



**ASSOCIATION ACTUARIELLE INTERNATIONALE  
INTERNATIONAL ACTUARIAL ASSOCIATION**

April 29, 2005

Technical Director  
International Auditing and Assurance Standards Board  
545 Fifth Avenue, 14<sup>th</sup> floor  
New York, New York 10017 USA  
(email: [Edcomments@ifac.org](mailto:Edcomments@ifac.org))

Dear Sir:

**Re: IAA comments on Materiality in the Identification and Evaluation of Misstatements**

In response to the request for comments to the IAASB Proposed International Standard on Auditing 320 (Revised), I am pleased to transmit on behalf of the International Actuarial Association (IAA) our comments and recommendations.

We hope that you find the attached comments to be of value.

These comments have been prepared by a committee of the IAA, the members of which are listed by name and association in the Appendix to this submission.

Yours sincerely,

Yves Guérard  
Secretary General

Attachment: IAA comments

# **IAA Comments on IAASB Proposed Revision to ISA 320**

## ***Materiality in the Identification and Evaluation of Misstatements***

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### **THE INTERNATIONAL ACTUARIAL ASSOCIATION**

The International Actuarial Association (the “IAA”) represents the international actuarial profession. Our fifty Full Member actuarial associations represent more than 95% of all actuaries practicing around the world. The IAA promotes high standards of actuarial professionalism around the globe and serves as the voice of the actuarial profession when dealing with other international bodies on matters falling within, or likely to have an impact upon, the areas of expertise and practice of actuaries.

We are not a trade association and do not represent the interests of either clients or employers. As actuaries, we have developed significant experience and expertise in the assessment of the value of contingent cash flows. Using this experience, actuaries will continue to provide assistance to those involved in the enhancement of auditing standards to make them more effective in providing useful and reliable information to users of financial statements.

### **IAA COMMENTS**

The IAA appreciates this opportunity to provide input to the IAASB’s proposed revision to the International Standard on Auditing 320, *Materiality in the Identification and Evaluation of Misstatements*. We commend the continuing, very worthwhile, efforts of the IAASB to enhance its set of international auditing standards.

1. Characterization of misstatements. It would be clearer if the characterization of misstatements, currently given in paragraphs 4, 5 and 31, were reformulated, put in one place and restated. In other words, incorporate the content of paragraph 31 with that of paragraphs 4 and 5. The categorization of misstatements is given in paragraph 31 and appears to be misplaced, being buried in the ISA, while the current paragraph 4 attempts to identify their nature.
  - a. The reference to “can arise from error or fraud” currently in the stem of paragraph 4 would be clarified if it were incorporated in the current paragraph 5. In paragraph 5, there are really three rather than two types of intentional misstatements relevant to the auditor: in addition to the current “fraudulent financial reporting” and “misstatements resulting from misappropriation of assets”, “incurring excessive amounts of obligations and understatement of liabilities” is one as well.
  - b. Paragraph 31 would be better placed to be a new paragraph 4; the current paragraph 4 would be better placed after the current paragraph 5. It is the characterization of misstatement given in paragraph 31 that is used throughout the ISA.
  - c. The current paragraph 4 is a hodgepodge of information regarding misstatements and would be more usefully described differently, as we do not believe that it is the IAASB’s intent to indicate that all misstatements consist of each of the five given characteristics – the end of the current stem to paragraph 4, “may consist of” is incorrect. For example, the quantification of a misstatement can be defined as the current 4(b). 4(c) is a type of misstatement. A misstatement can be either an inaccuracy (4(a)), an omission / misinterpretation (4(d)) or a difference in judgment (4(e)). 4(e) is really a description of 31(a)(ii) and could be combined with it. In addition, 4(d) might be usefully split into two items.

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- d. Based on our experience with the development of estimates, we believe that it might be worthwhile to discuss the concept of refinement of estimates with regards to misstatements. For example, changes in estimates may result from enhancements to judgment regarding an expanded set of available experience, or the development of revised models due to improved technology (e.g., application of stochastic methods).
2. Paragraph 6. We believe that the phrase “in the Context of an Audit” currently in the title of paragraphs 6 and 7 would more appropriately be placed after “Materiality”, the first word in the stem of paragraph 6.

In addition, although defined in IAS, it might provide additional guidance for auditing purposes if an example could be provided as to possible “surrounding circumstances”, e.g., segment reporting.

3. Paragraph 10. Although this paragraph indicates that consideration of specific users be given in the context of the objective of an audit being prepared for a special purpose, it may be useful to clarify that the specific users being considered should be disclosed.
4. Paragraph 12. It might enhance the ISA somewhat if the materiality level determined in the overall audit strategy is characterized as an “initial” or “anticipated” materiality level, as it is likely to change later as the audit progresses, as described in paragraphs 22 through 27. In paragraph 15, the phrase “in the planning process” might be added after the third word, “materiality”.
5. Paragraph 13. The IAASB might consider mentioning or discussing whether materiality might consist of more than one benchmark.
6. Paragraph 14. We are concerned whenever specific benchmarks are referenced, even as examples. Although the values given in the list are introduced as examples and that the auditor may consider “higher or lower” percentages, we do not believe that sufficient emphasis has been provided to indicate that the values shown are not intended to be used as *a priori* benchmarks.
7. Paragraphs 20 and 21. We assume that the phrase “tolerable error” is used rather than “tolerable misstatement” because the concept of “tolerable fraud” is not an appropriate one, as this is the rare reference to error in this proposed revision to ISA 320. If not, then the latter phrase may be more appropriate.

Subsequent to these paragraphs, there are numerous places in which materiality level is referred to as “the materiality level”, where we believe that the concept of “tolerable error” is also appropriate to refer to, e.g., in paragraph 22.

In addition, the footnote on page 11 should be expanded to include “an estimate” as the third example given. The examples do not make clear that this concept applies to both a misstatement in fact and a misstatement involving subjective decisions.

Although the concept underlying tolerable error sounds quite reasonable, we are not certain whether sufficient guidance has been provided to the auditor to determine the types of

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cases to which this concept might apply. We suggest that one or more examples would be helpful.

8. Page 13, footnote 4. We suggest adding something like “significant” after “any” in the fourth line. By definition, there is always some uncertainty involved in any estimate.
9. Paragraph 36(a). Should target error be referred to rather than materiality levels here? The concept described here seems like the same concept described in paragraphs 20 and 21.
10. Paragraph 40, first bullet. We suggest adding a phrase such as “that in the aggregate has created a lack of neutrality in the financial statement.” This would provide needed clarification.
11. Paragraph 40, second bullet. We are very concerned about the implication of this example. It appears to imply that it would be inappropriate for an estimate to be at the end of a reasonable range. It indicates that a material misstatement would occur if (1) a series of estimates consistently lie at one end or (2) when management changes the relative location. Thus bias would be presumed to exist whenever an estimate is the end of the range. We do not believe that this is the intent of this very important bullet point.

In addition, in the reference to “the reasonable range”, it is not clear whether management’s range or the auditor’s range is being referred to. It should be clear whose range is being referred to in each place where reference is made to a range.

12. Public Sector Perspective. Although we understand the reason that the Public Sector section of this proposed revision to ISA 320 was included, we feel that its description can be improved. For example, the auditor of a private sector entity should also consider any applicable legislation or regulation, and the public interest should also be considered by a private entity. Possibly the word “particularly” prior to “consider” in paragraph 1 might make this clearer. In paragraph 2, although the public interest should always be considered, we do not believe that “public interest” is appropriately characterized as an “issue.” We believe that this concern is only one of drafting that should be able to be fixed easily.

Some minor editorial suggestions follow:

1. Paragraph 23, second sentence. It needs a verb, such as “arises” after “operations”.
2. Paragraph 37, fifth bullet. We believe that “materiality” is intended when reference to “significance” is given. Although the statement in the seventh bullet is conceptually correct, many misclassifications between accounts are not significant in the context of a financial statement.
3. Paragraph 37, seventh bullet. “with” might be somewhat better than “having”.
4. Paragraph 40, end of second bullet. We believe that reference to ISA 545 should also be included here.
5. Paragraph 44. The “g” in governance should be capitalized.
6. Paragraph 45(a). The phrase “if applied” could be added after “tolerable error”, as it is not always used.

Again, along with other responders to these proposals, the IAA appreciates the opportunity to express our views regarding the IASC Foundation’s due process procedures and hope these comments add value to the deliberations.

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***Materiality in the Identification and Evaluation of Misstatements***

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**Appendix**

**Members of the IAA's Insurance Accounting Committee**

Sam Gutterman	Chair
W. Paul McCrossan	Vice-chair
Francis Ruygt	Vice-chair
Clive Aaron	Institute of Actuaries of Australia
William Abbott	Institute of Actuaries
Yutaka Amino	Institute of Actuaries of Japan
Victor Hugo Cesar Bagnati	Instituto Brasileiro de Atuária (IBA)
Daniel Barron	Israel Association of Actuaries
Ralph Blanchard	Casualty Actuarial Society
Guy Castagnoli	Association Suisse des Actuaire
Paolo De Angelis	Istituto Italiano degli Attuari
Angie Felipe Checa	Col.legi d'Actuaris de Catalunya
Mark J Freedman	Society of Actuaries
Stephen Handler	Actuarial Society of South Africa
William Hines	American Academy of Actuaries
Burton D Jay	Conference of Consulting Actuaries
Antony John Jeffery	Society of Actuaries in Ireland
Ad A.M. Kok	Het Actuarieel Genootschap
Kurt Lambrechts	Association Royale des Actuaire Belges
Jean-Pierre Lassus	Institut des Actuaire
Kristine Lomanovska	Latvijas Aktuaru Asociacija
W Paul McCrossan	Canadian Institute of Actuaries/Institut Canadien des Actuaire
Richard O'Sullivan	Society of Actuaries in Ireland
Markku Paakkanen	Suomen Aktuaariyhdistys
Venkatarama Rajagopalan	Actuarial Society of India
Nithiarani Rajasingham	Singapore Actuarial Society
Jaanus Sibul	Eesti Aktuaaride Liit
Dieter Silbernagel	Deutsche Aktuarvereinigung e.V. (DAV)
Bjarni Thórdarson	Félag Islenskra Tryggingastærðfræðinga
Tuomo Virolainen	Svenska Aktuarieföreningen
Kevin Yah	Actuarial Institute of the Republic of China
Jesús Zúñiga San Martin	Colegio Nacional de Actuarios A.C.

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**Appendix**

**Full Member Associations of the IAA**

Consejo Profesional de Ciencias Económicas de la Ciudad Autónoma de Buenos Aires (Argentina)  
Institute of Actuaries of Australia (Australia)  
Aktuarvereinigung Österreichs (AVÖ) (Austria)  
Association Royale des Actuaire Belges (Belgique)  
Instituto Brasileiro de Atuária (IBA) (Brazil)  
Canadian Institute of Actuaries/Institut Canadien des Actuaire (Canada)  
Cyprus Association of Actuaries (Cyprus)  
Česká Společnost Aktuárů (Czech Republic)  
Den Danske Aktuarforening (Denmark)  
Egyptian Society of Actuaries (Egypt)  
Eesti Aktuaaride Liit (Estonia)  
Suomen Aktuaariyhdistys (Finland)  
Institut des Actuaire (France)  
Deutsche Aktuarvereinigung e. V. (DAV) (Germany)  
Hellenic Actuarial Society (Greece)  
Actuarial Society of Hong Kong (Hong Kong)  
Magyar Aktuárius Társaság (Hungary)  
Félag Íslenskra Tryggingastærðfræðinga (Iceland)  
Actuarial Society of India (India)  
Society of Actuaries in Ireland (Ireland)  
Israel Association of Actuaries (Israel)  
Istituto Italiano degli Attuari (Italy)  
Institute of Actuaries of Japan (Japan)  
Japanese Society of Certified Pension Actuaries (Japan)  
Latvijas Aktuaru Asociācija (Latvia)  
Lebanese Association of Actuaries (Lebanon)  
Persatuan Aktuari Malaysia (Malaysia)  
Colegio Nacional de Actuarios A. C. (Mexico)  
Het Actuarieel Genootschap (Netherlands)  
New Zealand Society of Actuaries (New Zealand)  
Den Norske Aktuarforening (Norway)  
Actuarial Society of the Philippines (Philippines)  
Polskie Stowarzyszenie Aktuariuszy (Poland)  
Instituto dos Actuários Portugueses (Portugal)  
Academia de Actuarios de Puerto Rico (Puerto Rico)  
Singapore Actuarial Society (Singapore)  
Slovensko Aktuarsko Društvo (Slovenia)  
Actuarial Society of South Africa (South Africa)  
Col·legi d'Actuaris de Catalunya (Spain)  
Instituto de Actuarios Españoles (Spain)  
Svenska Aktuarieföreningen (Sweden)  
Association Suisse des Actuaire (Switzerland)  
Actuarial Institute of the Republic of China (Taipei)  
Faculty of Actuaries (United Kingdom)

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Institute of Actuaries (United Kingdom)  
American Academy of Actuaries (United States)  
American Society of Pension Professionals & Actuaries (United States)  
Casualty Actuarial Society (United States)  
Conference of Consulting Actuaries (United States)  
Society of Actuaries (United States)