

Analysis of comments

Forming an opinion on the financial statements

Background

The ISA 700 Exposure Draft proposed to introduce a new section on the *Auditor's Opinion on Financial Statements*.

The new guidance in the Exposure Draft was intended to explain more fully the judgments involved in reflecting, at the end of the audit process, on the fair presentation of the financial statements as a whole as a basis for the auditor's opinion on the financial statements. It discussed the terms used to express the auditor's opinion on general purpose financial statements ("true and fair view"/"presents fairly, in all material respects"), the fact that the applicable financial reporting framework provides the context for the auditor's opinion, and introduced new guidance on the matters the auditor considers in forming the opinion.

The proposed new guidance stated that forming the auditor's opinion involves both considering the entity's compliance with specific requirements of the financial reporting framework and the fair presentation of the financial statements as a whole. Matters the auditor needs to consider were identified, but no attempt made to separately align which of those matters relate to compliance with the framework and which relate to a judgment regarding fair presentation of the financial statements as a whole. The guidance also introduced, in essence, an "auditor override" that imposes a responsibility on the auditor to consider whether the financial statements result in misleading information – even if the financial statements are in compliance with the specific requirements of the financial reporting framework.

Overview of comments received

Overall, this section of the proposed ISA 700 attracted substantial comment by respondents. While quite a few responses specifically commented that they welcomed the introduction of the guidance and thought it was an important addition to the international auditing standards literature (FSR, ICANZ, ACCA, CICA, PwC, ACAG, HKSA and Basel Committee), many found the wording of the guidance confusing and lacking clarity, as discussed more fully below. There were also mixed and strongly held views on whether the auditor should have a responsibility to consider the fair presentation independent of compliance with the financial reporting framework.

The comments raised in responses broadly relate to the following underlying issues (which are not entirely mutually exclusive):

- Whether "fair presentation" is an accounting or auditing concept or both
- Whether the auditor's opinion is "one-part" or "two-part"
- Whether the guidance is consistent in the use of the phrase "taken as a whole"
- Whether "true and fair" and "presents fairly, in all material respects" are equivalent
- Whether the "override" is only in extremely rare circumstances
- The lack of clarity in how the guidance is presented

Material presented

This agenda paper presents the following:

- a summary of the comments raised by issue and how the Task Force proposes to address these comments
- a mark-up of the relevant paragraphs with the proposed wording changes

Analysis of comments raised by issue and proposed disposition

Whether “fair presentation” is an accounting concept or auditing concept or both

There were quite strongly held views on this matter.

Eight respondents (IDW, CICA, AICPA, NIVRA, DNR, FEE, JICPA and RR) argued that it is the financial reporting framework and not auditing standards that define whether a set of financial statements is fairly presented.

- IDW express the strongest view, arguing that the auditing standards should not be employed to overcome deficiencies in accounting standards. Providing for an auditor override is, in their view, not appropriate because it means that auditing standards setters are second-guessing accounting standards setters. IDW argue that the scope of ISA 700 should be limited to financial reporting frameworks that include a “fair presentation” override (general purpose financial statements for other frameworks would be included in the scope of ISA 800). Doing so would “obviate the need for an auditor override of any kind based on ethical considerations”.
- The CICA point out that Canadian GAAP was amended only recently to “remove the ability” for an entity to depart from Canadian GAAP. If paragraph 10 is left in the ISA, they argue that the guidance should acknowledge that it does not apply in all jurisdictions.
- AICPA, NIVRA, DNR and FEE all argue that there is a strong presumption that the financial reporting framework for general purpose financial statements in their jurisdiction would, in nearly all instances, result in information in the financial statements being fairly presented. In the case of IFRS, for example, IFRSs are presumed to result in financial statements that achieve a fair presentation in virtually all circumstances and the possibility of the need to override a specific requirement in rare circumstances when the specific requirements do not result in fair presentation is, in fact, embedded in the financial reporting framework. Thus, the respondents point out, it is primarily the financial reporting framework and not the auditing standard that defines whether a set of financial statements is fairly presented. In such circumstances, an “auditor’s override” beyond the financial reporting framework is normally redundant because the “accounting framework override” provides all the tools that the auditor needs to assess in the overall financial statements presentation.
- JICPA argue that providing guidance applicable to specific financial reporting frameworks is not appropriate because the ISAs should be framework neutral and, therefore, the guidance in paragraphs 10 and 11 on the “true and fair override” should be deleted (i.e., delete all but the first sentence in paragraph 10). They are concerned that the guidance could “mislead readers in countries whose financial reporting frameworks do not allow a “true and fair override” concept.
- IOSCO argues 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 where it is permitted by law or regulation for the auditors to exercise such override.
- RR argues that the guidance is inconsistent in whether the concept of true and fair is an auditing concept or an accounting/financial reporting concept. He suggests that regardless of IAASB’s philosophical view on this matter, it is important that the guidance is written in such a way that it is internally consistent and allows auditors to report in the same terms on financial statements prepared in accordance with frameworks that internalise the concept of the true and fair view as the terms they report on financial statements prepared in accordance with frameworks that do not.

An equally significant number of respondents support the view that the auditor does need to consider the fair presentation of the financial statements in addition to considering whether the financial statements are in accordance with the financial reporting framework (FEE, IRE, LSCA, APB, Basel Committee). For example:

- APB note that, in the UK and Ireland, the expression “true and fair view” is not qualified in any way (i.e., not “qualified” by the phrase “in accordance with the financial reporting framework”). Consequently, although the Courts will hold that, in general, compliance with accounting standards is necessary to meet the true and fair requirement, this does not mean that compliance with accounting standards alone is sufficient to meet the true and fair requirement.
- IRE argue that expressing an opinion on the “fairness” of the financial statements includes more than just considering if the financial statements are prepared in accordance with the underlying financial reporting framework and also observe that a disrespect of the framework does not necessarily impact the fair presentation of the financial statements as a whole.

DISCUSSION

Limiting the scope of ISA 700 to financial reporting frameworks that incorporate consideration of “fair presentation” – while having certain intellectual appeal – would be difficult to accomplish. It would further complicate the scope of ISA 800 and, pending further development of the ISA 800 project, it is not clear what would be the implications of including them in ISA 800 rather than ISA 700. In addition, it would be very difficult to draft the guidance necessary to enable auditors to conclude whether or not a particular financial reporting framework for general purpose financial statements has a sufficient guidance on fair presentation so that they can be considered within the scope of ISA 700. For these reasons, this alternative is not recommended.

At the heart of a number of the other arguments is the view that financial reporting frameworks that are “acceptable” for general purpose financial statements should be, by definition, designed to achieve fair presentation – making a separate assessment by the auditor unnecessary. Indeed, the guidance on the characteristics of suitable criteria for purposes of considering whether a financial reporting framework is acceptable includes reference to fair presentation (see ISA 200, paragraph 44). Therefore, since the scope of ISA 700 is auditor's reports on general purpose financial statements, it would be appropriate to recognise that compliance with an acceptable financial reporting framework for general purpose financial statements ordinarily achieves fair presentation.

On the other hand, auditors cannot disregard their professional responsibility under the Code of Ethics not to be associated with misleading information – which seems a reasonable expectation, particularly in relation to general purpose financial statements that are in the public domain. Therefore, it does not seem an option to ignore the fact that an override of specific requirements of the financial reporting framework may be necessary to achieve fair presentation. In circumstances when a financial reporting framework refers specifically to the need to depart from a specific requirement if it does not achieve fair presentation, the auditor will need to consider whether or not this provision should be used in evaluating the entity's compliance with the framework in any case. NIVRA, for example, said that the auditor must assess the acceptability of the accounting framework override – presumably referring to circumstances when management has invoked it. For those financial reporting frameworks that do not specifically contemplate circumstances when a specific requirement may not result in fair presentation, the auditor nevertheless has a professional responsibility to do so.

Thus, the guidance needs to acknowledge the possibility of the need to depart from a specific requirement in the financial reporting framework in order to achieve fair presentation, even if

considered quite a rare circumstance. It would be fair, however, to position the auditor's responsibility in terms of encountering circumstances that lead the auditor to conclude that a departure from a specific requirement is necessary to achieve fair presentation – thus being a response to circumstances encountered rather than an assertion that needs to be proved or disproved. Such circumstances would include management proposing to invoke an override, but could also include matters that come to the auditor's attention during the course of the audit.

Task Force Recommendation:

Retain guidance on the need to consider the fair presentation of the financial statements.

Make the point that application of financial reporting frameworks that are acceptable for general purpose financial statements ordinarily result in fair presentation.

Retain guidance on the extremely rare circumstances when an departure from a specific requirement is necessary to achieve fair presentation is needed, but redraft the guidance to focus on circumstances encountered that lead the auditor to conclude such a departure is necessary.

Whether the auditor's opinion is "one-part" or "two-part"

A number of the responses made comments that relate – directly or indirectly – to the issue of whether the auditor's opinion is "one-part" or "two-part". This issue is not entirely unrelated to the issue discussed above because it rests on whether an opinion on whether the financial statements give a true and fair view/presents fairly in accordance with a financial reporting framework involves considering the fair presentation of the financial statements as a whole in addition to compliance with specific requirements of the framework.

Five respondents (IRE, LSCA, PWC, FEE and APB) argue that expressing an opinion on the fairness of the financial statements includes more than just considering if they are prepared in accordance with the applicable financial reporting framework. Some responses acknowledge that the revised ISA makes some headway in clarifying that the auditor needs to consider both compliance with specific requirements of the financial reporting framework and "fair presentation" (i.e., in paragraphs 9 and 10 of the Exposure Draft). However, some do not believe that the guidance goes far enough in this regard.

IRE, for example, suggest that any reference to "financial reporting framework" in the first sentence in paragraph 10 should be removed in its entirety (i.e. rewritten as: *"The auditor has the responsibility to consider the fair presentation of the financial statements as a whole".*) PwC and LSCA argue that the guidance does not sufficiently promote the concept of a stand back because the matters in paragraph 9 are too closely tied to the financial reporting framework. FEE argues that paragraph 10 would be clearer if it was confined to the requirement for the auditor to "stand back" and consider the fair presentation of the financial statements as a whole.

The APB point out that the "European Union intends to amend the wording that will be required for audit reports on financial statements issued in the EU to be true and fair view in accordance with the relevant financial reporting framework". However, they also add that the Directive announcing this change makes clear that "The fundamental requirement that an audit opinion states whether the annual or consolidated accounts give a true and fair view in accordance with the relevant financial reporting framework does not represent a restriction of the scope of that opinion but clarifies the

context in which it is expressed". The APB recommend that the EU's wording be incorporated into the explanation of the term "true and fair view" in ISA 700.

Other comments, however, reflect the view that the guidance goes too far in separating the consideration of fair presentation from the framework. The CICA, for example, argue that the first sentence of paragraph 10 is inconsistent with the rest of the reporting guidance, in which the auditor is required to report on whether the financial statements are presented fairly, in all material respects, in accordance with IFRS – a one-part opinion. CICA believes the first sentence in paragraph 10 implies that the auditor is expected to make two opinions. They argue that fair presentation in accordance with the financial reporting framework includes the judgments set out in paragraph 9.

Other responses agree with the need to stand back and consider the fair presentation of the financial statements as a whole, but did not believe that there was sufficient clarity in the proposed guidance on what is involved in making that evaluation. A number of suggestions were offered to the structure and wording of the paragraphs (PwC, KPMG) to better achieve the aim of the TF.

If the guidance is to require considerations beyond the financial reporting framework, some responses (e.g., DNR and RR) said criteria are needed to make those judgments. For example, FEE suggested adopting guidance such as is found in Paragraph 13 of IAS 1. NIRVA suggest that additional guidance is necessary in the event of the use of the 'overriding principle' in situations where financial reporting frameworks do not provide any guidance on these circumstances. They echo the sentiment raised in the first issue that it is primarily the financial reporting framework that defines whether a set of financial statements are fairly presented, yet realise that the auditor still needs to "stand-back" and so further guidance is required.

DISCUSSION

There are merits in all of the points raised. Despite the fact that the responses might appear quite disparate, there are common points of agreement. Most respondents would not disagree that the auditor does need to stand back and consider the fair presentation of the financial statements as a whole. Where there is disagreement is whether that is achieved through complying with the financial reporting framework, or whether it should be described as an evaluation that is independent of the framework. In part this may reflect a difference in view on what "compliance with the framework" means, with some interpreting it as compliance with specific requirements alone.

The Task Force remains of the view that expressing an opinion on whether the financial statements give a true and fair view, or presents fairly, in all material respects, in accordance with the applicable financial reporting framework involves evaluating both (i.e., both considerations are integral to forming one opinion):

- whether the financial statements *comply* with the *specific requirements* of the financial reporting framework *for particular classes of transactions, account balances and disclosures*; and
- the *fair presentation* of the financial statements *as a whole*.

The Task Force agrees that the guidance should be made clearer in this respect. In separating the two considerations, the Task Force found that additional guidance is needed on the evaluation of the fair presentation of the financial statements as a whole. In drafting this guidance, the Task Force drew on comparable guidance in national auditing standards (for example, UK SAS 470, *Overall Review of Financial Statements*). In addition, because IAS 1 refers to "faithful representation" as relevant to achieving fair presentation, the Task Force concluded that former ¶9(c) should be moved to the discussion of the "standback".

Task Force Recommendation:

Amend the guidance to make it clear that there are two considerations in forming the auditor's one overall opinion – compliance with the specific requirements of the framework and fair presentation of the financial statements as a whole.

Attempt to more clearly separate considerations related to compliance with the framework and the “standback”. Add additional guidance on evaluating the fair presentation of the financial statements as a whole.

Whether the guidance is consistent in its use of the phrase “taken as a whole”

There were a number of comments in relation to various paragraphs in the Exposure Draft that related to the use of the phrase “taken as a whole”.

Five respondents (KIBR, GT, FSR, JICPA and CNCC/OEC) argue that the phrase “the financial statements, taken as a whole” is an important concept in understanding the auditor's opinion and, for that reason, it should be included in the wording of the auditor's report – some arguing to include it in the opinion (KIBR, FSR), others suggesting it be included in the description of the auditor's responsibilities (GT, JICPA, CNCC/OEC).

FSR suggest that the phrase is essential in providing guidance to the auditor and strongly support including it in the wording of the auditor's opinion to increase “stakeholders' understanding of the auditor's responsibility”. That being said, FSR argue that if the phrase is not used consistently throughout ISAs and in the example auditor's report (implying that they do not believe that it is used consistently in the Exposure Draft wording), they would prefer that it be deleted in those instances that it is now used to avoid any misunderstanding.

Conversely, IDW believe that the concept of “taken as a whole” should be removed from ISA 200 because not all frameworks embrace the concept. They would use “taken as a whole” in ISA 700 (which, as discussed earlier, they would limit to financial reporting frameworks that include a “standback”), but not in ISA 800. They note that although the phrase is used in US auditing standards (e.g., AU 508.05 which explains it is a concept that applies equally to a complete set of financial statements and to an individual financial statement), it does not appear to be well defined in those standards.

DISCUSSION

The concept of the “financial statements taken as a whole” is not new to the ISAs, having been in the explanation of reasonable assurance in ISA 200, as well as in ISAs 240, 540 and 545. It is primarily used in the ISAs in the context of evaluating material misstatements. This is reinforced in the proposed revision to ISA 320, *Materiality in the Identification and Evaluation of Misstatements*. For example, the proposed definition of materiality is based on when a “misstatement, or aggregate of misstatements, would reasonably change or influence economic decisions, taken on the basis of the audited financial statements *as a whole*.”

The following extracts from the ISAs illustrate how the concepts are used in the ISA auditing literature. The extracts show that there is a logical structure in the ISAs that links the objective of an audit, reasonable assurance, sufficient appropriate evidence, the concept of the financial statements

as a whole being free of material misstatement and reducing the risk of material misstatement to an appropriately low level.

- The objective of an audit of financial statements is to enable the auditor to express an opinion whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. (ISA 200 ¶2)
- An audit in accordance with ISAs is designed to provide reasonable assurance that the financial statements taken as a whole are free from material misstatement. Reasonable assurance is a concept relating to the accumulation of the audit evidence necessary for the auditor to conclude that there are no material misstatements in the financial statements taken as a whole. (ISA 200 ¶8) An auditor conducting an audit in accordance with ISAs obtains reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. (ISA 240 ¶21)
- The auditor obtains and evaluates audit evidence to obtain reasonable assurance about whether the financial statements give a true and fair view (or are presented fairly, in all material respects) in accordance with the applicable financial reporting framework. (ISA 200 ¶14)
- The auditor should plan and perform the audit to reduce audit risk to an acceptably low level that is consistent with the objective of an audit. The auditor reduces audit risk by designing and performing audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base an audit opinion. Reasonable assurance is obtained when the auditor has reduced audit risk to an acceptably low level. (ISA 200 ¶15)
- The auditor should obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the audit opinion. (ISA 500 ¶2)
- The auditor should identify and assess the risks of material misstatement at the financial statement level, and at the assertion level for classes of transactions, account balances, and disclosures. (ISA 315 ¶100)
- In order to reduce audit risk to an acceptably low level, the auditor should determine overall responses to assessed risks at the financial statement level, and should design and perform further audit procedures to respond to assessed risks at the assertion level. (ISA 330 ¶3)
- The auditor should conclude whether sufficient appropriate audit evidence has been obtained to reduce to an acceptably low level the risk of material misstatement in the financial statements. (ISA 330 ¶70)

The Task Force proposes that “as a whole” continue to be used in the literature when referring to the assessment of “whether there is material misstatement in the financial statements as a whole”. It is particularly useful in this context because it reinforces that the auditor needs to evaluate not only individual account balances, transactions and disclosures, but also whether the “story” told by the financial statements as a package makes sense. Thus, it reinforces both the auditor’s “standback” and the importance of both qualitative, as well as quantitative, aspects of materiality.

The Task Force does not propose to include the phrase in the auditor’s report, however. While the Task Force is of the view that it is very useful within the body of the ISAs – where it is in the context of the supporting guidance – the Task Force is concerned that using it on its own in the auditor’s report may lead the reader to infer that individual misstatements might be ignored if they counteract one another.

Task Force Recommendation:

Review Exposure Draft wording (and the ISAs) for consistency in when the phrase “financial statements as a whole” is used. For example, see proposed wording of ¶8.

Whether “true and fair” and “presents fairly, in all material respects” are equivalent

Six respondents (APB, IDW, KIBR, PAAB, NIVRA and RR) argue that the terms “true and fair” and “presents fairly” are not equivalent phrases, as suggested in paragraph 6 of the revised ISA.

KIBR argue that the phrases are not equivalent because only “presents fairly” is modified by “in all material respects”. They believe that “in all material respects” is applicable to both “true and fair” and “presents fairly” and, therefore, specifically referring to it in the context of “presents fairly” only introduces a difference in meaning.

APB and PAAB raise practical issues. For example, the PAAB comment that equating the terms may have legal implications in certain jurisdictions. They suggest removing the term “and are equivalent” (which was also supported by APB) and substituting it with “are both acceptable”. The APB goes further to suggest that the IAASB cannot make such an assertion without explaining or offering guidance in the revised ISA as to why they are equivalent. NIVRA asks whether users perceive them as equivalent.

RR argues that it is up to IAASB to establish the phrase that auditors should use in an ISA audit and, whilst IAASB might want to allow the use of both phrases for pragmatic reasons, it should do so based on the principle that the auditor should use the phrase most likely to be understood by the intended readers of the auditor's report rather than because it is required by law or regulation.

DISCUSSION

The phrases that auditors are expected to use are entrenched in national law and regulation establishing auditor's responsibilities. The survey of audit reports in 40 jurisdictions globally conducted in developing the Exposure Draft showed that “true and fair view” and “presents fairly, in all material respects” are equally widely used. Therefore, whilst recognising that there are strongly held views on this issue, pragmatically, it seems best to continue to accept either term.

In report wording today, “true and fair view” is seldom modified by “in all material respects” (note that the proposed EU Directive does not propose to modify “true and fair view” by “in all material respects”) and “presents fairly” seldom used without it. Thus, for similar reasons to those above, it seems best to codify the phrases as used in practice, even though no substantive difference is intended whether or not “in all material respects” is used.

Existing ISA 700 and the proposed ED made the assertion that the terms are equivalent. The guidance can communicate the thought that both phrases can be used without making an assertion regarding their equivalent. The fact that the ISA will include the same guidance on how to form the opinion regardless of the phrase used, however, does imply that they are equivalent under the ISAs. However, the guidance need not make that assertion.

Task Force Recommendation:

While continuing to recognise both “true and fair view” and “presents fairly, in all material respects” as the phrases used for the auditor's opinion in an audit of general purpose financial statements, rewrite the sentence to delete “and are equivalent”.

KIBR also point out that the guidance is ambiguous as written regarding whether the auditor can choose which phrase to use, or whether all auditors in any particular jurisdiction should be using the same term.

The intent is that the same term would be used in any particular jurisdiction and, therefore, the wording of the guidance should be amended to avoid any ambiguity.

Task Force Recommendation:

Clarify that the phrase used depends on the law, regulation or established practice in a particular jurisdiction, rather than being a choice of the auditor.

It was also pointed out that, if they are truly equal, one of the phrases should be not in brackets.

No preference is intended; the brackets had been used only because it seemed easier to read than through the use of commas alone.

Task Force Recommendation

Remove the brackets throughout the guidance.

Whether the “override” is only in extremely rare circumstances

There were two responses (APB and RR) that argue the inclusion of the term “extremely rare circumstances” in reference to the possible need to depart from specific requirements of the financial reporting framework in order to achieve fair presentation was misleading and unhelpful. RR acknowledges that this is the wording that IFRS uses, but might not apply to other frameworks. He adds that we do not have sufficient experience in judging the merits of acceptable frameworks to make this assertion.

The APB also comment on their dissatisfaction with the suggestion that it would be a rare circumstance when departure would be necessary – particularly in relation to disclosures not specifically required by the framework. The APB raise the concern that by making reference to, “extremely rare circumstances [where]... it is necessary for the financial statements to depart from a specific requirement in the framework in order to achieve the objective of fair presentation...”, in the same sentence as the discussion of the true and fair override, an impression is given that the circumstances that give rise to need to include disclosures that are not specifically required by the framework are rare. They argue that this is not the case in practice and make reference to IAS 1 to support the argument that an “override” for an additional disclosure would not necessarily be rare. Similarly, the new Canadian accounting standards on fair presentation similarly refers to the need to consider disclosures beyond those specifically required by the primary sources of GAAP.

Although not directly linking their comments to whether or not the situation was “extremely rare”, other respondents (KPMG, PwC) also suggest separating the consideration of the need for additional disclosures from the situation when departure from a specific requirement is needed to

achieve fair presentation. A number of other respondents also expressed confusion about the wording in the paragraph that combined them.

DISCUSSION

Based on the responses, it would seem best to separate the discussions of the possible need for additional disclosures beyond those mandated in the framework and the possible need to depart from a specific requirement because it would result in misleading information. As APB rightly points out, the need to consider the adequacy of disclosures is not a rare circumstance. Indeed, it is reflected in the list of matters in paragraph 9 that should be considered in assessing the preparation and presentation of the financial statements in accordance with the framework (see (d)). As DNR point out, IAS 1 states “the application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation” – i.e., those additional disclosures are considered to be part of the framework itself rather than an “override” or departure from the framework.

It would seem appropriate to continue to refer to departures from the framework as being extremely rare. Although, as RR points out, we may not yet have substantial experience with our criteria for the acceptability of financial reporting frameworks for general purpose financial statements, the criteria for them in ISA 200 includes completeness, comprehensiveness, relevance etc. Therefore, it would seem internally inconsistent within the ISAs to suggest that a departure from an acceptable framework to achieve fair presentation is other than a rare circumstance. Continuing to refer to the departures to achieve fair presentation as rare also has the advantage of being consistent with IAS 1.

Task Force Recommendation:

Address the need for additional disclosures separately from the need to depart from a specific requirement in order to achieve fair presentation. Continue to refer to the latter as occurring in extremely rare circumstance.

The lack of clarity in how the guidance is presented

There were a number of comments suggesting that the guidance in paragraphs 8-11 lacked clarity (FAR, FEE, LSCA, PAAB, PwC, NIVRA, PMG, APB). KPMG for example said, “These paragraphs are long and unclear.” APB noted that paragraph 10 is “a lengthy paragraph containing a number of disparate ideas that might be better articulated in separate paragraphs.” Indeed, ultimately the many comments received on this section reflect a lack of clarity.

Task Force Recommendation:

Address the concerns of the respondents by applying the recommendations above and then performing a review for clarity in the next draft of the proposed revised ISA 700.

Mark-up showing proposed changes to the ED wording Extract from ISA 700

The Auditor's Report on Financial Statements

Moved to precede
bold lettered ¶

4. The auditor's report should contain a clear expression of the auditor's opinion on the financial statements.

Moved from
former ¶12

~~The auditor should evaluate the conclusions drawn from the audit evidence obtained as the basis for forming an opinion on the financial statements.~~

Moved to new ¶7a

~~The Auditor's Opinion on Financial Statements~~

5. As stated in ISA 200, the objective of an audit of financial statements is to enable the auditor to express an opinion whether the financial statements are prepared, in all material respects, in accordance with a the applicable financial reporting framework.
6. ~~The terms used to express the auditor's opinion on an audit of a complete set¹ of general purpose financial statements (for purposes of this ISA referred to as financial statements) are states whether the financial statements "give a true and fair view", or "are presented fairly, in all material respects", and are equivalent in accordance with the applicable financial reporting framework. Which of these phrases the auditor uses is used in any particular jurisdiction will be determined by the law or regulations governing the audit of financial statements in that jurisdiction, or by established practice in that jurisdiction as reflected, for example, in national auditing standards.~~

To conform with
ISA 200 ¶2

To avoid
implication that
it's a matter of
terminology only

To avoid
impression that
it's a choice

Applicable Financial Reporting Framework

7. The auditor's judgment regarding whether the financial statements give a true and fair view, ~~or (or are presented fairly, in all material respects.)~~ is made in the context of the applicable financial reporting framework. As discussed in ISA 210, "Terms of Audit Engagements," without an acceptable financial reporting framework, the auditor does not have suitable criteria for evaluating the entity's financial statements. ISA 200 describes the auditor's responsibility to determine whether the financial reporting framework adopted by management is acceptable. for general purpose financial statements.

Stronger linkages
to ISA 200,
including
clarifying that the
auditor has
determined that
the framework is
acceptable.

Forming the Opinion on the Financial Statements

- 7a. The auditor should evaluate the conclusions drawn from the audit evidence obtained as the basis for forming an opinion on the financial statements.

Moved from
former ¶4 to set
principle for
section on forming
the opinion

¹ As explained in paragraph 43 of ISA 200, "Objective and General Principles Governing an Audit of Financial Statements", the financial reporting framework determines what constitutes a complete set of financial statements. A complete set of financial statements under IFRS includes a balance sheet, an income statements, a statement of changes in equity, a cash flow statement and a summary of significant accounting policies and other notes.

Link to ISA 200
definitions

8. ~~In-When forming the an opinion on the financial statements, the auditor evaluates whether, based on the audit evidence obtained, there is reasonable assurance about whether the financial statements taken as a whole are free from material misstatement. This involves concluding whether sufficient appropriate audit evidence has been obtained to reduce to an acceptably low level the risk of material misstatement in the financial statements² and considers all audit evidence obtained evaluating the effects of uncorrected misstatements identified³. and evaluates whether, based on that evidence, the auditor has obtained reasonable assurance that the financial statements taken as a whole are free from material misstatement. The auditor considers the sufficiency and appropriateness of audit evidence obtained, and evaluates the effects of misstatements identified.~~

Link to ISA 200 ¶17

Link to ISA 330 ¶70

Link to ISA 320

8a. Forming an opinion whether the financial statements give a true and fair view or are presented fairly, in all material respects in accordance with the applicable financial reporting framework involves evaluating:

a. the financial statements have been prepared and presented in accordance with the specific requirements of the applicable financial reporting framework for particular classes of transactions, account balances and disclosures; and

b. the fair presentation of the financial statements as a whole.

Clarifies that both compliance with specific requirements of the framework and fair presentation are integral parts of the auditor's opinion on true and fair view/presented fairly in accordance with the framework

9. ~~The auditor considers evaluates whether, in the auditor's judgment, the financial statements have been prepared and presented in accordance with the specific requirements of the applicable financial reporting framework, including considering whether:~~

(a) ~~The accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate in the circumstances;~~

(b) The accounting estimates made by management are reasonable in the circumstances;

(c) The information presented in the financial statements, including accounting policies, is relevant, reliable, comparable and understandable;

(e) ~~The financial statements reflect the underlying transactions and events in a manner that fairly presents the financial information in accordance with the applicable financial reporting framework; and~~

(d) The financial statements provide sufficient disclosures about transactions and events that have a material effect on the financial statements to enable users to understand their impact on the information conveyed in the financial statements. of particular transactions or events that have a material effect on, in the case of financial statements prepared in accordance with IFRS, for example, the entity's financial position, financial performance and cash flows.

Paragraph 9 is now focussed on matters that are ordinarily within the framework.

"Prepared and presented" from IAS 1 (e.g. see ¶2)

Included "estimates" in response to comments to align with management's responsibilities in audit report and ISA 200.

Moved to next paragraph.

Editorial changes in respond to comments raised.

² See ISA 330, "The Auditor's Procedures in Response to Assessed Risks".

³ See ISA 320, "Materiality in the Identification and Evaluation of Misstatements".

9a. The evaluation of the fair presentation of the financial statements as a whole is a matter of professional judgment. In making that judgment, the auditor reflects on whether the financial statements, after any adjustments made by management as a result of the audit process, are consistent with the auditor's understanding of the entity and its environment. The auditor considers the overall presentation, structure and content of the complete set of financial statements. Analytical procedures performed at or near the end of the audit help to corroborate conclusions formed during the audit and assist in arriving at the overall conclusion as to the fair presentation of the financial statements. The auditor also considers whether the financial statements, including the note disclosures, faithfully represent the underlying transactions and events in a manner that gives a true and fair view of or presents fairly, in all material respects, the information conveyed in the financial statements.

Attempt to better explain the “standback”.

Stronger connection to knowledge of business in ISA 315.

Stronger link to the risk assessments at both assertion and financial statement level. “recognition, measurement and disclosure” of individual transactions, and “presentation and content” from IAS 1 ¶1.

National standards for the “standback” relate the final analytical procedures.

IAS 1 ¶13 links fair presentation to faithful representation, therefore seemed appropriate to move this from paragraph 9)

9b. By definition, the application of financial reporting frameworks that the auditor has determined to be acceptable for general purpose financial statements will, except in extremely rare circumstances, result in financial statements that achieve fair presentation. The financial reporting framework may not specify how to account for and report a particular transaction or event, but ordinarily provides sufficient broad guidelines of general application to serve as a basis for developing and applying accounting policies that are consistent with the concepts underlying and requirements of the framework. Thus, the financial reporting framework provides a context for the auditor's opinion on whether the financial statements give a true and fair view or are presented fairly, in all material respects. The auditor makes these judgments by considering the entity's compliance with specific requirements of the financial reporting framework and the fair presentation of the financial statements as a whole. In some circumstances,

To explain that most acceptable frameworks achieve fair presentation.

To convey thought that additional disclosures to those mandated in the framework are not unusual. Keep this separate from the “override”.

failure to disclose relevant information not specifically contemplated by the financial reporting framework, or in extremely rare

10. In extremely rare circumstances, compliance with a specific requirement in the framework ~~itself~~, may result in financial statements that are so misleading that they fail to give a true and fair view of (or present fairly, in all material respects) for example, in the case of financial statements prepared in accordance with International Financial Reporting Standards (IFRS), the financial position, financial performance or cash flows of the entity. In these circumstances, the auditor discusses with management its responsibilities under the financial reporting framework. Some Most financial reporting frameworks for general purpose financial statements acknowledge that there may be circumstances when it is necessary for the financial statements to disclose information not specifically contemplated by the financial reporting framework, or that there are extremely rare circumstances when it is necessary for the financial statements to depart from a specific requirement in the framework in order to achieve the objective of fair presentation of the financial statements. Those financial reporting frameworks often and provide guidance on the disclosures required in such circumstances. Other financial reporting frameworks, however, may not provide any guidance on these circumstances.

Focus on
“override”
only.

11. If the auditor encounters circumstances that leads the auditor to conclude that compliance with a specific requirement results in financial statements that are misleading irrespective of the requirements of the financial reporting framework, the auditor discusses the matter with management and considers the need to modify the auditor's report, which will depend on how management addresses the matter in the financial statements and how the financial reporting framework deals with these rare circumstances (see ISA 701, “Modifications to the Independent Auditor's Report”). Ultimately, the auditor is guided by the ethical responsibility to avoid being associated with information where the auditor believes that the information contains a materially false or misleading statement, or omits or obscures information required to be included where such omission or obscurity would be misleading.⁴ Accordingly, in making a final judgment on the matter, the auditor needs to be satisfied that the information conveyed to readers in the financial statements together with the auditor's report is not misleading.

Since most acceptable frameworks for general purpose financial statements include an override, put emphasis on circumstances that “lead auditor to conclude” rather than imply it is an assertion to be proved or disproved.

12. ~~The auditor's report should be in writing and should contain a clear expression of the auditor's opinion on the financial statements. [Note: the first part of this bold lettered requirement has been moved to precede ¶ 51. The second part has been moved to ¶ 4.)~~

⁴ See paragraph 2.2 in Section 2 of the “Proposed Revised Code of Ethics for Professional Accountants” July 2003 Exposure Draft.

The Auditor's Report

51a. The auditor's report should be in writing.

51b. A written report encompasses both reports issued in hard copy format and those using an electronic medium.