

The Auditor's Responsibilities Relating to Other Information

Background

1. At the December 2013 IAASB meeting, a number of Board members expressed support for an alternative approach to the objectives of the auditor to be stated in proposed ISA 720 (Revised), and indicated that broad agreement on the objectives was needed before the IAASB could finalize the ISA. This perspective was the subject of limited IAASB discussion at the closing stages of the December 2013 IAASB meeting.

Inputs to the Task Force's Deliberations

2. Subsequent to the December 2013 IAASB meeting, the ISA 720 Task Force discussed revisions to proposed ISA 720 (Revised), including the objectives of the auditor.¹
3. In relation to the objectives in particular, the Task Force also took the opportunity to gain a further understanding of the perspectives and concern of those IAASB members who supported an alternative approach to the objectives. The following broadly summarizes the Task Force's understanding of what these IAASB members believe the objectives should convey:
 - (a) The objectives should address the auditor's consideration of whether the other information is materially inconsistent with the financial statements, because such inconsistencies may undermine the credibility of the audited financial statements and the auditor's report thereon (including that an inconsistency may indicate that the financial statements are materially misstated).
 - (b) The objectives should focus the auditor on meeting the auditor's ethical obligations not to be knowingly associated with other information that is otherwise misleading.
 - (c) The objectives should not be primarily focused on the auditor identifying material misstatements in the other information. Nonetheless, the auditor would need to respond to concerns regarding the other information itself that arise in the course of the auditor's work in addressing (a) and (b) above.

However, if the objectives are also to reflect the auditor's consideration of the other information in light of the auditor's knowledge gained during the course of an audit (i.e., an "intelligent read"), the objectives should be drafted so as to avoid giving the impression that the auditor would need to perform an exhaustive search of the audit documentation to identify any such inconsistencies.

- (d) The reporting objective should focus on transparency being provided about the auditor's work regarding the other information, rather than on increasing the credibility of the other information itself.

¹ In its discussions, the Task Force took into account comments made at the December 2013 IAASB meetings, and also considered reactions to the US Public Company Accounting Oversight Board's proposed rule addressing other information. Comment letters received by the PCAOB are available at pcaobus.org/Rules/Rulemaking/Pages/Docket034Comments.aspx.

Proposed Revised Objectives

4. In response to these inputs, the Task Force has redrafted the objectives of the auditor for proposed ISA 720 (Revised). The proposed revised objectives are presented below. (For reference, the objectives proposed in the December 2013 IAASB meeting papers are provided in the Appendix.)

Objectives

The objectives of the auditor are to:

- (a) Read the other information and perform certain limited procedures to consider whether there is an apparent material inconsistency between the other information and the financial statements or the auditor's knowledge gained during the course of the audit, because such an inconsistency may undermine the credibility of the financial statements and the auditor's report thereon;
- (b) Respond appropriately when the auditor identifies such an apparent material inconsistency or when, in light of the auditor's knowledge gained during the course of the audit, the auditor becomes aware that other information is apparently materially incorrectly stated or is otherwise misleading; and
- (c) Report in accordance with this ISA.

Discussion

5. The Task Force has aimed to write the objectives in a way that will assist the auditor in understanding what the requirements of the ISA are intended to achieve, whilst also making clear how the objectives link to those requirements. In doing so, the objectives:
- Emphasize the auditor's consideration of whether the other information is materially inconsistent with the financial statements, and why this consideration is important.
 - Reflect the need for the auditor's consideration to be based on an "intelligent read."
 - Acknowledge that the auditor would need to respond to concerns regarding the other information itself that may arise in the course of the auditor's work.
6. The following further explains key aspects of the proposed objectives:
- (a) *"Read the other information and perform certain limited procedures..."*

This phrase is included in order to convey the intended level of work effort in ISA 720 (Revised).

The phrase "perform certain limited procedures" is intended to apply only to the auditor's consideration of the consistency between the other information and the audited financial statements (the "consistency check") in part (a) of the objective. It is not intended to signal that procedures are required to consider the consistency of the other information with the auditor's knowledge gained during the course of the audit nor to signal required procedures to identify material misstatements in the other information itself.

The Task Force notes that some respondents to the PCAOB's proposed rule noted that the phrase "read...and evaluate" implied too strong a work effort, as the term "evaluate" is typically used in the US auditing standards in connection with procedures that result in

obtaining sufficient appropriate audit evidence to support reasonable assurance – which is not the intention of ISA 720 (Revised).

The Task Force notes that the approach being taking for this aspect of objectives is similar to that used in the objective of ISA 250, which also references the work effort requirements in the objectives.

- (b) *“...there is an apparent material inconsistency between the other information and the financial statements or the auditor’s knowledge gained during the course of the audit...”*

The Task Force agrees that the objectives should acknowledge the need for the auditor to consider whether an apparent material inconsistency exists between the other information and the financial statements. However, the Task Force also believes that this should include an “intelligent read” – and therefore, consideration of the consistency of the other information with the auditor’s knowledge gained during the course of the audit.

The revised objectives focus the auditor on whether there are ‘apparent’ material inconsistencies. The term “apparent” is preferred by the Task Force rather than directing the auditor to consider whether there ‘may be’ material inconsistencies, which could suggest too low a threshold for requiring a response to resolve the inconsistency. The Task Force noted that some have commented that using “apparent” as meaning only inconsistencies that are very obvious, but the Task Force believes that the term will convey the concept of “seeming so” to the auditor and is therefore appropriate in light of the intended work effort.²

Further, the term “apparent” is used to signal that an exhaustive search of the audit documentation is not required to complete the intelligent read – although the auditor may refer to audit documentation when memory alone is insufficient.

- (c) *“...because such an inconsistency may undermine the credibility of the financial statements and the auditor’s report thereon”*

This phrase highlight that the principal work carried out under ISA 720 (Revised) relates to the auditor’s responsibilities in connection with the engagement to audit the financial statements.

Notwithstanding this, as discussed below, the Task Force notes that an outcome of the audit of financial statements and the ISA 720 work effort may be an improvement in the quality of the other information when, based on the required work effort of that ISA, the auditor is able to identify material inconsistencies with their knowledge gained during the course of the audit.

- (d) *“Respond appropriately... when, in light of the auditor’s knowledge gained during the course of the audit, the auditor becomes aware that other information is apparently materially incorrectly stated or otherwise misleading”*

This phrase signals that the auditor’s response to an apparent material misstatement in the other information is not only triggered when the auditor identifies inconsistencies that undermine the credibility of the financial statements, but also when the auditor identifies, based only on the auditor’s knowledge gained during the course of the audit, that there is an apparent material misstatement of the other information. The auditor is not required to

² Apparent is defined as “clearly visible or understood” or “seeming real or true, but not necessarily so.”

perform procedures to obtain evidence about whether the other information is materially misstated, beyond the evidence required to form the audit opinion.

For purposes of the objectives, the Task Force has used the phrase “*apparently materially incorrectly stated or otherwise misleading*” in place of the term “materially misstated” or the phrase “material misstatement of the other information.” This is intended to make an implicit link to the auditor’s ethical obligation to avoid association with misleading other information. It also avoids using “misstatement” in the objective which – when read absent the context provided by the definitions, requirements and application material of the ISA – could be mistakenly understood as implying a greater work effort on the other information than intended.^{3,4}

7. The Task Force does not believe that the objectives of the auditor to be stated in ISA 720 (Revised) should explicitly direct the auditor to achieve the auditor’s ethical obligations not to be knowingly associated with other information that is otherwise misleading. The Task Force concluded that: (i) by itself, the auditor’s ethical obligations may set too low a bar for the need to respond to concerns in the other information; and (ii) a single ISA is not able to provide all the requirements that might be necessary to fulfill the auditor’s ethical obligation, and obligation which originates outside of the ISAs.
8. Rather, the Task Force believes that the auditor’s ethical obligation is most appropriately discussed in the Scope section of the standard. Accordingly, it proposes to relocate the wording previously in paragraph 9 of proposed ISA 720 (Revised) to the Scope paragraphs to recognize that this obligation provides context for the whole of ISA 720 (Revised).

Matter For IAASB Consideration

The IAASB is asked for its views on whether the proposed objectives are clear and appropriate and, accordingly, whether it supports the proposals of the Task Force.

³ The Task Force believes that “incorrect presentation” of the other information, which was used in the Task Force’s previous draft of the definition of a misstatement of the other information, is encompassed by the use of the term “incorrectly stated or otherwise misleading.” A conforming change will be proposed to the definition of a material misstatement of the other information.

⁴ The Task Force will continue to use the term “misstatement of the other information” in the requirements and application material of ISA 720 (Revised) as shorthand to avoid overcomplicating the requirements and application material when the concept is used repeatedly, as sometimes happens multiple times in a single sentence of the remainder of the ISA.

Appendix

For Reference Purposes only: Objectives of Proposed ISA 720 (Revised) Per the December 2013 IAASB Meeting Papers

8. The objectives of the auditor, having read the other information taking into account relevant audit evidence obtained and conclusions reached during the course of the audit, are to:
 - (a) Respond appropriately when the auditor identifies:
 - (i) An apparent material misstatement of the other information; or
 - (ii) That there may be a material misstatement in the financial statements; and
 - (b) Report in accordance with this ISA.
9. This ISA may also assist the auditor in complying with relevant ethical requirements⁵ that require the auditor to avoid being knowingly associated with other information that the auditor believes contains a materially false or misleading statement, statements or information furnished recklessly, or omits or obscures information required to be included where such omission or obscurity would be misleading.

⁵ See paragraph 110.2 of the International Ethical Standards Board for Accountants' *Code of Ethics for Professional Accountants*.