements, relevance is assessed in terms of the information necessary to meet the common financial information needs of a wide range of users in making economic decisions. These needs are ordinarily met by presenting the financial position, financial performance and cash flows of the business enterprise.)
- (b) Completeness, in that transactions and events, account balances and disclosures that could affect conclusions based on the financial statements are not omitted.
- (c) Reliability, in that the information provided in the financial statements:
  - Where applicable, reflects the economic substance of events and transactions and not merely their legal form; and

- Results in reasonably consistent evaluation, measurement, presentation and disclosure, when used in similar circumstances.
- (d) Neutrality, in that it contributes to information in the financial statements that is free from bias.
- (e) Understandability, in that the information in the financial statements is clear and comprehensive and not subject to significantly different interpretation.

[200.44a3](#). The auditor may decide to compare the accounting conventions to the requirements of an existing financial reporting framework considered to be acceptable. For example, the auditor may compare the accounting conventions to IFRSs. For an audit of a small entity, the auditor may decide to compare the accounting conventions to a financial reporting framework specifically developed for such entities by an authorized or recognized standards setting organization. When the auditor makes such a comparison and differences are identified, the decision as to whether the accounting conventions adopted by management in preparing and presenting the financial statements constitute an acceptable financial reporting framework includes considering the reasons for the differences and whether application of the accounting conventions, or the description of the financial reporting framework in the financial statements ~~(see paragraph 48i)~~, could result in financial statements that are misleading. ~~[From extant ISA 200.47]~~

[200.454](#). A conglomeration of accounting conventions devised to suit individual preferences is not an acceptable financial reporting framework for general purpose financial statements.

[200.46](#). ~~———— [Moved to ISA 200.48i]~~

[200.47](#). ~~———— [Moved to ISA 200.44a]~~

[200.48](#). ~~———— [Moved to ISA 200.38a]~~

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