

April 7, 2008

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

Dear Mr. Sylph:

We appreciate this opportunity to comment on proposed International Standard on Auditing (ISA) 501, Audit Evidence Regarding Specific Financial Statement Account Balances and Disclosures, (the “proposed standard”), as developed by the International Auditing and Assurance Standards Board (IAASB).

Throughout this comment letter, within our recommendations for editorial changes, additions are noted in “bold underline” and deletions in “double strike-through.”

RESPONSES TO THE SPECIFIC QUESTION POSED:

Below is our view on the significant matter identified by the IAASB in the exposure draft of the proposed standard.

Do you agree with the proposal to remove the requirement and guidance on auditing the valuation and disclosure of long-term investments?

Yes, we agree with the proposal to remove the requirements and guidance on auditing the valuation and disclosure of long-term investments from ISA 501.

RESPONSES TO THE APPLICATION OF THE CLARITY DRAFTING CONVENTIONS:

1. Are the objectives to be achieved by the auditor, stated in the proposed redrafted ISA, appropriate?

No. Although it is also addressed in ISA 540 (as noted in paragraph A18 of the proposed standard), we believe that valuation should be included in the objective regarding litigation and claims, as the procedures required by the proposed standard address both completion and valuation. Additionally, we believe that the objective should be limited to those litigation and claims that would affect the financial statements. Our proposed revision to paragraph 3(b) is as follows:

*3(b) The completeness **and valuation** of litigation and claims ~~involving the entity~~
in the financial statements; and*

2. Have the criteria identified by the IAASB for determining whether a requirement should be specified been applied appropriately and consistently, such that the resulting requirements promote consistency in performance and reporting, and the use of professional judgment by auditors?

Yes, we believe that the criteria have been applied appropriately and consistently.

OVERALL COMMENT – Future Withdrawal of ISA 501:

We understand that the objective of the IAASB in issuing this proposed standard was to simply redraft extant ISA 501 in accordance with the clarity drafting conventions. However, we believe that it is strange to single out three specific financial statement account balances and disclosures (inventory, litigation and claims, and segment information) for discussion within an ISA (and within those, deal only with certain assertions and not all), and not provide similar detailed guidance on others.

Accordingly, for note as the IAASB develops its *future* agendas, we would support withdrawal of ISA 501 altogether, along with movement of its requirements and guidance as necessary into other places within the standards, for example, ISA 330.

OVERALL COMMENT – Materiality of an Account Balance:

Within the proposed ISA, materiality of the account balance is discussed in some requirements (4 and 8) but not others (5, 6, 7, and 14). We recommend that materiality of specific account balances be addressed consistently throughout the proposed standard. One option would be to include “consideration of the materiality at each inventory count” within paragraphs 5, 6 and 7, as well as “when segment information is material to the financial statements” within paragraph 14. Another option would be to delete reference to “material to the financial statements” in paragraphs 4 and 8, which would be consistent with all other ISAs where materiality is not normally used as a qualifier. Our preference is for the second option, as we believe all ISAs are written to be applicable to material information.

If the first option is selected (including discussion of materiality of account balances), we believe that additional guidance should be included on the materiality of inventory distributed amongst multiple locations. Paragraph 4 requires attendance at the entity's physical inventory count when inventory is material to the financial statements, but does not provide guidance for those situations when the entire inventory balance is material, but it is split between multiple locations. It is not clear whether the auditor is required to attend the physical inventory count at all locations in this circumstance (even if the inventory balance at the individual locations is immaterial), or whether the auditor would be able to avail himself or herself of the "unless impracticable" exception provided in paragraph 7. We recommend that the IAASB include application material to clarify what the auditor would do in this situation. However, if the second option is selected (excluding mention of materiality of account balances), we do not believe that this additional guidance is necessary.

COMMENTS BY PARAGRAPH:

- **Paragraph 8 – Elevation to a Requirement**

We do not agree with the elevation of some of the specific procedures within extant paragraph 18 to proposed paragraph 8. We believe that the auditor should be able to exercise professional judgment about the procedures necessary to obtain sufficient appropriate audit evidence when inventory is under the custody and control of a third party, for example, based on the risk assessment, the auditor could "confirm only," "inspect only," or "both confirm and inspect". Accordingly, we recommend revisions to paragraph 8 as noted below, as well as moving the deleted portions of bullets 8(a) and 8(b) to application material, as examples of audit procedures which may be performed.

8. When inventory under the custody and control of a third party is material to the financial statements, the auditor shall ~~either:~~
~~(a) Request confirmation from the third party as to the quantities and condition of inventory held on behalf of the entity; or~~
~~(b) Perform inspection or other~~ audit procedures appropriate in the circumstances to obtain sufficient appropriate audit evidence regarding the existence and condition of that inventory.

- **Paragraph 9(b):**

Paragraph 9(b) states that the auditor would review correspondence with the entity's external legal counsel. We suggest that application material be added related to this statement, which limits "legal counsel" to only those who would have significant involvement with the financial statements. Otherwise, the auditor may be compelled to review a significant amount of material which is unrelated to the financial statements.

- **Paragraph 10:**

Paragraph 10 requires the auditor to seek direct communication with the entity's external legal counsel, however, in some jurisdictions, this is not permitted. We suggest that application material be added to describe what the auditor would do in such situation.

- **Paragraph A12:**

We believe that, in circumstances where attendance at an entity's physical inventory count is impracticable, one alternative audit procedure would be to perform substantive analytical procedures. Accordingly, we suggest adding the performance of substantive analytical procedures as a second example in this paragraph.

We would be pleased to discuss our letter with you or your staff at your convenience. If you have any questions, please contact Jens Simonsen, Director of Global Audit Services at + 1 212 492 3689 or John Fogarty, Chairman – DTT Assurance Technical Policies and Methodologies Group at + 1 203 761 3227.

Very truly yours,

A handwritten signature in black ink, appearing to read "Jens Simonsen". The signature is written in a cursive style with a large, looped initial "J".