

## **Auditor's Report on Financial Statements – Wording of the Auditor's Report**

### **Introduction**

1. This agenda paper proposes wording for the auditor's report of an audit of financial statements conducted in accordance with ISAs when there are no modifications to the report (i.e., there is no need for an emphasis of matter paragraph and the auditor is able to express an unqualified opinion).

### **Action Required by IAASB**

Review the proposed auditor's report wording and the reasons the Task Force is recommending that wording.

Consider:

- Do you agree with the proposed wording?
- Are there any additional wording changes that you believe should be considered?
- Do you believe that the auditor's report should include reference to the auditor's responsibility for fraud and, if so, how (see discussion on pages 12-13)?
- Do you support the proposed style and structure to the auditor's report?

### **Background**

2. Included are:
  - A complete clean version of the proposed wording (see page 2)
  - A mark-up showing the proposed changes from the illustrative report wording now in ISA 700 (see page 3)
  - An analysis documenting the Task Force's reasons for recommending particular wording (see pages 4-16)
3. Current plans are to discuss the draft wording of the auditor's report with, at a minimum, the IAASB Consultative Advisory Group (CAG) at its meeting in May 2003, which will provide an opportunity to "test the waters" on the suggested wording.

**Tentative Proposed Wording of the Auditor's Report****Auditor's Report**

(Appropriate Addressee)

**Report on the financial statements**

We have audited the financial statements of the ABC Company for the year ended December 31, 20X1 which comprise *[state the primary financial statements such as the balance sheet, income statement, statement of changes in equity and cash flow statement]* and the related notes.

Management is responsible for the preparation and fair presentation of the financial statements in accordance with *[state the relevant financial reporting framework]*. This includes responsibility for maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for making the estimates inherent in the financial statements.

Our responsibility is to express an opinion on these financial statements based on our audit. Our opinion should be read in conjunction with the financial statements including the related notes.

We conducted our audit in accordance with International Standards on Auditing *[or refer to both the International Standards on Auditing and relevant national standards or practices, when appropriate]*. Those Standards require that we design and perform audit procedures to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, information to provide evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the appropriateness of the accounting principles used and reasonableness of significant estimates made by management. In addition, it includes evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements give a true and fair view of (or 'present fairly, in all material respects,') the financial position of the Company as of December 31, 20X1, and of the results of its operations and its cash flows for the year then ended in accordance with International Accounting Standards (or *[title of financial reporting framework with reference to the country of origin]*) (and comply with ... *[refer to relevant statutes or law]*).

**Report on other legal and regulatory requirements** *[If the auditor has other reporting responsibilities]*

In addition, in accordance with relevant ... legal and regulatory requirements....

AUDITOR

Date

Address

**Mark-up of Proposed Changes to Current ISA 700 Wording****(Independent) Auditor's Report**

(Appropriate Addressee)

**Report on the financial statements**

We have audited the financial statements of accompanying<sup>7</sup> balance sheet of the ABC Company as ~~of~~ for the year ended December 31, 20X1, which comprise [state the primary financial statements such as the balance sheet, and the related statements of income statement, statement of changes in equity and cash flows statement] for the year then ended and the related notes.

(split into new ¶) Management is responsible for the preparation and fair presentation of the financial statements in accordance with [state the relevant financial reporting framework]. This includes responsibility for maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for making the estimates inherent in the financial statements. These financial statements are the responsibility of the Company's management.

Our responsibility is to express an opinion on these financial statements based on our audit. Our opinion should be read in conjunction with the financial statements including the related notes.

We conducted our audit in accordance with International Standards on Auditing (or refer to both the International Standards on Auditing and relevant national standards or practices, when appropriate). Those Standards require that we plan design and perform the audit procedures to obtain reasonable assurance ~~about~~ whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, information to provide evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the appropriateness of the accounting principles used and reasonableness of significant estimates made by management. In addition, it includes as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements give a true and fair view of (or 'present fairly, in all material respects,') the financial position of the Company as of December 31, 20X1, and of the results of its operations and its cash flows for the year then ended in accordance with International Accounting Standards (or *[title of financial reporting framework with reference to the country of origin]*) (and comply with ... *[refer to relevant statutes or law]*).

**Report on other legal and regulatory requirements [If the auditor has other reporting responsibilities]**

In addition, in accordance with relevant ... legal and regulatory requirements....

AUDITOR

Date

Address

<sup>7</sup> The reference can be by page numbers.

## Discussion of Reasons for the Recommended Wording

<i>Proposed wording of the auditor's report</i>	<i>Reasons supporting the recommended wording</i>
<i>Title of the report</i>	
(Independent) Auditor's Report	<ul style="list-style-type: none"> <li>▪ The Task Force believes that it is useful, where not otherwise apparent, to refer to the "Independent Auditor" in the title of the auditor's report. Doing so assists in distinguishing the external auditor from internal or other auditors, and reinforces that the auditor is "independent."</li> <li>▪ In the comparison of auditor's reports, 16 of the 40 auditor's reports compared included a reference to "independent" in the title.</li> <li>▪ The practice is not used in virtually all of the European countries – rather those reports tend to refer to being the report of the "Statutory Auditor." As by definition the Statutory Auditor is an independent auditor, it would be a tautology and illogical to refer to the "Independent Statutory Auditor."</li> <li>▪ For that reason, it is not possible to mandate that the title of the auditor's report include "Independent." However, the ISA could recommend that it be included whenever the reference to the auditor does not otherwise convey that message.</li> <li>▪ The Task Force also debated advantages and disadvantages of expanding the auditor's report to discuss the auditor's independence.</li> <li>▪ 5 of the auditor's reports refer to independence other than in the title of the report. 3 of them do so by way of referring to an independent audit (Australia) or independent opinion (Japan, New Zealand, Portugal) in the description of the auditor's responsibilities.</li> <li>▪ After deliberation, the Task Force is of the view that the auditor's report should not include further discussion of the auditor's independence other than in the title to the auditor's report. The reasons for this include that fact that doing so would put specific emphasis on only one of the auditor's professional quality, despite the fact that the auditor's integrity, competence, technical proficiency etc. are equally important. The Task Force was also concerned that, in many cases, it would be difficult to identify all of the sources that impose professional and regulatory independence requirements that are relevant in any particular engagement and unclear what information readers gain by such a list. Where differences in governing rules exist, readers might assume differences in the auditor's independence</li> </ul>

Proposed wording of the auditor's report	Reasons supporting the recommended wording
	that may not, in fact, exist.
<i>Introductory wording</i>	
<p>We have audited the <u>financial statements of accompanying<sup>†</sup> balance sheet</u> of the ABC Company <del>as of</del> <u>for the year ended</u> December 31, 20X1, <u>which comprise [state the primary financial statements such as the balance sheet, and the related statements of income statement, statement of changes in equity, and cash flows flow statement] for the year then ended, and the related notes.</u></p>	<ul style="list-style-type: none"> <li>■ In December 2002, IAASB supported the proposal to require the auditor's report to identify the title of the statements and to make specific mention of the notes to the financial statements.</li> <li>■ Since the statements to be included and the titles of them may vary in different financial reporting frameworks, the guidance will have to be worded in a neutral manner. However, it seems logical that the illustrative example should use the titles in International Accounting Standard IAS 1 (Revised 1997). Paragraph 7 in IAS 1 says:</li> </ul>
<p><sup>†</sup>The reference can be by page numbers</p>	<p><b>“Components of Financial Statements</b></p> <p><b>7. A complete set of financial statements includes the following components:</b></p> <ul style="list-style-type: none"> <li><b>(a) balance sheet;</b></li> <li><b>(b) income statement;</b></li> <li><b>(c) a statement showing either:</b> <ul style="list-style-type: none"> <li><b>(i) all changes in equity; or</b></li> <li><b>(ii) changes in equity other than those arising from capital transactions with owners and distributions to owners;</b></li> </ul> </li> <li><b>(d) cash flow statement; and</b></li> <li><b>(e) accounting policies and explanatory notes.”</b></li> </ul> <p>IFAC Technical Staff had recently received a query from the Audit Practice Committee of the Institute of Chartered Accountants of Jamaica asking why ISA 700 does not refer to the Statement of Changes in Equity. If the illustrative report wording refers to the statements in IAS 1, IAASB will have addressed this concern.</p> <ul style="list-style-type: none"> <li>■ The proposed wording of the reference to the financial statements is taken from the UK auditor's reports. The approach appealed to the Task Force because it allows for variation in the titles of the statements. In addition, it also puts emphasis first on the “financial statements” rather than the list of individual components of those financial statements. The approach is also consistent with the view that it is the financial statements as a whole that “tell the story,” and arguably emphasizes the need for the auditor to think about the financial statements as a whole in forming his or her opinion.</li> <li>■ Six of the auditor's reports in the comparison include reference to specific amounts in the financial statements (Belgium, Hungary, Italy (Collegio Sindacale, which is a long form report), Norway, Poland and Portugal). The</li> </ul>

Proposed wording of the auditor's report	Reasons supporting the recommended wording
	<p>Task Force debated this alternative but concluded that it would not be any more effective in ensuring that the financial statements accompanying the auditor's report are the financial statements on which the auditor has expressed an opinion, because those with an incentive to fraudulently amend the financial statements once the auditor has signed his or her report would do so in any case.</p>
<i>Statement of management's responsibilities</i>	
<p><u>These financial statements are the responsibility of the Company's management. Management is responsible for the preparation and fair presentation of the financial statements in accordance with [state the relevant financial reporting framework]. This includes responsibility for maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for making the estimates inherent in the financial statements.</u></p>	<ul style="list-style-type: none"> <li>▪ Of the 40 auditor's reports reviewed, 37 included a statement of management's responsibility, 31 of which are limited to stating that the financial statements are the responsibility of (or prepared/approved by) management.</li> <li>▪ The first sentence of this proposed description of management's responsibilities brings the auditor's report wording more consistently in line with the description of management's responsibilities in ISA 200 and ISA 580.</li> </ul> <p>ISA 200. 7 says, "While the auditor is responsible for forming and expressing an opinion on the financial statements, the <u>responsibility for preparing and presenting the financial statements is that of the management of the entity. The audit of financial statements does not relieve management of its responsibility.</u>"</p> <p>ISA 580.3 says, "The auditor should obtain evidence that management acknowledges its <u>responsibility for the fair presentation of the financial statements in accordance with the relevant financial reporting framework, and has approved the financial statements.</u>"</p> <p>It is also consistent with the description of the responsibility for financial statements in IAS 1, the May 2002 exposure draft of which refers to "general purpose financial statements" being "prepared and presented in accordance with IFRSs" and that financial statements shall "present fairly."</p> <ul style="list-style-type: none"> <li>▪ At the December 2002 IAASB meeting, members suggested that the description of management's responsibilities might be expanded to also refer to management's responsibility for: <ul style="list-style-type: none"> <li>- the selection of accounting policies</li> <li>- judgments in estimates</li> <li>- the prevention and detection of fraud</li> </ul> </li> <li>▪ The proposed wording of the second sentence is drawn from, in parts, wording in the ISA 210 illustrated engagement letter and in ISA 240. It also includes new wording regarding estimates.</li> </ul>

<i>Proposed wording of the auditor's report</i>	<i>Reasons supporting the recommended wording</i>
<i>Statement of auditor's responsibility</i>	
Our responsibility is to express an opinion on these financial statements based on our audit.	<ul style="list-style-type: none"> <li>▪ 30 of the 40 reports reviewed described the auditor's responsibility in words similar to ISA 700 ("... to express an opinion on the financial statements based on the audit"). Although there were some variations to the wording, including: <ul style="list-style-type: none"> <li>- "... to audit the financial statements" (UK, Poland)</li> <li>- "... to conduct an audit in order to express an opinion" (Australia, Finland)</li> <li>- refer to the responsibility to report the opinion (UK, Malta, New Zealand).</li> </ul> </li> </ul> <p>The Task Force was not convinced that the variations significantly improved the existing wording and recommends that no changes are made to this sentence.</p>
<i>Readers' responsibilities</i>	
<u>Our opinion should be read in conjunction with the financial statements including the related notes.</u>	<ul style="list-style-type: none"> <li>▪ At the December 2002 meeting, it was suggested that the Task Force consider introducing into the auditor's report some sort of description of readers' responsibilities.</li> <li>▪ Task Force members carried out a number of consultations with in-house legal counsel and other knowledgeable people.</li> <li>▪ Those consultations explored whether in light of the increasing use of financial statement across borders, the growing importance of judgment in the selection and application of accounting policies, as well as the increasing complexity of business and financial reporting in a general sense, the auditor's report should highlight: <ul style="list-style-type: none"> <li>- The need for readers to be reasonably knowledgeable.</li> <li>- The need for readers to use reasonable care in understanding the financial statements.</li> <li>- The need for readers to understand the accounting policies adopted and the implications of the choices made in selecting those policies.</li> </ul> </li> </ul>

<i>Proposed wording of the auditor's report</i>	<i>Reasons supporting the recommended wording</i>
	<ul style="list-style-type: none"> <li>▪ Initial reaction to this proposal was not enthusiastic. Comments included that, in the current environment, this is not the right time to introduce such a change; the wording goes largely to the quality of the company's reporting and are disclosures that the company, not the auditor, should make; auditors could be criticized for trying to focus attention on the complexity of the financial statements as a way of deflecting their own responsibilities, and, last but not least, it would quickly become boilerplate and therefore not particularly useful. Other responses included that such wording would not provide any protection from liability and that, if the purpose is to address liability, a disclaimer would be more effective.</li> <li>▪ However, there was some preliminary support for the type of wording suggested in the left-hand column. Rather than address the "expertise" of the reader, it makes it clear that the audit opinion, on its own, does not tell the whole story and, therefore, readers should not rely on the auditor's report, or the opinion stated therein, on its own.</li> <li>▪ The Task Force is interested in IAASB members reaction to this wording and encourages members to seek input on it from legal counsel and others prior to the March 2003 IAASB meeting.</li> </ul>
<i>Reference to auditing standards</i>	
<p>We conducted our audit in accordance with International Standards on Auditing (or refer to <u>both the International Standards on Auditing and relevant national standards or practices, when appropriate</u>).</p>	<ul style="list-style-type: none"> <li>▪ At the IAASB meeting in December 2002, the IAASB accepted the Task Force's recommendation to amend ISA 700 on the basis that the guidance would focus first on audits conducted in accordance with the ISAs, but also provide guidance on audits conducted in accordance with both the ISAs and national standards. The revised wording illustrates these two options.</li> </ul>
<i>Description of the audit process</i>	
	<ul style="list-style-type: none"> <li>▪ The current wording in the middle paragraph of ISA 700 makes the following points to readers: <ul style="list-style-type: none"> <li>- The auditor obtains "reasonable assurance."</li> <li>- The auditor tests evidence supporting amounts and disclosure – i.e. the auditor does not look at all transactions and available evidence.</li> <li>- The audit also involves assessing the accounting principles used and estimates made by management. This is in a separate sentence from that discussing "evidence."</li> <li>- The auditor evaluates the overall financial statement presentation.</li> </ul> </li> </ul>



<i>Proposed wording of the auditor's report</i>	<i>Reasons supporting the recommended wording</i>
	<ul style="list-style-type: none"> <li>▪ Almost all of the auditor's reports surveyed included most of these statements. Only Spain and Greece were selective and included some, but not all, of these matters.</li> <li>▪ Some people (e.g. some participants at the meeting of European national auditing standard setters) expressed a view that this paragraph should inform the reader that the audit was conducted in accordance with ISAs and that's all. They argued that any attempt to summarize the audit process is flawed because it can never adequately convey the whole audit process or the requirements of the audit standards. They also argued that it underplays the "professionalism" of the auditor and the complex judgments made.</li> <li>▪ However, the fact that so many of the auditor's reports surveyed include this paragraph suggests a strong majority view that it serves some purpose. Much of this paragraph wording was developed in response to the perceived "expectation gap" and it may be hard to argue now that a report that includes less explanation is more useful.</li> </ul>
<p>Those Standards require that we <del>plan-design</del> and perform <del>the</del>-audit <u>procedures</u> to obtain reasonable assurance <del>about</del> whether the financial statements are free of material misstatement.</p>	<ul style="list-style-type: none"> <li>▪ At the December 2002 IAASB meeting, the Task Force proposed that it would try to find a surrogate for the word "plan" to be more consistent with the view of the audit process in the new Audit Risk ISAs.</li> <li>▪ The Task Force reviewed the proposed Audit Risk Standards and found two phrases that might be used as an alternative to the current wording in ISA 700: <ul style="list-style-type: none"> <li>- "obtaining and evaluating audit evidence" (e.g., ¶13 in the proposed amendment to ISA 200); and</li> <li>- "designing and performing audit procedures" (e.g., ¶14 in the proposed amendment to ISA 200, ¶4 of the Assessing Risk ED).</li> </ul> </li> <li>▪ The Task Force believes that the latter phrase is better in the sentence. The Task Force also thought that "about" was unnecessary in the sentence and proposes deleting it.</li> <li>▪ Although it could be argued that the term "reasonable assurance" is code (which the Task Force is trying to avoid whenever possible), the Task Force recommended to the IAASB in December 2002 that it should not try to explain the term more fully in the auditor's report. The Task Force argued that it was impossible to avoid the use of all such concepts in the auditor's report and that trying to explain this concept more fully is likely not achievable in a succinct auditor's</li> </ul>

Proposed wording of the auditor's report	Reasons supporting the recommended wording
	<p>report. There are some who believe that the profession should debate more fundamentally what “reasonable assurance” means. The auditor's report could be amended in future if and when new insights emerge following broader debate.</p> <ul style="list-style-type: none"> <li>▪ The Task Force did, however, agree to conform the use of “reasonable assurance” to how it is used in the ISAs. Unfortunately, the ISAs are currently inconsistent between “obtaining” and “providing” assurance, as shown below. There is more use of “provide” in existing ISAs, but the newer standards and proposed Audit Risk / Moderate Assurance Standards seem to be shifting to “obtain.”</li> </ul> <p>ISA 120 ¶13 <i>“The auditor's opinion enhances the credibility of financial statements by <u>providing</u> a high, but not absolute, level of assurance.”</i></p> <p>ISA 200 ¶8 says, <i>“An audit in accordance with ISAs is designed to <u>provide</u> reasonable assurance that the financial statements taken as a whole are free from material misstatement.”</i></p> <p>ISA 240 ¶17 <i>“The auditor's opinion on the financial statements is based on the concept of <u>obtaining</u> reasonable assurance; hence in an audit, the auditor does not guarantee that material misstatements, whether from fraud or error, will be detected.”</i></p> <ul style="list-style-type: none"> <li>▪ The “assurance building blocks” principles from the Assurance Task Force included:</li> </ul> <p><i>“Practitioners <u>obtain</u> assurance and <u>provide</u> a conclusion that conveys that assurance.”</i></p> <ul style="list-style-type: none"> <li>▪ On balance, the Task Force concluded that the existing wording in the auditor's report should remain unchanged in this regard.</li> <li>▪ See also discussion on page 13 of whether this sentence should also make reference to the misstatements whether caused by “fraud or error.”</li> </ul>
<p>An audit includes examining, on a test basis, <u>information to provide</u> evidence supporting the amounts and disclosures in the financial statements.</p>	<ul style="list-style-type: none"> <li>▪ The current wording of this sentence of the auditor's report is inconsistent with how “audit evidence” is defined in the Audit Evidence ED. It defines “evidence” as “... <i>all of the information used by the auditor in arriving at the conclusions on which the audit opinion is based, and includes the accounting records underlying the financial statements and other information.</i>” Thus, the auditor does not “examine evidence,” the auditor examines the underlying accounting records and other information in order to obtain evidence.</li> </ul>

Proposed wording of the auditor's report	Reasons supporting the recommended wording
	<ul style="list-style-type: none"> <li>▪ Conforming amendments proposed to align existing ISAs to the proposed Audit Risk Standards are amending wording that uses “evidence” in the way it is now used in the ISA 700 auditor’s report.</li> <li>▪ The Task Force tried to identify an alternative for “on a test basis” – a phrase that some people had questioned. The Task Force believes that it is important to convey to readers that the auditor does not examine every transaction or supporting document, but has been unable to come up with alternative wording that would convey that thought any better.</li> </ul>
<p>An audit also includes assessing the <u>appropriateness of the</u> accounting principles used and <u>reasonableness of</u> significant estimates made by management...</p>	<ul style="list-style-type: none"> <li>▪ The Task Force debated the extent to which the discussion of the auditor’s consideration of the accounting principles and estimates should be amended, if at all.</li> <li>▪ Some have argued that the auditor’s report would be more useful if the auditor commented more fully in the auditor’s report – perhaps in an emphasis of matter paragraph – on the significant measurement uncertainties in the financial statements (as suggested in the agenda paper on Accounting Estimates at the December 2002 IAASB meeting). Such communications are currently directed to those charged with governance (ISA 260), but not to external users. The Task Force did not believe it appropriate to debate this more fundamental change to the use of the auditor’s report to try to communicate these matters to other users of the audit pending the outcome of the deliberations on the Estimates project.</li> <li>▪ However, in reviewing the various auditor’s reports used around the world, some of them do provide a more informative discussion of what the auditor considers in “assessing” the accounting principles and significant estimates. For example the New Zealand auditor’s report refers to: <i>“It also includes assessing:</i> <ul style="list-style-type: none"> <li>- <i>the significant estimates and judgments made by the (governing body) in the preparation of the financial report and</i></li> <li>- <i>whether the accounting policies are appropriate to the (entity’s) circumstances, consistently applied and adequately disclosed.”</i></li> </ul> <p>The UK, Ireland and Portuguese reports use similar wording although the Portuguese auditor’s report refers to <i>“assessing the reasonableness of estimates.”</i></p> </li> </ul>

Proposed wording of the auditor's report	Reasons supporting the recommended wording
	<ul style="list-style-type: none"> <li>▪ The Task Force did believe that there was merit in emphasizing in the discussion of what an audit is that the auditor has a responsibility for assessing the appropriateness of the accounting policies. In recognition of the fact that the Task Force did not believe it possible to change the wording of the auditor's opinion (see Agenda Item 2-D), this is a visible way of reinforcing that the auditor does not just focus on compliance with the financial reporting framework, but also considers whether the choices made in selecting accounting policies under that framework are appropriate in the circumstances. This message could then be reinforced in the Risk Assessment ISA (e.g. see ¶5) and in the proposed new wording for ISA 700 on the auditor's considerations in concluding on whether the financial statements give a true or fair view or are fairly presented (see Agenda Item 2-D).</li> <li>▪ With respect to accounting policies, the Task Force debated whether to refer separately to their "consistent application" and "adequate disclosure", and concluded that the reference to assessing their "appropriateness" would subsume those considerations. The Audit Risk ED uses this terminology (see ¶5 and ¶34).</li> <li>▪ The Task Force believed it was useful to refer to the "reasonableness" of estimates as it distinguishes the nature of the auditor's consideration between the accounting policies and estimates. This wording is also consistent with the Audit Risk ED (see ¶5).</li> </ul>
<p>... as well as <u>In addition, it includes</u> evaluating the overall financial statement presentation.</p>	<ul style="list-style-type: none"> <li>▪ The Task Force consider alternative wording in various of the reports, for example:  Denmark refers to <i>"In addition, we have evaluated the overall adequacy of the presentation of the financial statements."</i>  Portugal refers to considering the <i>"adequacy of the overall presentation."</i>  Sweden refers to evaluating the <i>"the overall presentation of information in the annual accounts."</i>  But the Task Force concluded that, on balance, they did not improve on the existing wording. The Task Force did believe, however, that there was merit in splitting the sentence and putting this thought in a separate sentence both for readability and to give it separate emphasis.</li> </ul>
<p>We believe that our audit provides a reasonable basis for our opinion.</p>	<ul style="list-style-type: none"> <li>▪ Only 27 of the auditor's reports include this sentence – which is significantly less than those which include the other matters discussed in this paragraph.</li> </ul>

<i>Proposed wording of the auditor's report</i>	<i>Reasons supporting the recommended wording</i>
	<ul style="list-style-type: none"> <li>▪ The Task Force concluded that, although perhaps not a necessary sentence in conveying the auditor's responsibilities or the nature of an audit, it did serve a useful purpose in that it requires the auditor to assert that (and, therefore, hopefully to reflect on whether) the work performed and evidence obtained has provided a reasonable basis for the opinion.</li> </ul>
	<p><b><i>Other possible matters that could be included in this paragraph</i></b></p> <ul style="list-style-type: none"> <li>▪ The Task Force discussed whether any additional matters should be included in this paragraph.</li> <li>▪ For example, in reviewing the various other reports, the following additional matters were in some of the reports:             <ul style="list-style-type: none"> <li>- Obtaining written confirmation of management representations (PwC Australia report).</li> <li>- Obtaining appropriate explanations and information (Belgium, UK and Ireland reports).</li> <li>- Further description of the basis for planning or a reference to materiality and risk (e.g. Brazil and Danish reports).</li> </ul> </li> </ul> <p>On balance, the Task Force did not believe that there were compelling reasons to include any of these additional matters.</p> <p><b><i>Auditor's responsibility with respect to fraud</i></b></p> <ul style="list-style-type: none"> <li>▪ At the December 2002 IAASB meeting, the Task Force had proposed to IAASB that it should try to communicate more clearly the auditor's responsibility with respect to fraud, and that it should do so in a positive sense rather than by referring solely to the limitations of an audit in this respect.</li> <li>▪ Only 3 of the auditor's reports currently make any reference to fraud – the UK, Ireland and New Zealand reports. They do so by explaining, in the first sentence, that the auditor designs and performs "audit procedures" to obtain reasonable assurance whether the financial statements are free of material misstatement, <i>whether caused by fraud or error</i>. This is how the auditor's responsibility is currently defined – in a positive way – in the ISAs (see ISA 240, and similarly the new US SAS 99 ¶12).</li> <li>▪ The Task Force has not proposed to include this phrase because it was unsure whether this would contribute to a better understanding of the</li> </ul>

Proposed wording of the auditor's report	Reasons supporting the recommended wording
	<p>auditor's responsibilities or rather, inadvertently, heighten the expectation gap. Although ISA 240 sets out this responsibility, it also includes a thorough discussion of fraud and error and why fraud, particularly when it involves collusion and concealment, is difficult to detect. Such a discussion is too long to include in the auditor's report.</p> <ul style="list-style-type: none"> <li>▪ The Task Force could not think of another way to describe the auditor's responsibilities with respect to fraud without paraphrasing the responsibilities in ISA 240 (which is under review). Again, that explanation would be too long for the auditor's report and would also put an overemphasis on the auditor's procedures with respect to fraud vis-à-vis the auditor's procedures for other significant matters, such as going concern.</li> <li>▪ If the responsibility cannot easily be written in a positive way, the Task Force then considered whether it should try to describe the limitations of the audit. For example, wording might be: <p><i>Fraud can be difficult to detect because it is intentional and often involves collusion and concealment. My opinion is based on persuasive not conclusive evidence and, therefore, provides reasonable, not absolute, assurance that the financial statements are free of material misstatement caused by fraud or error.</i></p> <p>However, the Task Force does not support including this sort of wording. In the current environment, including wording in the auditor's report that could be perceived to be defensive and denying responsibility may not be well received.</p> </li> <li>▪ The Task Force came to the conclusion that, perhaps, the auditor's report is not the right vehicle to try to communicate further the auditor's responsibility for fraud. There may be better vehicles for communicating more fully what an audit involves, such as the revision suggested by the Materiality Task Force at the December 2002 IAASB meeting to the guidance IFAC issued in the early 1990's "Understanding Financial Statement Audits – A Guide for Financial Statement Users."</li> <li>▪ However, the Task Force seeks IAASB's input on this matter.</li> </ul>
<i>Audit opinion</i>	
<p>In our opinion, the financial statements give a true and fair view of (or 'present fairly, in all material respects,') the financial position of the Company as of December 31, 20X1, and of the results of its operations and its cash flows for the year then ended in accordance with International Accounting Standards (or [title of financial reporting framework</p>	<ul style="list-style-type: none"> <li>▪ See Agenda Item 2-D for a discussion of the wording of the use of "true and fair" or "presents fairly."</li> <li>▪ Otherwise the Task Force does not recommend any changes to this paragraph.</li> </ul>

<i>Proposed wording of the auditor's report</i>	<i>Reasons supporting the recommended wording</i>
with reference to the country of origin) (and comply with ...).	
<i>Structure of the Auditor's report</i>	
	<p><b><i>Use of headings</i></b></p> <ul style="list-style-type: none"> <li>▪ The Task Force discussed the use of headings in the auditor's report.</li> <li>▪ With the proposal to move to a two-part report, at a minimum, headings will be needed to separately identify the auditor's report on the financial statements from the report on other responsibilities. Both Belgium and France adopt this structure in their reports.</li> <li>▪ 9 other auditor's reports made use of headings (Australia, Denmark, Malta, the Netherlands, New Zealand, Portugal, South Africa, the UK and Ireland). The headings identify different parts of the report, such as the Introduction, Respective responsibilities of Directors and the Auditor, Basis of Audit Opinion.</li> <li>▪ While the use of headings is consistent with modern report writing, the Task Force was of the view that use of headings in addition to those to identify the report on the financial statements from the report on other responsibilities would be excessive in a report of this length.</li> </ul> <p><b><i>Order of the auditor's report</i></b></p> <ul style="list-style-type: none"> <li>▪ The Task Force also considered the order of the report. The 40 reports surveyed all followed a consistent style – introductory paragraph, scope of audit, audit opinion. However, the report used by PwC in Australia puts the audit opinion first – which is consistent with modern report writing.</li> <li>▪ While the Task Force was intrigued by the change in order, it believes that the length of the auditor's report is not so long that the opinion is difficult to find, and believes that convergence is more likely if the familiar sequence is retained.</li> </ul>

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