

July 31, 2005

Mr. Jim Sylph  
Technical Director  
International Federation of Accountants  
545 Fifth Avenue, 14th Floor  
New York, NY 10017

Dear Mr. Sylph:

We appreciate this opportunity to comment on the proposed International Standard on Auditing (ISA) 705, *Modifications to the Opinion in the Independent Auditor's Report*, and proposed ISA 706, *Emphasis of Matter Paragraphs and Other Matters Paragraphs in the Independent Auditor's Report*, (the "proposed standards") as developed by the International Auditing and Assurance Standards Board (IAASB). We commend the IAASB for their efforts in developing this guidance and believe that it has adequately addressed considerations related to audits of small entities and public sector entities.

**Comments on "Guide for Commentators":**

With respect to the specific questions outlined in the "Guide for Commentators" in the explanatory memorandum to the exposure draft, our comments are as follows:

- **Question 1 – Should paragraph 33 of ISA 705 be retained, permitting the auditor to issue a disclaimer of opinion when multiple uncertainties exist?**

Yes, we believe that, in addition to ISA 706 requiring an emphasis of matter paragraph when a significant uncertainty is both unusual and of fundamental importance to the user's understanding of the financial statements, it is appropriate to allow the auditor to disclaim an opinion in situations when *multiple* uncertainties exist.

- **Question 2 – Is the use of sub-headings desirable in auditors’ reports with modifications to the opinion, and auditors’ reports with an emphasis of matter paragraph or an other matters paragraph?**

Yes, we believe the use of sub-headings is beneficial, as it appropriately flags modifications to the auditors’ reports, drawing the readers’ attention to the important issues.

- **Question 3 – Do you believe the use of the terms “significant uncertainty” and “material uncertainty” causes confusion?**

No, we do not believe the use of the two terms causes confusion. We support the use of the term “significant uncertainty” in ISA 706.

### **Other Comments on Proposed ISA 705:**

We have no comments on proposed ISA 706. Our specific recommendations for clarifying proposed ISA 705 are described below. Throughout our comments, additions are noted in bold underline and deletions are noted in double-strike through.

In addition to the comments below, we also recommend that proposed ISA 705 include “navigational aids” to help auditors identify the type of report which should be issued based on the circumstances, similar to the ones included in the new UK reporting requirements (see the appendices to the Draft Bulletin 2005/4 issued by the Auditing Practices Board, entitled *Auditor’s Report on Financial Statements*.)

- **Paragraph 8**

In some jurisdictions, the financial reporting framework specifically dictates the presentation and format of the financial statements. We recommend that this paragraph include guidance stating that the auditor modifies the opinion if management does not follow the presentation format required in the financial reporting framework.

- **Paragraph 8, footnote 2**

For clarification purposes, we strongly recommend the following revisions to the footnote:

Footnote 2: A disagreement with management also encompasses the instance where management acknowledges that the financial statements contain a departure from the applicable financial reporting framework but management refuses to amend the financial statements for any reasons, for example, due to ~~such as~~ cost-benefit considerations.

- **Paragraph 15**

This paragraph references ISA 320 on materiality because the application of selected accounting policies may give rise to misstatements which are evaluated based on materiality. We believe that materiality relates to more concepts in the proposed standard than only the “application of selected accounting policies.” Therefore, we recommend that the reference to ISA 320 be moved towards the beginning of the document instead of being limited to paragraph 15.

- **Paragraph 18**

To link the proposed standard with ISA 315, we recommend adding the following to the list of examples of circumstances which may limit the auditor’s ability to obtain sufficient appropriate audit evidence:

- **When substantive procedures alone are not sufficient, but controls are not effective**

- **Paragraph 35(a)**

We recommend that the IAASB define or clarify what is meant by “before the financial statements are finalized,” as this phrase could be interpreted in various ways, for example, when the financial statements are finalized by management, approved by the Board of Directors, or voted on by the shareholders.

- **Paragraph 39**

We suggest including an additional sentence in paragraph 39 to cover situations where the auditor expresses a disclaimer of opinion due to an inability to obtain sufficient appropriate audit evidence about one or several aspects of the financial statements and such inability is material and pervasive, but the auditor has nonetheless obtained sufficient audit evidence to conclude that a material disagreement with management exists about one or several other aspects of the financial statements. Our recommended revision is as follows:

39. The auditor describes in the basis for modification paragraph of the auditor’s report the reasons for all matters that require modification to the opinion, and the effects thereof. For example, even when the auditor expresses an adverse opinion because the auditor concludes that the entity is not a going concern, the adverse opinion does not justify the omission of specific modifications for specific disagreements with management about the recognition, measurement, or disclosure of certain assets and liabilities, for example, the existence of inventory. **Additionally, even when the auditor expresses a disclaimer of opinion because of an inability to obtain sufficient appropriate audit evidence, the disclaimer of opinion does not justify the omission of specific modifications for specific disagreements with management about the recognition, measurement, or disclosure of certain assets and liabilities**

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We would be pleased to discuss our letter with you or your staff at your convenience. If you have any questions, please contact P. Nicholas Fraser at + 1 (212) 492-4118.

Very truly yours,

/s/ Deloitte Touche Tohmatsu