

27 November 2009

Mr G Tanzer  
Secretary General  
IOSCO General Secretariat  
Calle Oquendo 12  
28006 Madrid  
SPAIN

**Standard Life Investments**  
1 George Street  
Edinburgh  
EH2 2LL  
**phone: 0131 245 6813**  
fax: 0131 245 6463  
email: [guy\\_jubb@standardlife.com](mailto:guy_jubb@standardlife.com)  
[www.standardlifeinvestments.com](http://www.standardlifeinvestments.com)

**By Post & E-mail: [auditorcommunications@iosco.org](mailto:auditorcommunications@iosco.org)**

Dear Mr Tanzer

## **PUBLIC COMMENT ON AUDITOR COMMUNICATIONS: CONSULTATION REPORT**

Standard Life Investments is a subsidiary of Standard Life plc, a FTSE 100 listed company. It is a leading global institutional investor with assets under management at 30 September 2009 of €149.8 billion. The majority of these assets are invested in securities listed on international stock exchanges.

We are very pleased that IOSCO has taken the initiative to assess the usefulness of the standard audit report and to consult on this issue. As investors we rely heavily on audited financial information to assist us in taking stewardship and portfolio management decisions on behalf of our clients, who are long-term shareholders. Therefore, we attach considerable value to an effective audit process, which we believe is brought to bear at the vast majority of listed companies. However, we have been and continue to be critical of the standard audit report insofar as of itself it adds little or no value when it comes to assisting us in making decisions for stewardship and portfolio management purposes. In our view, the usefulness of the standard audit report is undermined by the use of boilerplate language, excessive use of statements relating to auditor liability limitation, and the binary nature of the audit opinion. These criticisms are usefully highlighted and discussed in your Consultation Report.

We should like to see progress towards more informative audit reports that are tailored to the company concerned so that they enhance the understanding of users of the audited financial information and otherwise assist shareholders in holding boards to account. Accordingly, we are keen that your initiative should deliver useful improvements. We hope that auditing firms and their professional bodies will respond to your initiative in such a way that they embrace its spirit and take positive steps to achieving progress.

### **Comments of Emphasis and Observation from a User's Perspective**

With reference to the content of the Consultation Report, we should like to render the following comments of emphasis and observation to enhance your understanding of our perspective as users of audited financial information.

Standard Life Investments Limited, tel. +44 131 225 2345, a company registered in Scotland (SC 123321) Registered Office 1 George Street Edinburgh EH2 2LL.

The Standard Life Investments group includes Standard Life Investments (Mutual Funds) Limited, SLTM Limited, Standard Life Investments (Corporate Funds) Limited and SL Capital Partners LLP. Standard Life Investments Limited acts as Investment Manager for Standard Life Assurance Limited and Standard Life Pension Funds Limited.

Standard Life Investments may record and monitor telephone calls to help improve customer service. All companies are authorised and regulated by the Financial Services Authority.  
[www.standardlifeinvestments.com](http://www.standardlifeinvestments.com)

- Auditor Liability Concerns - Myth or Reality?

The last decade has witnessed considerable rhetoric, primarily from leading audit firms and networks, regarding what they consider to be the undue burden of auditor liability, which they have often cited as a reason for being unwilling to provide more informative audit reports. In the early years of such rhetoric, we tended to have some sympathy with it, taking the representations at face value. However, as time has gone by, we have witnessed no catastrophic failure of any major global auditing network by virtue of liability considerations and we have observed that shareholders and investors have generally taken a responsible approach to exercising their litigation rights. Accordingly, we are no longer inclined to regard auditor liability reasons as legitimate in defending the status quo of the standard audit report. Furthermore, we should emphasise that in the United Kingdom, statutory provision now exists to enable auditors to limit their liability, subject to the approval of shareholders. In this regard, UK institutional shareholders, including Standard Life Investments, have sent a strong signal that they are willing to consider favourably proposals that seek to limit liability on a proportional basis. However, it is notable that, to our knowledge, no auditor of a major UK listed company has sought to take advantage of these provisions; this serves to reinforce the basis for the shift in our perception of auditor liability.

That said, we recognise the reality that auditors are concerned about liability. Therefore, we encourage IOSCO to encourage legislators and regulators to take steps to enable the principle of proportional liability, which we consider to be fair and reasonable, to be established on a global basis so that there is a level global playing field that would serve to remove a practical barrier to making audit reports more useful.

- Perceived Shortcomings of the Current Standard Audit Report

We support the view set out in the Consultation Report that the criticisms cited therein are compounded by the limited amount of direct communication between auditors and users of financial statements, other than in the standard audit report. In the UK, we hope that the proposed Audit Firm Governance Code will go some way to improving the dialogue between auditors and investors on non-company specific matters. Also, we commend to you the efforts of the Global Auditor Investor Dialogue<sup>1</sup>, which commissioned an independent working group that published enhanced disclosure guidelines relating to audit and risk matters for directors and others. The guidelines are for global application and were endorsed by a number of leading organisations including the International Corporate Governance Network (ICGN) and the Asian Corporate Governance Association (ACGA). They can be found at [www.enhanceddisclosure.org](http://www.enhanceddisclosure.org). A copy is enclosed for ease of reference.

Also, with a sense of conviction, we agree that the usefulness of the current standard audit report is undermined by the binary nature of the opinion and the use of boilerplate and technical language. These aspects detract from effective communication. We should like to see a more enlightened and informative opinion which uses language that is not only tailored to the circumstances but also is understandable by non-accountants.

- Cost Benefit of Improvements

Whilst we believe it would be beneficial to make improvements to auditor communications, we are mindful, from a pragmatic standpoint, of the need to ensure that any additional disclosures are largely derived from the work which auditors are already doing; this will help to ensure that any improvements proposed by IOSCO will not result on an unreasonable cost burden on issuers. In

---

<sup>1</sup> The Global Auditor Investor Dialogue is an informal forum whose members comprise the major global auditing networks and leading global investors and share owners.

assessing the cost benefit of such improvements we urge IOSCO to take a robust approach to challenging claims by audit networks for additional fees.

**Questions to be Addressed in Assessing Whether Changes Should be Made**

Q1. *Are investors receiving inadequate information to make investment decisions? If so, should this information gap be filled? By whom?*

The information gap does genuinely exist; investors receive inadequate audit related information to make appropriately informed investment decisions. In this regard, we should emphasise that 'investment decisions' include not only decisions as to whether or not to buy, sell or hold a security, but also stewardship decisions pertaining to the conduct of the company's affairs.

In our investment decisions, as referred to above, we find that we make increasing use of non-financial, narrative information, such as the management commentary and information pertaining to the company's corporate governance. Also, we make considerable use of information contained on corporate websites and the presentations made by companies at analyst presentations.

In the light of the above, we support the view in the Consultation Report that some of the perceived shortcomings of the standard audit report suggest that investors need more (or better) information to facilitate their investment decisions. We support the view put forward in the Report that some information gaps should be filled through disclosures by issuers rather than auditors. Equally, we believe that auditors should be more willing than is currently the case to attest to (1) the content of certain information issued by a company that is currently not within the scope of the audit and (2) its fair presentation. In this latter regard, we believe that auditors have a useful role to play in ensuring that information provided by issuers is presented objectively and without 'spin'.

Accordingly, we suggest that IOSCO should, in tandem with any recommendations for improving auditor communications, promote and foster the development of guidelines to assist issuers and others in respect of the information that is useful for investors and is not currently included within the scope of the audit. The aforementioned Guidelines for Enhanced Disclosure are illustrative in this regard.

Q2. *For information gaps that should be filled by others, what should be the auditor's role with the additional disclosure?*

To amplify our response to Q1, we should like the auditor to assure shareholders that, in relation to the additional disclosures, they:

- reliably reflects information that is supported by and/or is consistent with underlying books and records or other appropriate verifiable information;
- are reported in a fair and objective manner; and
- are appropriate for inclusion in information provided to and for shareholders.

In the event that, for example, certain aspects of the additional disclosure are not capable of verification by reference to the underlying books and records then this should be noted in the auditor's report if the matter is deemed material. For the avoidance of doubt, we believe that it would be better that such information is reported upon by the auditor in this way rather than not disclosed at all, provided that it is otherwise deemed appropriate for disclosure to shareholders.

One further aspect that we commend for consideration is the auditor's responsibility for ensuring that post-balance sheet date events and trends are properly taken into account by an issuer when presenting information to shareholders. We are concerned that undue emphasis is given to the state of affairs at the balance sheet date without due and prudent regard for post-balance sheet events and trends that might otherwise result in audited information being misleading and unsuitable for decision-making by shareholders and others.

- Q3. *For information gaps that should be filled by the auditor, should changes to the standard audit report be made or are other auditor communications warranted?*

We do not regard the alternatives as mutually exclusive. In other words, we believe there are grounds for changing the standard audit report and for improving other auditor communications. Whilst we wish to see more useful audit reports, we do not wish them to be cluttered by so much information that users cannot see the wood for the trees. For example we commend the use of cross-referencing by auditors to additional information contained on an issuer's website.

We agree that the nature of auditing is not wisely understood by users of audit reports. We note the reference to the IAASB plans to consider whether to develop a communication to users of financial statements on the meaning of an audit. Whilst this may be useful, we believe that communication on such matters is probably best promulgated jointly with a different organisation that is demonstrably independent of standard setters and the major auditing networks. Perhaps IOSCO could play a role in this regard. Alternatively, IOSCO is better positioned than most to identify or set up the body which is best positioned to have responsibility for such communication. We envisage that there is a case for not only developing a 'foundation' communication on the meaning of an audit but also for communicating, in a timely manner, relevant developments pertaining to the audit and assurance environment that would be of genuine interest and use to shareholders and other users of audited information.

- Q4. *What legal, practical and regulatory issues would result from any changes to auditor communication requirements?*

We have commented earlier in this letter regarding our views on auditor liability and auditor liability limitation. Whilst we acknowledge the legal realities and the practical challenges, we are somewhat cynical regarding the evaluation by audit firms of their litigation exposure. Accordingly, we encourage IOSCO to approach its responsibilities in the context of this consultation in a manner which seeks to find ways to enable improvements to be made rather than regarding any legal or practical challenges as immovable impediments to progress.

**Conclusion**

We hope that the views set out in this letter will assist the IOSCO Technical Committee in understanding the needs and views of a major global institutional investor. As well as being pleased to answer any questions that you may have arising from the matters raised in this letter, we are keen to be of continuing assistance. In this latter respect, we should be delighted to provide you with such additional assistance and support as you may reasonably request. Please do not hesitate to contact me if and when you believe we can be of further assistance.

Yours sincerely

Guy R Jubb  
*Investment Director, Head of Corporate Governance  
Standard Life Investments*