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12 December 2008

By e-mail only

Dear Sirs

Exposure Draft: Proposed ISA (UK and Ireland) 700 (Revised) – The Auditor’s Report on Financial Statements

We welcome the opportunity to comment on this proposed ISA (UK and Ireland).

We continue to believe that, in the interests both of international convergence and of minimising the frequency of changes, APB should:

- make no change to the current standard, providing report examples showing the changes from the Companies Act 1985 to the Companies Act 2006. We note that APB has now provided these in APB Bulletin 2008/8;
- on adoption of the clarity standards as a whole for use in the UK, include the clarity version of ISA 700, providing a consistent report in all countries that have adopted clarity ISAs; and
- use the thoughts and ideas developed from the recent consultation to contribute to the IAASB’s future work on the form of the audit report and to any development by the European Commission of a single European audit report.

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However, we appreciate the position that APB has now reached and that it now envisages adopting a new standard for use for periods ending on or after 5 April 2009. We therefore set out in the appendices our detailed responses on this basis to the questions set out in the consultation paper. If you wish to discuss our comments please contact Martyn Jones (020 7007 0861) or Richard Gillin (020 7007 0202).

Yours faithfully

A handwritten signature in black ink that reads "Deloitte LLP". The signature is written in a cursive, slightly slanted style.

Deloitte LLP

Appendix 1

Responses to questions set out in the consultation paper

Question 1 – The APB invites comments on:

- (a) the proposed ISA (UK and Ireland) 700 (Revised) on pages 15 to 31;**
- (b) the proposed “Statement of the scope of an audit and the auditor’s responsibilities in respect of a publicly traded company incorporated in the United Kingdom”, on pages 33 to 39, which it is intended would be posted to the APB’s web site; and**
- (c) the example auditor’s reports on pages 11 to 14.**

Proposed ISA (UK and Ireland) 700

We believe that the right course for APB would be to adopt the now current version of ISA 700, rather than to diverge from this standard and then have to reconsider the approach again when the European Union decides to adopt either the ‘clarity’ version of that standard or some other form of standard European audit report. This would contribute to efforts to minimise the differences throughout the world and improve cross-border understanding of audit reports.

However, we appreciate the position that the APB has come to in considering the results of the consultation exercise and on that basis, we are broadly supportive of APB’s proposed standard, statement and example reports. Our comments on the detailed drafting of these documents are set out in appendices 2-4.

We are strongly supportive of the inclusion of paragraphs 5 and 6 which set out the depth of the auditors’ consideration of the truth and fairness of accounts before issuing an unqualified audit opinion. Whilst we believe that auditors already consider all of these factors in practice under the existing standard, including these as bold requirements sends a strong message to critics of the audit profession who believe that auditors take a ‘box-ticking’ approach to compliance with the relevant accounting standards as their only consideration when forming their opinion.

Statement of the scope of an audit and the auditors’ responsibilities and specimen report

We believe that the proposed “Statement of the scope of an audit and the auditor’s responsibilities in respect of a publicly traded company incorporated in the United Kingdom” provides a useful description of an audit and the auditor’s responsibilities. The comments of preparers referred to in the feedback paper included with the exposure draft note that the need for a detailed explanation has reduced as a result of the recent debates on the topic of director and auditor responsibility. However, in time the memory of these debates will fade and the provision by APB of a summary on their website will provide a useful reference. We are aware that some institutional investors have commented that existing reports are already too long and consisting largely of wording designed to minimise prospective liability; they may consequently regard the longer statement on APB’s website as compounding the problem. We believe that such arguments are wrong as APB’s statement does not contain any additional descriptions of the limitations of an audit and of the auditor’s responsibility; rather the additional material is helpful in setting out the factors that the auditor must consider, as a minimum, before forming their opinion. We believe this section to be particularly helpful as:

- the work of the Audit Quality Forum indicated that some readers of audit reports are surprised at the low number of qualified audit opinions and that there is a perception that this is because auditors set a high threshold before qualifying. APB’s explanation reminds users that the auditor considers uncorrected misstatements, and by implication that misstatements identified by the auditor are normally corrected before the opinion is issued; and
- recent debates about the “true and fair” view have indicated that some users of financial statements believe that preparers and auditors take a “box-ticking” approach. Inclusion of paragraphs 5 and 6 in the standard will help address such concerns but public inclusion of these requirements in this statement will assist. The APB’s statement clearly explains why this is not the case and sets out the breadth of the auditor’s consideration before issuing their report.

We are aware, however, that there may be practical difficulties in this approach because:

- each time the responsibilities of the auditors change, a new version will need to be prepared; and
- in situations where APB have not prepared a statement, the auditor may need to reproduce an amended version of the full statement within their audit report or elsewhere in the annual report.

These issues are dealt with in more detail below but we suggest that they be addressed by splitting the statement into two:

- material common to all audit reports (“The Scope of an Audit of Financial Statements Arising From The Requirements of ISAs (UK and Ireland)”) which could be made available on APB’s website; and
- material specific to the type of entity concerned deriving from law and regulations which could be included on APB’s website (where the entity was one for which APB has a description) or in the audit report or elsewhere in the accounts (where they do not).

Question 2 – Do commentators support APB’s proposal of describing the auditor’s responsibilities and the work an auditor typically performs by either:

- (a) cross-referring to standard paragraphs maintained by the APB on its web site; or**
- (b) including a description in the auditor’s report itself?**

As set out in our response to question 1, we recommend splitting the statement into two. This would allow a cross-reference to material standard to all audit reports arising from the ISAs and give auditors the option for material specific to the type of entity in question. Permitting both cross-reference to a standard maintained by APB or inclusion in the auditor’s report itself allows auditors to deal with non-standard audit reports for which APB do not provide an example (e.g. general partnerships which are not subject to statutory audits) or where APB have not yet provided

an updated example (e.g. where company law changes and a company with a short period of account requires a statutory audit).

Question 3 – On pages 41 and 42 the APB sets out a schedule of the range of example statements that it presently intends to post to its web site. Are there any other examples that you believe it is imperative the APB should post to its web site?

Yes:

- AIM companies. Many AIM companies choose voluntarily to comply with corporate governance and to ask the auditors to undertake a review and/or provide a directors' remuneration report and ask for the auditable parts to be audited as if they were a listed company.
- Charities registered in both England and Wales and in Scotland and, once the legislation comes into force, Charitable Incorporated Organisations and charities registered in Northern Ireland.
- Unit Trusts and Open-Ended Investment Companies.
- NHS Foundation Trusts.

Question 4 – In addition to the need for the APB to develop and maintain current examples relating to a number of different types of entity what other practical difficulties do you think might arise from the APB's proposed approach?

If auditors choose to refer to a statement available on APB's website, APB will need to maintain these examples for as long as the accounts are available. As a minimum, the Disclosure and Transparency Rules require that listed companies maintain their annual reports on their website for a period of five years. Continuing changes in legal and regulatory requirements and in auditing standards may result in a large number of different statements that would be required to cover all of the permutations.

In order to reduce the confusion and APB's efforts in maintaining these statements, it would be helpful if the number of changes to requirements could be reduced. Whilst only the changes in auditing standards are within APB's gift, it is worth noting that BERR have committed to making changes to company law on a maximum of two dates each year (6 April and 1 October). It would be helpful if APB could encourage other legislators, regulators and standard-setters to restrict similarly the dates at which changes are made.

Question 5 – Is the wording of paragraph 18 in the Exposure Draft of the proposed ISA (UK and Ireland) 700 (revised) sufficiently generic to apply to all entities that are required to be audited? (In this regard more detail concerning the legal framework applicable to a particular type of entity will be provided in the applicable example "Statement of the scope of an audit and the auditor's responsibilities"). If not please describe any concerns?

No. There are several situations where this will not be appropriate:

- ISA (UK and Ireland) 700 applies to the statutory audits of local authorities in the UK. At present, such reports do not give a true and fair view;
- Many entities in the UK choose to have an audit but do not prepare GAAP-compliant financial statements, and hence do not give a true and fair view.

Unless APB intends to promulgate ISA 800 in the UK which would deal with these situations, APB should reintroduce the requirements of paragraph 16-1 of extant ISA (UK and Ireland) 700 within this section of the proposed standard.

Question 6 – Do you agree that it is logical for the reference to the “true and fair view” to be the final element in the auditor’s opinion on the financial statements? If you disagree what would be your preference for ordering the elements?

We disagree. We believe that the true and fair requirement should be first. This mirrors the requirements of the law and the primacy of the true and fair view, rather than leaving the reader to look through several other opinions before finding it as an afterthought.

Question 7 – Please provide any comments that you may have on the steps set out concerning the APB’s proposed course of action and the proposed timing of those steps (see pages 5 and 6)? Are there any other actions that you believe the APB should be taking?

We have set out above our recommendations that the APB adopts ISA 700 as issued by the IAASB rather than a new ISA (UK and Ireland) 700. However, assuming that APB issues a standard in the form envisaged, we believe that the timetable is appropriate. We would, however, encourage the FRC to provide guidance on the nature of adequate accounting records before the new standard becomes effective and for the standard to describe the nature of “investigations” required by the Act.

Appendix 2

Detailed comments on the drafting of the exposure draft

In addition to the points raised in Appendix 1:

- The end of paragraph 21(a) could be more clearly expressed as “... and the national law that is applicable when using IFRSs and, in the case of the consolidated accounts of publicly traded companies, Article 4 of the IAS Regulation (1606/2002/EC)”, removing the need for footnote 7.
- Paragraph 22. We disagree with the requirement that the second opinion is clearly distinguished from the opinion on the financial statements required by company law. This position made sense when the reference to the accounting framework was combined with the true and fair view. Now that these two responsibilities have been separated and there is no longer any reference to the legally applicable framework as part of the description of directors’ responsibilities, we believe that it is simpler and clearer to add to the relevant bullet of the opinion, for example “have been properly prepared in accordance with IFRSs as adopted by the European Union and as issued by the IASB.” We understand that the SEC has accepted such reports and believe that this provides more clearly an opinion on compliance with the second framework than the existing model as set out in APB Bulletin 2006/6.
- Paragraph 23. We believe that it is important that auditors do not give an opinion on compliance with a second framework without those charged with governance first asserting their compliance with that framework. In addition, some of the differences between frameworks could be dealt with by additional disclosure (for example, during 2007 some companies chose to adopt both IFRS 8 (which was unendorsed) and IAS 14 (as required by law), providing two sets of segmental disclosure). We suggest replacing the second sentence with: “Before giving such an opinion, the auditor considers whether the financial statements clearly explain how they have complied with both frameworks and whether, including any additional disclosure required to achieve such compliance, the financial statements comply with both frameworks.”
- Paragraphs 6(d) and 56 refers to “management”. This should read “those charged with governance”, given that APB is proposing changing “management” to “those charged with governance” everywhere else in the standard.
- Paragraph 72 sets out that the new standard is effective for audits of financial statements for periods ending on or after 5 April 2009. This is inconsistent with APB Bulletin 2008/8 which sets out the APB’s expectation that any new standard will apply for periods beginning on or after 6 April 2008 and ending on or after 5 April 2009. If left as in the exposure draft, certain companies preparing accounts for a period longer than a year will be applying the new standard to reports issued under the Companies Act 1985, for which report examples will not be provided by APB. In addition, it is unclear what auditors of entities other than companies are expected to do and from what date. For example, the statutory auditor reporting requirements mirroring those for limited companies change for Limited Liability Partnerships for periods commencing on or after 1 October 2008.

Appendix 3

Detailed comments on the proposed “Statement of the scope of an audit and the auditor’s responsibilities in respect of a publicly traded company incorporated in the United Kingdom”

In addition to the points raised in Appendix 1:

- The term “management” is used in several places. As this is for a company, we believe this term should be replaced with “directors”. Alternatively, if our suggestion of separating the material common to all audits from that for company audits is adopted, this term should be replaced with “those charged with governance”.
- Footnote 19 refers to APB Bulletin 2001/1. ISA (UK and Ireland) 720 also provides an appendix on electronic publication of the auditors’ report. We note that these two sets of material are inconsistent in certain regards and do not necessarily represent current practice. We believe that including one revised set in an appendix to ISA (UK and Ireland) 700 would be more appropriate. Alternatively, withdrawing all of the material from the standards and preparing an updated Bulletin on electronic publication would provide the flexibility to update the material as regulatory requirements change. Matters that should be considered in updating this material include the following:
 - Legislative references to The Companies Act 1985 (Electronic Communications) Order 2000 are outdated as electronic publication is dealt with in the Companies Act 2006. This material could usefully also deal with the electronic filing requirements of the new Act that Companies House will be implementing from 1 October 2009.
 - The requirement to identify the nationality of the accounting and auditing standards used is now addressed in the body of the standard.
 - Guidance around the separation of the annual report from other website materials does not reflect current practice of using PDF format to reproduce the report in a separate document that is identical to the hard copy annual report and accounts.
 - The majority of websites now contain disclaimers or terms and conditions relating to the use of the website that reduce the risk that the first of APB’s recommended additional footnotes to the report is designed to address.
 - The fact that in essence the accounting and auditing standards applied by public interest entities are basically IFRS and ISAs reduces the risk that the second of APB’s recommended additional footnotes to the report is designed to address.
 - Both of these recommended footnotes appear to address risk management issues. APB does not normally address the risk management activities of the firms. In addition, these footnotes are not common practice in other jurisdictions and are unlikely to be required in any single European audit report.
 - The proposed use of XBRL for certain filings is not addressed in the Bulletin or ISA (UK and Ireland) 720.

- The material on Corporate Governance, together with footnote 21 is technically incorrect. These requirements arise from LR 9.8.11R and LR 9.8.12R. LR 9.1 sets out the applicability of LR9.8 and only applies these provisions to companies with a primary listing of equity shares. It does not apply to other listed companies, including those with only debt securities listed (i.e. outside the scope of LR9), or with only preference shares or convertible shares listed.

Whilst we know that APB's plan requires a completed suite of similar statements to be ready for 5 April 2009, we believe that it would be helpful for a brief exposure period on the other statements to consider their technical correctness once APB has confirmed their approach for this report.

Appendix 4

Detailed comments on the example auditor's reports

We have no specific comments on the drafting of the example auditors' report for a UK publicly traded company, assuming that the company is using IFRS as adopted by the European Union for both its individual and consolidated financial statements. However, we are less clear how this would work where individual accounts are prepared under UK GAAP, nor for other forms of company. Whilst we know that APB's plan requires a completed suite of example reports to be ready for 5 April 2009, we believe that it would be helpful for a brief exposure period on the other reports once APB has confirmed their approach for this report.