

EXPOSURE DRAFT

ED 22/08

(November 2008)

**Proposed Auditing Standard
ASA 720
*The Auditor's Responsibility
in Relation to Other
Information in Documents
Containing Audited Financial
Reports (Revised and
Redrafted)*
(Re-issuance of ASA 720)**

Issued for Comment by the **Auditing and Assurance Standards Board**

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Australian Government

Auditing and Assurance Standards Board

Commenting on this Exposure Draft

Comments on this Exposure Draft should be forwarded so as to arrive by no later than 1 December 2008. Comments should be addressed to:

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A copy of all non-confidential submissions will be placed on public record on the AUASB website: www.auasb.gov.au.

Obtaining a Copy of this Exposure Draft

This Exposure Draft is available on the AUASB website: www.auasb.gov.au. Alternatively, any individual or organisation may obtain one printed copy of this Exposure Draft without charge until no later than 1 December 2008 by contacting:

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The Auditor's Responsibility in Relation to Other Information in Documents Containing Audited Financial Reports (Revised and Redrafted) (Re-issuance of ASA 720)

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PREFACE

Reasons for Issuing ED 22/08

The Auditing and Assurance Standards Board (AUASB) is proposing to re-issue Auditing Standard ASA 720 *Other Information in Documents Containing Audited Financial Reports* pursuant to the requirements of the legislative provisions and the Strategic Direction explained below.

The AUASB is an independent statutory board of the Australian Government established under section 227A of the *Australian Securities and Investments Commission Act 2001*, as amended (ASIC Act). Under section 336 of the *Corporations Act 2001*, the AUASB may make Australian Auditing Standards for the purposes of the corporations legislation. These Auditing Standards are legislative instruments under the *Legislative Instruments Act 2003*.

The International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC), has undertaken a programme to redraft, in “clarity” format, the entire suite of International Standards on Auditing (ISAs). In some cases, and in accordance with normal practice, the ISAs have been revised in addition to being redrafted. The redrafted ISAs are effective for audits of financial statements for periods beginning on or after 15 December 2009.

Under the Strategic Direction given to the AUASB by the Financial Reporting Council (FRC), the AUASB is required to have regard to any programme initiated by the IAASB for the revision and enhancement of the ISAs and to make appropriate consequential amendments to the Australian Auditing Standards. Accordingly, the AUASB has decided to revise and redraft the Australian Auditing Standards using the equivalent redrafted ISAs.

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Main Proposals

This proposed Auditing Standard establishes mandatory Requirements and provides Application and Other Explanatory Material regarding the auditor's responsibility in relation to other information in documents containing audited financial reports and the auditor's report thereon.

Proposed Operative Date

It is intended that this proposed Auditing Standard will be operative for financial reporting periods commencing on or after 1 January 2010.

Main changes from existing ASA 720 *Other Information in Documents Containing Audited Financial Reports* (April 2006)

The main differences between this proposed Auditing Standard and the Auditing Standard that it supersedes, *ASA 720 Other Information in Documents Containing Audited Financial Reports* (April 2006), are included in the Tables of Differences provided as an attachment to this Exposure Draft.

Request for Comments

Comments are invited on this Exposure Draft of the proposed re-issuance of Auditing Standard ASA 720, *Other Information in Documents Containing Audited Financial Reports* by no later than 1 December 2008. The AUASB is seeking comments on the main changes from the existing ASA 720. In addition, respondents are asked to consider and respond to the following questions:

1. Have applicable laws and regulations been appropriately addressed in the proposed standard?
2. Are there any references to relevant laws or regulations that have been omitted?
3. Are there any laws or regulations that may, or do, prevent or impede the application of the proposed standard, or may conflict with the proposed standard?

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4. What, if any, are the additional significant costs to/benefits for auditors and the business community arising from compliance with the main changes to the Requirements of this proposed Auditing Standard? If there are significant costs, do these outweigh the benefits to the users of audit services?
5. Are there any other significant public interest matters that constituents wish to raise?

The AUASB prefers that respondents express a clear opinion on whether the main changes to the Requirements of this proposed Auditing Standard are supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on the above matters. The AUASB regards both supportive and critical comments as essential to a balanced review of the Auditing Standard.

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AUTHORITY STATEMENT

The Auditing and Assurance Standards Board (AUASB) makes this Auditing Standard ASA 720 *The Auditor's Responsibility in Relation to Other Information in Documents Containing Audited Financial Reports (Revised and Redrafted)* pursuant to section 227B of the *Australian Securities and Investments Commission Act 2001* and section 336 of the *Corporations Act 2001*.

This Auditing Standard is to be read in conjunction with ASA 100 *Preamble to Auditing Standards (Revised and Redrafted)*, which sets out the intentions of the AUASB on how the Australian Auditing Standards are to be understood, interpreted and applied.

AUDITING STANDARD ASA 720

The Auditor's Responsibility in Relation to Other Information in Documents Containing Audited Financial Reports (Revised and Redrafted)

Application

- Aus 0.1 This Auditing Standard applies to:
- (a) an audit of a financial report for a financial year, or an audit of a financial report for a half-year, in accordance with the *Corporations Act 2001*; and
 - (b) an audit of a financial report for any other purpose.
- Aus 0.2 This Auditing Standard also applies, as appropriate, to an audit of other historical financial information.

Operative Date

- Aus 0.3 This Auditing Standard is operative for financial reporting periods commencing on or after 1 January 2010.

Introduction

Scope of this ASA

1. This Auditing Standard deals with the auditor's responsibility in relation to other information in documents containing audited financial reports and the auditor's report thereon. In the absence of any separate requirement in the particular circumstances of the engagement, the auditor's opinion does not cover other information and the auditor has no specific responsibility for determining whether or not other information is properly stated. However, the auditor reads the other information because the credibility of the audited financial reports may be undermined by material inconsistencies between the audited financial reports and other information. (Ref: Para. A1)
2. In this Auditing Standard "documents containing audited financial reports" refers to annual reports (or similar documents), that are

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issued to owners (or similar stakeholders), containing audited financial reports and the auditor's report thereon. This Auditing Standard may also be applied, adapted as necessary in the circumstances, to other documents containing audited financial reports, such as those used in securities offerings. (Ref: Para. A2-A4)

Effective Date

3. [Deleted by the AUASB. Refer Aus 0.3]

Objective

4. The objective of the auditor is to respond appropriately when documents containing audited financial reports and the auditor's report thereon include other information that could undermine the credibility of those financial reports and the auditor's report.

Definitions

5. For the purposes of the Australian Auditing Standards, the following terms have the meanings attributed below:
- (a) Other information – Financial and non-financial information (other than the financial reports and the auditor's report thereon) which is included, either by law, regulation or custom, in a document containing audited financial reports and the auditor's report thereon.
 - (b) Inconsistency – Other information that contradicts information contained in the audited financial reports. A material inconsistency may raise doubt about the audit conclusions drawn from audit evidence previously obtained and, possibly, about the basis for the auditor's opinion on the financial reports.
 - (c) Misstatement of fact – Other information that is unrelated to matters appearing in the audited financial reports that is incorrectly stated or presented. A material misstatement of fact may undermine the credibility of the document containing audited financial reports.

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Requirements

Reading Other Information

6. The auditor shall read the other information to identify material inconsistencies, if any, with the audited financial reports.
7. The auditor shall make appropriate arrangements with management or those charged with governance to obtain the other information prior to the date of the auditor's report. If it is not possible to obtain all the other information prior to the date of the auditor's report, the auditor shall read such other information as soon as practicable. (Ref: Para. A5)

Material Inconsistencies

8. If, on reading the other information, the auditor identifies a material inconsistency, the auditor shall determine whether the audited financial reports or the other information needs to be revised.

Material Inconsistencies Identified in Other Information Obtained Prior to the Date of the Auditor's Report

9. When revision of the audited financial reports is necessary and management refuses to make the revision, the auditor shall modify the opinion in accordance with ASA 705 (Revised and Redrafted).¹
10. When revision of the other information is necessary and management refuses to make the revision, the auditor shall communicate this matter to those charged with governance; and
 - (a) Include in the auditor's report an Other Matter(s) paragraph describing the material inconsistency in accordance with ASA 706 (Revised and Redrafted);² or
 - (b) Withhold the auditor's report; or
 - (c) Where withdrawal is legally permitted, withdraw from the engagement. (Ref: Para. A6-A7)

¹ ASA 705 (Revised and Redrafted) *Modifications to the Opinion in the Independent Auditor's Report*.

² ASA 706 (Revised and Redrafted) *Emphasis of Matter Paragraphs and Other Matter(s) Paragraphs in the Independent Auditor's Report*, paragraph [9].

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Material Inconsistencies Identified in Other Information Obtained Subsequent to the Date of the Auditor's Report

11. When revision of the audited financial reports is necessary, the auditor shall follow the relevant requirements in ASA 560 (Redrafted).³
12. When revision of the other information is necessary and management agrees to make the revision, the auditor shall carry out the procedures necessary under the circumstances. (Ref: Para. A8)
13. When revision of the other information is necessary, but management refuses to make the revision, the auditor shall notify those charged with governance of the auditor's concern regarding the other information and take any further appropriate action. (Ref: Para. A9)

Material Misstatements of Fact

14. If, on reading the other information for the purpose of identifying material inconsistencies, the auditor becomes aware of an apparent material misstatement of fact, the auditor shall discuss the matter with management. (Ref: Para. A10)
15. When, following such discussions, the auditor still considers that there is an apparent material misstatement of fact, the auditor shall request management to consult with a qualified third party, such as the entity's legal counsel, and the auditor shall consider the advice received.
16. When the auditor concludes that there is a material misstatement of fact in the other information which management refuses to correct, the auditor shall notify those charged with governance of the auditor's concern regarding the other information and take any further appropriate action. (Ref: Para. A11)

* * *

³ ASA 560 (Revised and Redrafted) *Subsequent Events* paragraphs 10-17.

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Application and Other Explanatory Material

Scope of this Auditing Standard (Ref: Para. 1-2)

- A1. The auditor may have additional responsibilities, through statutory or other regulatory requirements, in relation to other information that are beyond the scope of this Auditing Standard. For example, some jurisdictions may require the auditor to apply specific procedures to certain of the other information such as required supplementary data or to express an opinion on the reliability of performance indicators described in the other information. When there are such obligations, the auditor's additional responsibilities are determined by the nature of the engagement and by law, regulation and professional standards. If such other information is omitted or contains deficiencies, the auditor may be required by law or regulation to refer to the matter in the auditor's report.
- A2. Other information may comprise, for example:
- A report by management or those charged with governance on operations.
 - Financial summaries or highlights.
 - Employment data.
 - Planned capital expenditures.
 - Financial ratios.
 - Names of officers and directors.
 - Selected quarterly data.
- A3. For purposes of the Australian Auditing Standards, other information does not encompass, for example:
- A press release or a transmittal memorandum, such as a covering letter, accompanying the document containing audited financial reports and the auditor's report thereon.
 - Information contained in analyst briefings.
 - Information contained on the entity's web site.

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Considerations Specific to Smaller Entities (Ref: Para. 2)

- A4. Unless required by law or regulation, smaller entities are less likely to issue documents containing audited financial reports. However, an example of such a document would be where a legal requirement exists for an accompanying report by those charged with governance. Examples of other information that may be included in a document containing the audited financial reports of a smaller entity are a detailed income statement and a management report.

Reading Other Information (Ref: Para. 7)

- A5. Obtaining the other information prior to the date of the auditor's report enables the auditor to resolve possible material inconsistencies and apparent material misstatements of fact with management on a timely basis. An agreement with management as to when the other information will be available may be helpful.

Material Inconsistencies

Material Inconsistencies Identified in Other Information Obtained Prior to the Date of the Auditor's Report (Ref: Para. 10)

- A6. When management refuses to revise the other information, the auditor may base any decision on what further action to take on advice from the auditor's legal counsel.

Considerations Specific to Public Sector Entities

- A7. In the public sector, withdrawal from the engagement or withholding the auditor's report may not be options. In such cases the auditor may issue a report to the appropriate statutory body giving details of the inconsistency.

Material Inconsistencies Identified in Other Information Obtained Subsequent to the Date of the Auditor's Report (Ref: Para. 12-13)

- A8. When management agrees to revise the other information, the auditor's procedures may include reviewing the steps taken by management to ensure that individuals in receipt of the previously issued financial reports, the auditor's report thereon, and the other information are informed of the revision.
- A9. When management refuses to make the revision of such other information that the auditor concludes is necessary, appropriate

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further actions by the auditor may include obtaining advice from the auditor's legal counsel.

Material Misstatements of Fact (Ref: Para. 14-16)

- A10. When discussing an apparent material misstatement of fact with management, the auditor may not be able to evaluate the validity of some disclosures included within the other information and management's responses to the auditor's enquiries, and may conclude that valid differences of judgement or opinion exist.
- A11. When the auditor concludes that there is a material misstatement of fact that management refuses to correct, appropriate further actions by the auditor may include obtaining advice from the auditor's legal counsel.

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Conformity with International Standards on Auditing

This Auditing Standard conforms with International Standard on Auditing ISA 720 *The Auditor's Responsibility in Relation to Other Information in Documents Containing Audited Financial Statements* (Redrafted), issued by the International Auditing and Assurance Standards Board (IAASB), an independent standard-setting board of the International Federation of Accountants (IFAC).

Paragraphs that have been added to this Auditing Standard (and do not appear in the text of the equivalent ISA) are identified with the prefix "Aus".

Compliance with this Auditing Standard enables compliance with ISA 720.

Tables of Differences — ASA 720 (Revised and Redrafted) and Extant ASA 720

Underlying Standard

ISA 720 *The Auditor's Responsibility in Relation to Other Information in Documents Containing Audited Financial Statements* (Redrafted) is used as the underlying Auditing Standard for the purpose of re-drafting this proposed Auditing Standard. The underlying Auditing Standard will be amended for the following matters:

- Australian Laws and Regulations (including the *Corporations Act 2001*);
- Changes considered necessary because this Auditing Standard is a legislative instrument; and
- Changes considered necessary in the public interest.

Summary of Main Differences — ASA 720 (Revised and Redrafted) and Extant ASA 720

The table below details the main differences (excluding editorial amendments) between this proposed Auditing Standard and extant ASA 720.

Item #	ASA (Revised and Redrafted) Para. #	ASA (Revised and Redrafted) Requirements	Commentary
Objectives			
1	4	The objective of the auditor is to respond appropriately when documents containing audited financial reports and the auditor's report thereon include other information that could undermine the credibility of those financial reports and the auditor's report.	New Objectives. [Similar to extant Introduction paragraph 9]
Definitions			
2	5	For the purposes of the Australian Auditing Standards, the following terms have the meanings attributed below: (a) Other information – Financial and non-financial information (other than the financial reports and the auditor's report thereon) which is included, either by law, regulation or custom, in a document containing audited financial reports and the	New Definitions. [Similar to extant guidance paragraph 7]

Item #	ASA (Revised and Redrafted) Para. #	ASA (Revised and Redrafted) Requirements	Commentary
		auditor’s report thereon. (b) Inconsistency – Other information that contradicts information contained in the audited financial reports. A material inconsistency may raise doubt about the audit conclusions drawn from audit evidence previously obtained and, possibly, about the basis for the auditor’s opinion on the financial reports. (c) Misstatement of fact – Other information that is unrelated to matters appearing in the audited financial reports that is incorrectly stated or presented. A material misstatement of fact may undermine the credibility of the document containing audited financial reports.	[Similar to extant guidance paragraph 6] [Similar to extant guidance paragraph 19]
Reading Other Information			
3	7	The auditor shall make appropriate arrangements with management or those charged with governance to obtain the other information prior to the date of the auditor’s report. If it is not possible to obtain all the other information prior to the date of the auditor’s report, the auditor shall read such other information as soon as practicable.	Elevation of extant ASA Explanatory Guidance [Extant ASA 720 para 12—equivalent Explanatory Guidance]
Material Inconsistencies			
4	10	When revision of the other information is necessary and management refuses to make the revision, the auditor shall communicate this matter to those charged with governance; and (a) Include in the auditor’s report an Other Matter(s) paragraph describing the material inconsistency in accordance with ASA 706 (Revised and Redrafted); or (b) Withhold the auditor’s report; or	Shaded text is equivalent in meaning to the extant ASA Requirement [para 16]. Note: Extant ASA requires an “Emphasis of Matter” Unshaded text is an elevation of extant ASA Explanatory Guidance.

Item #	ASA (Revised and Redrafted) Para. #	ASA (Revised and Redrafted) Requirements	Commentary
		(c) Where withdrawal is legally permitted, withdraw from the engagement.	[Extant ASA 720 para 17—equivalent Explanatory Guidance]
5	11	When revision of the audited financial reports is necessary, the auditor shall follow the relevant requirements in ASA 560 (Redrafted). [ASA 560 = Subsequent Events]	Elevation of extant ASA Explanatory Guidance [Extant ASA 720 para 27—equivalent Explanatory Guidance]
6	12	When revision of the other information is necessary and management agrees to make the revision, the auditor shall carry out the procedures necessary under the circumstances	Elevation of extant ASA Explanatory Guidance [Extant ASA 720 para 28—equivalent Explanatory Guidance]
7	13	When revision of the other information is necessary, but management refuses to make the revision, the auditor shall notify those charged with governance of the auditor’s concern regarding the other information and take any further appropriate action.	Shaded text is equivalent in meaning to the extant ASA Requirement [para 29]. Unshaded text is an elevation of extant ASA Explanatory Guidance. [Extant ASA 720 para 30—equivalent Explanatory Guidance]
Material Misstatement of Fact			
8	16	When the auditor concludes that there is a material misstatement of fact in the other information which management refuses to correct, the auditor shall notify those charged with governance of the auditor’s concern regarding the other information and take any further appropriate action.	Shaded text is equivalent in meaning to the extant ASA Requirement [para 23]. Unshaded text is an elevation of extant ASA Explanatory Guidance. [Extant ASA 720 para 24—equivalent Explanatory Guidance]