

IAASB CAG PAPER



International Federation of Accountants

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Agenda Item

D

Committee: IAASB Consultative Advisory Group

Meeting Location: New York

Meeting Date: March 8-9, 2011

**Draft Minutes of the Public Session of the Meeting of the
INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD
CONSULTATIVE ADVISORY GROUP (CAG)**

Held on September 13-15, 2010

London, United Kingdom

PRESENT

Members

David Damant
Vânia Borgerth

Kristian Koktvedgaard
Nathalie de Basaldúa (September 13)
Jan Robberecht
Federico Diomeda
Jean-Luc Peyret
Hilde Blomme
Philip Johnson
Elena Lobanova
Paul Koster
Robert Roussey
Margie Bastolla
Wayne Upton (September 14-15)
Sam Gutterman (September 14-15)
Peter Windsor
George White
Bengt Hallqvist (September 14-15)
Koichiro Kuramochi
Patricia Sucher
Filip Cassel
Frank Bollmann
Rifaat Karim (September 14-15)
Hayanari Uchino
Gaylen Hansen
David Morris

Chair

Associação Brasileira de Instituições Financeiras de
Desenvolvimento
BUSINESSEUROPE
European Commission
European Commission
European Federation of Accountants and Auditors for SMEs
European Financial Executives' Institutes
Fédération des Experts Comptables Européens
Fédération des Experts Comptables Européens
Graduate School of Financial Management
Gulf States Regulatory Authorities
Information Systems Audit and Control Association
Institute of Internal Auditors
International Accounting Standards Board
International Actuarial Association
International Association of Insurance Supervisors
International Bar Association
International Corporate Governance Network
International Organization of Securities Commissions
International Organization of Securities Commissions
International Organization of Supreme Audit Institutions
International Valuation Standards Council
Islamic Financial Services Board
Japan Securities Dealers Association
National Association of State Boards of Accountancy
North American Financial Executives Institutes

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Dominique Pannier	Organisation for Economic Cooperation and Development
Ajith Ratnayake	Sri Lanka Accounting and Auditing Standards Monitoring Board
Yoseph Asmelash	United Nations Conference on Trade and Development
Simon Bradbury	World Bank
Linda de Beer	World Federation of Exchanges
Thomas Krantz (September 14-15)	World Federation of Exchanges

Observers

Ken Dakdduk (September 13)	International Ethics Standards Board for Accountants (IESBA) Chair
Richard Fleck	IESBA CAG Chair
Martin Baumann*	U.S. Public Company Accounting Oversight Board
Giancarlo Attolini (September 14-15)	IFAC SMP Committee

IAASB

Prof. Arnold Schilder	Chairman
Diana Hillier	Deputy Chair
Phil Cowperthwaite (September 14)	Member
Cédric Gélard (September 15)	Member
Jon Grant	Member
Caithlin McCabe (September 15)	Member (via teleconference for Agenda Item N)
John Fogarty (September 14)	Task Force Chair
Roger Simnett (September 15)	Joint Chair of the ISAE 3410 Task Force (via teleconference for Agenda Item N)

IESBA (Joint Session September 13)

Michael Niehues	Deputy Chair
Robert Franchini	Member
Jim Gaa	Member
Isabelle Sapet	Member
Brian Walsh	Member

Public Interest Oversight Board

Dr. Kai Uwe Marten (September 14-15)

IFAC Staff

Jim Sylph	Executive Director, Professional Standards
James Gunn	IAASB Technical Director
Kathleen Healy	IAASB Senior Technical Manager
Brett James	IAASB Technical Manager
Jan Munro (September 13)	IESBA Deputy Director
Michael Nugent (September 15)	IAASB Technical Manager

* Views expressed by PCAOB representatives represent their views and do not necessarily reflect the view of the PCAOB Board or other Board members or staff.

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APOLOGIES

Members

Han Fang	Asian Financial Executives' Institutes
Conchita Manabat	Asian Financial Executives' Institutes
Marc Pickeur	Basel Committee on Banking Supervision
Matthew Waldron	CFA Institute
L. Nelson Carvalho	Chairman of the Standards Advisory Council of the IASB
Georges Couvois	European Financial Executives' Institutes
Gerald Edwards	Financial Stability Board
Dr. Obaid Saif Hamad Ali Al Zaabi	Gulf States Regulatory Authorities
Susan Koski-Grafer	International Organization of Securities Commissions
Frank Bollman	International Valuation Standards Council
Norio Igarashi	Japanese Financial Services Agency

IAASB

Craig Crawford	Member
Prof. William Kinney	Member

Public Interest Oversight Board

Gonzalo Ramos

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SEPTEMBER 13, 2010¹

Joint Session of the IAASB and IESBA CAGs – Monitoring Group Review (Item A)

To DISCUSS the Monitoring Group Review as it pertains to the CAG, including a discussion of the recommendation about the timing of the CAG meetings.

Mr. Fleck introduced the session, noting its purpose was to discuss the sections of the Monitoring Group's (MG) Consultation Paper (CP) pertaining to the CAGs. He then invited Ms. Erhardt to present on behalf of the MG. Ms. Erhardt introduced Ms. van Diggelen and Messrs. Pickeur and Windsor, attending the session in their capacity as MG Task Force (TF) members.

Ms. Erhardt briefed the Representatives on the progress of the CP. She noted that, while the comment period closed in mid-August, the MG continues to receive responses. She also noted that there had not yet been a significant response from investors, but that the MG continues to reach out to obtain additional input. The TF's intent is to present the final recommendations at the World Congress of Accountants in November.

Ms. Erhardt explained that the purpose of the report is not intended to be a referendum on the past but rather a reflection on what the best way forward could be within the current IFAC governance structure. She noted the aim of the consultation was to understand whether the 18 MG recommendations were valid. The style of the final report has not yet been decided.

RECOMMENDATION 7²

Ms. Erhard explained that respondents had questioned what this recommendation was intended to cover. She noted that the MG's questions related to the role of the CAGs in the overall structure of IFAC and in relation to the Public Interest Oversight Board (PIOB). In her view, clarification was first needed to determine whether the CAGs were meant to have more of a managerial role or a governance role to clarify how the CAGs are meant to advise the Public Interest Activity Committees (PIACs). For example, because the PIOB looks to the CAGs to give comfort as to the due process being followed in standard-setting, this may be seen to be playing a governance role, which is not mentioned in the CAGs' Terms of Reference (ToR). On the other hand, the practice of the CAGs discussing most significant matters being addressed by the PIACs may lead to the impression that the CAGs are undertaken a more managerial-type role, when in fact in may be more beneficial for the CAGs to have deeper discussions on a few issues rather than the PIACs' broad agendas. The TF's view that it will be important to come to a common understanding as to what the CAGs role is and then adjust the operating aspects accordingly.

¹ The minutes present the discussions in the order that they were taken. This may not be the same as that indicated on the agenda.

² As noted in Agenda Item A.1, recommendation 7 notes "The Monitoring Group recommends that IFAC revise the manner in which the CAGs determine their agenda items, the manner in which discussion matters are presented to the CAGs, and the manner in which the CAG input is summarized and presented to Board members so that the approaches used do not appear to go beyond the CAG's technical advisory input role."

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The Representatives commented as follows:

- Mr. Damant noted that he and Ms. de Beer had submitted a response to the MG, included in the agenda material as Agenda Item A.2. In his view, the observations and conclusions drawn in relation to Recommendation 7 are incorrect. He noted that the original IFAC reform documents had initially proposed that the CAG have a role in judging whether due process had been followed overall, however, this proposal was later removed as the IAASB CAG did not support doing so. Mr. Damant explained that the PIOB then asked the CAG Chairs to comment on the due process as it related to the CAGs. More recently, the PIOB has given the CAGs a role in advising the Chairs in commenting on due process as it related to the CAGs, a matter which was discussed by the CAGs in March 2010. In his view, as this change was requested and made by the PIOB, it warrants separate discussion apart from the MG review.
- A number of Representatives were concerned that the observations supporting recommendation 7 may have been made by those who had not formally observed the work of the CAGs.
- Mr. Damant, supported by Mr. White, also noted his view that the IAASB CAG's work to date is entirely in line with its ToR. He believed that what the IAASB CAG has achieved to date has been valuable to the IAASB. He was also of the view that organizations that have expressed an interest in the IAASB CAG have been welcomed, and that efforts have been made to increase the geographic representation of the IAASB CAG as well. Ms. Erhardt explained that the report was not intended to be a review of the work of the CAGs to date, but rather an opportunity to reevaluate the structure and operations of not only the CAG, but also other parts of IFAC's structure.
- Mr. White suggested that the discrepancies between what the CAG members believe their role is and what outsiders may perceive as the role of the CAG may be resolved through enhanced communications. Mr. Damant strongly recommended that, should recommendation 7 be maintained, that the MG also develop specific recommendations about the overall structure and roles of the CAGs which they believe would be more appropriate, or suggest how external perceptions could be corrected.
- Mr. Roussey was of the view that Recommendation 7 was very difficult to read. In his view, the role of the CAG is to provide technical advice, which is aided by the Report Back mechanism. This mechanism allows the CAG Representatives to see how the CAG's advice is being received by the PIACs, including whether or not points they have raised have been taken up by the PIACs and, if not, why. He believed that where the CAGs were of the view that the standards being developed were not of high quality, the CAGs would notify the PIOB. This would seem to be within the remit of the CAGs in providing advice on technical matters.
- Mr. Fleck noted that he believes his role as the IESBA CAG Chair is not to provide a technical sign-off on the content of the *Code of Ethics for Professional Accountants*, but to advise the IESBA on issues and to confirm to the PIOB whether there has been appropriate interaction between the CAG and the IESBA. He acknowledged that at times the CAG may not have agreed with the technical content of the code, but believed its role was to express

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views to the IESBA, and receive feedback on whether these points had been taken up in the final Code. In doing so, he believed the CAG had expressed its satisfaction that its counterparties (i.e., the IESBA and PIOB) have executed their respective roles as they relate to the CAG. He suggested that the MG's final report could make clearer the anticipated roles of the CAGs, the PIACs and the PIOB in the development of the standards so that their respective responsibilities were better understood by the public.

- Mr. Diomeda did not agree with the statement within the MG's report that a lack of understanding of the role of the CAGs could "give the appearance of a greater degree of credibility to audit standards and the Ethics Code than is warranted." In his view, the Representatives appreciate that their role is not to take responsibility for the standard-setting process, but rather to enhance the degree of discussion within the process. Mr. Cassel agreed that this is the current role, but noted that certain Member Organizations (MOs) like INTOSAI may be hesitant to be directly connected with a formal clearance of the standards.
- Mr. Fleck suggested the final MG report should address the CAGs' attention to whether the PIACs' agendas are appropriately addressing the public interest. In his view, the IESBA CAG pays particular attention to this in advising the IESBA.

RECOMMENDATION 8³

The Representatives commented as follows:

- Mr. Damant noted the point raised that the volume of papers for a CAG meeting equals or exceeds the volume of papers for a Board meeting is incorrect in the case of the IAASB CAG. He clarified that, within the IAASB CAG papers, links to the IAASB papers are provided, for reference only. On rare occasions, an IAASB paper may be made into an IAASB CAG paper if it is very relevant.
- Mr. Damant also did not believe the manner in which the IAASB CAG comments are relayed to the IAASB was correctly stated. He noted that most of the TF Chairs are present during the IAASB CAG discussions, and draft minutes of the CAG meeting are provided to the TF Chairs prior to the IAASB's discussions, despite the limited time in between the meetings.
- Mr. Damant suggested that timing of the CAG meetings has worked out well in his view, and supported continuing the current model because the Chair and TF Chairs can report back to the IAASB on a timely basis. However, he acknowledged the incoming CAG Chair may wish to consider the matter further. Mr. Fleck noted the practical challenges that would result if the CAG meetings and Board meetings were scheduled farther apart, in that it might restrict the progress of the Board's agenda and result in the CAGs not discussing the most up-to-date thinking of the TFs and Boards. Ms. Erhardt suggested there may be further ways to

³ As noted in Agenda Item A.1, recommendation 8 notes "The Monitoring Group recommends that IFAC revise the approach to CAG meeting content to provide for a more realistic and effective participation approach on the part of CAG members and revise the approach to the CAG meeting process to provide for the submission of final CAG meeting minutes to the Board members before the Board meeting in which they discuss the related topics."

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take advantage of technology, and changes in how the meetings are structured may allow for the Representatives to have more time to collect relevant input from their MOs. Mr. Fleck noted that the IESBA CAG had conducted a meeting via teleconference that was not without difficulty.

- Mr. Diomeda noted the challenges of the timing of the CAG papers, but acknowledged this was due to the need for adequate time between Board meetings to develop the papers. In his view, the concerns over reduced time for Representatives to discuss the papers with their constituents is somewhat mitigated by the fact that the CAGs often discuss topics on several occasions over the life of a project. In his view, he would not support reducing the amount of CAG papers to accommodate concerns over timing.

GENERAL COMMENTS

Mr. Fleck invited the Representatives to comment further on any matters not yet discussed, or matters that had not been addressed in the MG report which, in their view, warranted further attention.

The Representatives commented as follows:

- Mr. Koktvedgaard inquired as the MG's process for reporting back on the comment letters received. Ms. Erhardt explained that all responses will be made publicly available, and that the MG is considering whether to develop a feedback statement to accompany the final report.
- Ms. de Beer acknowledged Ms. Erhardt's point that the MG's focus is to look forward as to how the processes can be improved. However, in her view, it is important for the final report to highlight current practice and offer the MG's views on whether the original reforms have resulted in significant improvements. Without this context, Ms. de Beer feared the resulting report would be received quite negatively by the wider business community when in fact she believes many would support what the CAGs and IFAC had accomplished to date. Mr. Fleck agreed, noting he would not want the report to be perceived as indicating that IFAC's standard-setting activities had failed over the past five years. Messrs. Johnson and Roussey also agreed, noting that while it may be appropriate for the report to be forward-looking, care should be taken to ensure that the successes of IFAC are adequately addressed to balance the 18 recommendations. Ms. Erhardt noted the MG's intent was to acknowledge what had been done in response to the reforms, but in her view the final report should focus on what IFAC's objectives are for the next five years (for example, continuous improvement and implementation), and what needs to change in order to accomplish these objectives.
- Mr. Roussey questioned the recommendations relating to the balance between practitioners and non-practitioners, including the proposals to discontinue reserving seats for Forum of Firm (FoF) nominees and potentially providing stipends to attract public board members. In his view, while it is important to have non-practitioner representation, suggesting that a majority of the Boards be non-practitioners seems to imply that practitioners are not being independent, which he did not believe to be the case. He noted that initiatives such as the International Accounting Standards Board (IASB) liaison, which expects the IAASB

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members to have accounting knowledge as well as auditing, leads him to believe that there is a very high level of skill required to be on the IAASB. These activities may not be best served by looking to non-practitioners who have to be paid to participate. In his view, the Transnational Auditors Committee (TAC) and FoF have been critical to the development and adoption of the ISAs. If their seats are taken away, it may give a message that this input has not been meaningful without suggesting who might be able to provide the necessary skill sets. Ms. Erhardt responded that their participation would still be needed, however the MG was suggesting that their financial contributions should not necessarily guarantee seats on any Board. Within the four recommendations about composition of the Boards, Ms. Erhardt noted the message was the need to determine the balance between auditing skills and other relevant perspectives in setting the standards.

- Mr. Koktvedgaard questioned the recommendation about the process by which the Boards provide direct feedback to individual MG members if their input will not be taken up in a final standard. Ms. Erhardt explained the original reforms contemplated the possibility of this additional report back, although it has been done informally over the past five years. Mr. Damant agreed that the CAG meetings were not the appropriate venue for the dialogue between the PIACs and individual MG members to take place on points raised in their comment letters. Ms. Erhardt also noted that some respondents to the CP did not support having a provision for special interest groups to receive direct responses to their comments.

SEPTEMBER 14, 2010

Welcome and Approval of Minutes of Previous Meeting (Item B)

To APPROVE the minutes of the March CAG meeting.

OPENING REMARKS

Mr. Damant welcomed the Representatives, including Mr. Windsor, the new International Association of Insurance Supervisors (IAIS) Representative. He welcomed new Member Organizations (MOs) and Representatives: Ms. Borgerth of the Associação Brasileira de Instituições Financeiras de Desenvolvimento (ABDE), Messrs. Hansen and Pannier of the National Association of State Boards of Accountancy (NASBA) and the Organisation for Economic Cooperation and Development, respectively. He also welcomed Mr. Marten as the Representative of the PIOB; IESBA Chair, Mr. Dakdduk; Mr. Jusuf, attending in place of Dr. Manabat; Ms. Lang, accompanying Mr. Diomeda and Mr. James, observing on behalf of the International Organization of Securities Commissions (IOSCO).

Mr. Damant noted with pleasure that many of the IAASB Task Force Chairs would be in attendance to present to the CAG. He also noted that this would be his last meeting as Chair of the CAG, and that the incoming Chair, Ms. Linda de Beer, will take office on October 1, 2010.

MINUTES OF THE PREVIOUS MEETING

Mr. Damant confirmed that the minutes of the previous meeting reflected the comments received from the Representatives. The minutes were approved.

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Limited Assurance (Item C)

To RECEIVE a paper on the Board's general views and direction on limited assurance, that will be implemented in various ISAEs, and comment on these principles.

Ms. Hillier explained that the purpose of this session was to draw together the three IAASB projects on the CAG agenda that touch on limited assurance, being ISRE 2400,⁴ ISAE 3000,⁵ and ISAE 3410,⁶ in advance of the individual discussions.

Ms Hillier briefed the Representatives on the differences between limited assurance engagements and reasonable assurance engagements, with a focus on engagement risk, evidence gathering, the nature, timing and extent of the practitioner's procedures, and the respective opinions and reports. Ms. Hillier noted that the respective Task Forces have attempted to frame the limited assurance opinions in a positive form but have not been able to develop satisfactory wording. Ms. Hillier also explained the difference between limited assurance engagements and agreed-upon procedures (AUP) engagements relates to the exercise of the practitioner's judgment. She noted that limited assurance engagements require a certain level of understanding of the entity, as well as "triggers" that direct the auditor to perform further or additional procedures, and judgment is required to determine what further or additional procedures should be performed. Ms. Hillier noted that that the practitioner's conclusion about the subject matter is formed based on the evidence obtained, and a summary of work performed on limited assurance engagements is critical to users' understanding of the practitioner's opinion.

Ms. Hillier summarized by noting that all limited assurance engagements do not provide the same level of assurance, will not necessarily include the same types of procedures (particularly in new or emerging areas), and the conduct of engagements for a particular subject matter may not always be the same. Mr. Cowperthwaite illustrated this by noting that under proposed ISRE 2400, if the procedures are performed as specified in the standard then a report may be issued. This was different from both ISAE 3000 and ISAE 3410, which focus on limited assurance as being less than reasonable assurance.

The Representatives commented as follows:

- Mr. Hallqvist and Mr. Damant asked what drove the demand for these standards. Ms. Hillier noted that there is significant market demand for limited assurance services. Mr. Johnson noted that entities may also be able to acquire lower cost funding if their financial information has been assured. Mr. Johnson further commented that the introduction of audit exemptions in Europe had increased demand for limited assurance engagements. He related some of the findings of a Fédération des Experts Comptables Européens (FEE) study, including noting that Denmark used to subject every company to audit but now exempts some entities from audits entirely, but that some banks and regulators are working on new

⁴ International Standard on Review Engagements (ISRE) 2400, *Engagements to Review Financial Statements*

⁵ International Standard on Assurance Engagements (ISAE) 3000, *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*

⁶ ISAE 3410, *Assurance on a Greenhouse Gas Statement*

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limited assurance requirements to maintain some assurance over these entities' financial reporting. He also noted that Switzerland has a mandatory review if an entity does not have an audit. Mr. Johnson commented that the IAASB needed to act quickly to give countries a standard to converge with. Mr. Ratnayake agreed with Mr. Johnson, noting that there is market demand for limited assurance engagements for small- and medium-sized entities (SMEs) and for AUP engagements.

- Mr. Johnson noted that FEE has prepared a report on assurance on a corporate governance statement. From that report Mr. Johnson noted that assurance does not increase in a straight line, rather assurance increases in blocks which was made clear by Ms. Hillier's presentation.
- Ms. Sucher, Mr. Johnson and Mr. Kocktvedgaard noted that the market, including regulators and users, has a lower level of understanding of limited assurance compared to reasonable assurance and that it was difficult for the market to understand what has been done without additional education. Ms. Sucher and Mr. Kocktvedgaard supported standards that defined procedures rather than defining limited assurance as a level of assurance less than reasonable assurance. She also noted that another myth regarding limited assurance engagements was that limited assurance engagements are preferable for areas where the subject matter is challenging. Ms. Hillier agreed, noting her view that limited assurance was not appropriate if the subject matter was not understood. Mr. Gutterman noted that there seems to be a consensus about users' level of understanding of limited assurance and that a survey of users to gauge their level of understanding of negative form conclusions is needed.
- Mr. Damant indicated that there were many outside the profession that believed that all audits were forensic audits. Mr. Baumann noted that both IAASB and U.S. Public Company Accounting Oversight Board (PCAOB) standards consider fraud detection as part of an audit, and that both boards consider reasonable assurance to be a high level of assurance that the financial statements as a whole are free of material misstatement, whether due to fraud or error.
- Mr. Peyret asked if there was feedback from particular countries or from bankers in relation to trying to rely on limited assurance reports. He also asked if there were any civil or criminal liability implications of using limited assurance rather than reasonable assurance. Ms. Hillier responded by saying that this was a debate for particular jurisdictions. Ms. Hillier noted that in Canada, for example, there are professional obligations and firm quality control obligations but the legal implications depend on whether the mandate arises from law or contract.
- Mr. Peyret noted that SMEs are likely to prefer having International Financial Reporting Standards for Small and Medium-Sized Entities (IFRS for SMEs) financial statements audited under the same rules as full IFRS financial statements.
- Mr. Kocktvedgaard noted his view that a negative form of conclusion was not appropriate, while acknowledging the difficulties in developing a positive form of conclusion. Mr. Kocktvedgaard asked whether it was possible for a practitioner to issue a positive form of opinion that is less than a full audit under ISAs, noting that there is a proposal in Denmark to express a positive form opinion without having conducted full audit procedures. He

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suggested the IAASB needs to determine who the users are and what they need in a particular engagement; in his view, users want a positive phrased assurance report that they understand. Mr. Koktvedgaard noted that the IASB had encountered the same challenge before undertaking IFRS for SMEs, but that the ISAs attempt to do with wording of the opinions what the IASB does by branding of the standards. Mr. Krantz agreed with Mr. Koktvedgaard and noted that examples of different reports would help inform the debate. Ms. Hillier acknowledged his points but noted that, while the IAASB cannot specify a particular metric for reasonable assurance, it has determined that reasonable assurance is obtained when engagement risk is reduced to an acceptably low level. As such, it is difficult to give a range for reasonable assurance. She also noted that the ISRE 2400 Task Force has made numerous attempts to find positive language for a limited assurance engagement but none have been acceptable: they have either been too similar to the reasonable assurance opinion or have not articulated the concept appropriately. Mr. Johnson noted that it was important to understand the context of the Danish positive form report: they did try to develop an engagement with reasonable assurance, but that commentators from outside of Denmark were not supportive and that the Danish parliament rejected the standard. Mr. Koktvedgaard clarified that the Danish government decided not to include the standard in the proposal that went to the Parliament, so the Parliament has not voted on the standard. Mr. Damant also noted that some non-practitioners did not endorse the negative form of opinion.

- Mr. Attolini noted that there may be difficulties in understanding the differences between the different levels of assurance. He further commented that he continues to believe there might be some merit for a positive form of conclusion. While negative assurance may be appropriate for medium-sized enterprises, a limited assurance engagement of a small enterprise is close to a reasonable assurance engagement as the percentage of transactions reviewed is normally quite high. Mr. Diomeda also supported a positive form conclusion as he does not believe that SMEs will want an engagement with a negative form conclusion due to user expectations. Ms. Hillier explained that there are jurisdictions which have accepted negative forms of assurance for some time and, while it is important to not underestimate the challenges, it is possible to explain what is intended by a negative form of conclusion.
- Mr. Ratnayake noted that there is substantial variation in limited assurance engagements from client to client, and asked whether it is possible to standardize the level of assurance to facilitate comparability. Ms. Hiller responded by noting that standardization is difficult for limited assurance engagements due to the range such assurance encompasses. However, the IAASB is addressing this by looking at what procedures would be performed in particular limited assurance engagements.

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Review and Compilation Standards – ISRE 2400 and ISRS 4410⁷ (Item D)

To DISCUSS matters highlighted by the Task Force since the last CAG meeting or brought forward by CAG Representatives at previous meetings and obtain further input from the CAG.

Mr. Cowperthwaite introduced the topic noting a few overall themes considered by the Task Force in developing the two draft standards:

- The revisions take into account a “think small first” approach, as the standards will be applicable to a wide variety of entities, especially very small entities. However, this is not to say that larger entities may not also request review and compilation engagements.
- Both standards have been drafted to be stand-alone, meaning they address all the necessary requirements without the need for reference to be made to the ISAs.
- While existing standards in these areas exist, the revisions also aim to enhance the value these services to users. Accordingly, appropriate differentiation needs to be made among audits, reviews and compilations to manage the expectations gap of users.

REPORT BACK

Mr. Cowperthwaite drew attention to matters noted in the report back in the CAG agenda material.

COMPILATION ENGAGEMENTS

Mr. Cowperthwaite noted the Task Force was seeking the views of the Representatives on the scope of the standard, in particular the activities undertaken by the practitioner in a compilation engagement. He explained that the focus of the requirements in the standard is on activities that relate to assisting management of the entity in presenting the financial information in accordance with the applicable financial reporting framework.

The Representatives were also asked for their views on how the proposed standard defines the “applicable financial reporting framework” and management’s responsibilities to identify and select the applicable financial reporting framework for use in the compilation engagement. Mr. Cowperthwaite also drew attention to the proposed requirement in paragraph 35 of Agenda Item D.1. He explained that this proposal was intended to give flexibility to the entity and practitioner. For example, if during a compilation engagement amounts to be presented were deemed to be misleading (for example, if a capital lease should be recorded differently under a particular financial reporting framework), this could be rectified by changing the applicable financial reporting framework to another framework, such a special purpose framework, with the concomitant reporting implications.

⁷ International Standard on Related Services (ISRS) 4410, *Compilation Engagements*

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The Representatives commented as follows:

- Mr. Damant supported the flexibility in the standard, which acknowledges that smaller entities may use frameworks other than IFRS or U.S. Generally Accepting Accounting Principles (GAAP).
- Mr. Morris did not agree with the proposal. He noted that under the standards of the US Auditing Standards Board (ASB), if a practitioner performing a compilation engagement noted an exception, the exception would be reported in the practitioner's report rather than allowing for a change in the financial reporting framework or resigning from the engagement. In his view, given that compilations are a fairly significant activity of the accounting profession, it is not in the public interest to require that practitioners always resign if the financial statements being compiled would be misleading. Rather, exception reporting should be permitted to allow for completion of the engagement if the client does not agree to change the financial information. Mr. Ratnayake did not support allowing exception reporting, because the financial statements would be misleading if the user had not read the practitioner's report. It is also undesirable for the practitioner to be associated with financial information not prepared in accordance with the financial reporting framework.
- Mr. Attolini suggested the standard could give guidance on who is responsible for preparing estimates in the compiled financial statements. Mr. Johnson recommended the standard be more explicit about the process by which the practitioner communicates with management and those charged with governance, on both general matters and topics such as the application of accounting policies. In his view, significant communication should take place at the beginning of a compilation engagement, but this communication should also continue throughout the engagement.
- Mr. Attolini questioned whether the requirement in paragraph 35 of Agenda Item D.1 is meant to address circumstances in which the practitioner questions the existence of a going concern. If not, he suggested this could be made clearer in the proposed standard. Mr. Cowperthwaite explained that this was not meant to allow for the entity to adjust the financial reporting framework to avoid addressing going concern issues. ~~Mr. Koltvedgaard questioned whether it is appropriate to allow management to choose whether or not to address going concern.~~ Mr. Johnson suggested that it may be appropriate to acknowledge that management's selection of the appropriate financial reporting framework also depends on whether there is a going concern issue, and that it would be helpful to have the standard emphasize this early in the document.
- Mr. Attolini suggested the use of the word "ordinarily" in describing that management or those charged with governance has responsibility for determining the financial reporting framework is not necessary, in that it is unclear who else would have this responsibility.

The Representatives were asked for views on the purpose and form of the practitioner's compilation report. Mr. Cowperthwaite explained that the illustrative reports included in Agenda Item D.1 are meant to show examples of the different types of financial reporting frameworks that may be used in a compilation engagement.

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- Mr. Koktvedgaard noted that the objective of the compilation engagement is not fully reflected in the illustrative reports. He suggested the report could be redrafted using language in the objective and requirements of the standard to more positively describe what the practitioner had done, to assist the reader in understanding what work has been performed and what the objective of a compilation engagement is. He provided some suggested wording for consideration. Mr. Diomeda supported this view, suggesting that the current form appears to be more similar to a disclaimer.
- Mr. Baumann suggested that performing compilation engagements exposed firms to significant reputational risk. In his view, to mitigate this, it is necessary to explicitly state in the report that the practitioner does not have any understanding whether the information (i.e., the underlying data) compiled in the financial statements is materially misstated. Mr. Koktvedgaard agreed and offered some suggested wording.
- Mr. Hansen suggested the phrase “on management’s behalf” could be deleted in the illustrations, and be replaced with language describing what the practitioner is responsible for.
- Mr. Johnson suggested Illustration 3 in Agenda D.1 was likely to be the most common form of reporting for compilation engagements and should be placed first. Messrs. Attolini and Hansen supported this. In Mr. Johnson’s view, as this illustration addresses significant accounting policies, it is a more appropriate illustration on which to focus to promote the knowledge and wider user of compilations, and strengthen the debate about the importance of including cash flow and other information. In his view, Illustration 1 was unlikely, and reversing the presentation would show how the first example could be further restricted. Mr. Cowperthwaite explained that Illustration 1 was put first in accordance with the Task Force’s view to “think small first,” and in many cases the compilation may be part of a hybrid engagement.
- Mr. Roussey suggested that when financial statements do not include notes, reference to this exclusion should be made within the report, as most frameworks require notes to the financial statements. Mr. Cowperthwaite explained that the terms of engagement would outline the financial reporting framework to be used, as agreed by the practitioner and management. Mr. Roussey noted other users of the report, such as suppliers, likely will not have access to the engagement letter and would benefit from it being made clear in the report.
- Mr. Hansen also noted that the U.S. has a different view in regard to independence for compilation engagements. He suggested the illustrations should note that the practitioner *complies with* ethical standards rather than observing them. He also questioned why the concept of independence was not highlighted in the report. In his view, if independence is considered not to be present because of the nature of a compilation engagement, then the report should clearly state that the practitioner is not independent. Mr. Cowperthwaite explained that independence in regard to a compilation engagement is not defined in the IESBA *Code of Ethics for Professional Accountants* (the IESBA Code) and, accordingly, the practitioner has no basis for reporting whether he or she is independent. Mr. Johnson noted

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that the requirement of the IESBA Code for the practitioner to not be associated with misleading information is a safeguard on which users of the report. Mr. Hansen suggested it could be confusing to readers of the report if independence is not addressed.

- Mr. Koktvedgaard suggested the report could be more explicit in explaining to users what is meant by the reference to quality control and relevant ethical requirements and be more positive about what compliance with these standards involves. He provided some suggested wording for consideration. Mr. Attolini agreed, noted it may be useful to make a clear statement within the report as to which ethical requirements were applicable.
- Mr. Hansen also suggested the report could note that the auditor does not express any form of assurance rather than specifically referencing expressing an opinion or conclusion. He also suggested the illustrations alternated references to financial statements or financial information. Mr. Diomeda did not believe the report needed to emphasize that the practitioner does not express an audit opinion or review conclusion because it is clear that it is a compilation engagement. In his view, this may be misleading as readers may not understand the concepts of audit opinions or review conclusions. Mr. Cowperthwaite noted the Board had determined that a clear statement of differentiation was important, but agreed that the wording could be refined. Mr. Ratnayake supported making this distinction.
- Mr. Attolini noted that the proposed standard assumes ISQC 1⁸ is in place but does not explicitly require it to be. In his view, if there is a requirement that ISQC 1 needs to be in place, SMEs will need a longer implementation period. He suggested the IAASB should consider whether the concepts of scalability and proportionality can be applied to ISQC 1 to assist small and medium practices (SMPs) doing compilation work. Mr. Cowperthwaite noted that the standard states that it is premised on ISQC 1 while not explicitly stating that the practitioner has to have implemented it in order to perform compilation engagements. He also shared his view that the only requirement in ISQC 1 that may pose challenges in the SMP context is the initial documentation of the system of quality control. ~~Mr. Robberecht noted that, while the European Commission does not plan to adopt ISQC 1, the phrase in the standard “or national requirements that are at least as demanding” should address Mr. Attolini’s concern.~~ Mr. Damant suggested it should be made clearer within the standard whether the IAASB expects ISQC 1 to be implemented when not required by national law.
- Mr. Johnson questioned whether the restriction of the standard to engagements only where the practitioner is issuing a report is clear in the standard. In his view, some small practitioners may routinely do what they consider to be compilation engagements to which this standard may not always apply. Mr. Attolini suggested the standard could be more explicit in stating which types of circumstances would not be covered by this standard.

⁸ International Standard on Quality Control (ISQC) 1, *Quality Controls for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

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REVIEW ENGAGEMENTS

Mr. Cowperthwaite noted the procedures of a review engagement are designed to allow the practitioner to obtain sufficient appropriate evidence to form a conclusion. The Representatives were then asked for their views on the practitioner's objective in a review of financial statements.

The Representatives commented as follows:

- Ms. Sucher did not agree with the use of the phrase “to perform procedures” in the objective. In her view, it would be more appropriate to state “to obtain limited assurance.” Mr. Cowperthwaite explained that since the concept of limited assurance is not defined, it would be difficult to make reference to it in the objective of the standard. Mr. Hansen suggested the phrase simply could be deleted.
- Mr. Kuramochi suggested that the concept of information being meaningful to users could be articulated in the objective.
- Mr. Koktvedgaard questioned whether the omission of the concept of fair presentation from the objectives was deliberate. Mr. Cowperthwaite confirmed this was the case, explaining that the standard could also be applied to a compilation framework. Mr. Damant suggested this could be further clarified in the standard.
- Mr. Attolini reported the view of the SMP Committee that further differentiation needs to be made between audits, reviews, and compilations, and that a communications approach could be developed for this purpose. In his view, practitioners may be performing reviews and compilations but not referring to them as such, as the terms may translate well. Mr. Sylph reminded the Representatives that the concepts of review and compilation have existed for many years and standards are currently available to practitioners to meet the market demand for these services. These standards have also been translated.
- Mr. Hansen suggested the term sufficient appropriate *review* evidence could be defined to differentiate it from the concept of sufficient appropriate audit evidence. He also suggested the phrase in the objective which makes reference to matters coming to the practitioner's attention could be deleted. In his view the objective is obtain evidence and form a conclusion.

Mr. Cowperthwaite explained that, after significant debate, the IAASB has concluded that the negative form of assurance is appropriate for a review engagement. However, he noted that, within the report, there is a now a more positive statement of what has been done by the practitioner. It also states that “the nature and extent of procedures performed in a review is substantially less than that performed in an audit conducted in accordance with International Standards on Auditing. Accordingly, we do not express an audit opinion on these financial statements.” The Representatives were also asked for their views as to the form of the practitioner's conclusion in a review engagement.

OTHER COMMENTS

Mr. Cowperthwaite reported that the proposed approval of the review standard is planned for December 2010. Mr. Diomeda expressed his view that the review and compilation projects

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should continue to move together.

Mr. Koktvedgaard encouraged the IAASB to explicitly seek comments on the understandability of the practitioner's reports for both types of engagement during the exposure process.

Auditing Complex Financial Instruments – IAPS 1000⁹ – Including the Status and Authority of the IAPS (Item E)

To DISCUSS matters highlighted by the Task Force since the last CAG meeting or brought forward by CAG Representatives at previous meetings and obtain further input from the CAG.

Mr. Fogarty introduced the topic, explaining that the Task Force had reorganized the document into two sections to respond to comments from the IAASB at its June 2010 meeting. Section I of the document now includes background and informational material designed to be useful to auditors who are not as familiar with complex financial instruments.

Mr. Fogarty noted the challenge in drafting a practice statement whose purpose is not only application to audits of complex financial instruments in the financial services industry, but also to all entities, including SMEs. He explained that certain topics may not be covered in extensive detail in light of the current length of the pronouncement, and the objective of having broader guidance aimed at a broad audience.

Regarding Section II of the document, Mr. Fogarty noted the emphasis on management's process for valuing complex financial instruments.

REPORT BACK

Mr. Fogarty drew attention to matters noted in the report back in the CAG agenda material. In particular, he noted the Task Force's discussions with experts about whether to include further guidance on auditing financial liabilities. He reported that, while the experts were of the view that own credit risk in relation to financial liabilities was important, they concluded that it would be difficult to address the topic in a meaningful way in the IAPS given its complexity.

The Representatives commented as follows:

- Mr. Gutterman, speaking on behalf of the Working Group, was of the view that own credit and non-performance risk should be addressed in the IAPS or in another form. He suggested that, if this could not be done in advance of exposure, then the Task Force should develop the wording in anticipation of receiving further comments on the matter during exposure. Mr. Damant agreed. Ms. Sucher suggested a recent UK Financial Services Authority (FSA) discussion paper on the fundamental review of trading activity regulation may be helpful in this regard, as it provides commentary about issues that arise in own credit risk. Mr. Fogarty noted that the Task Force recognized that own credit risk is an important issue but was of the view that it might unbalance the document to attempt to deal with the topic comprehensively.

⁹ International Auditing Practice Statement (IAPS) 1000, *Special Considerations in Auditing Complex Financial Statements*

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However, he noted that it may be possible to include a description of own credit risk to highlight its importance. Ms. Sucher suggested this could address the inconsistent accounting treatment in practice and alert the auditor of the emphasis made in the accounting standards.

STATUS AND AUTHORITY OF THE IAPS

Mr. Fogarty drew the Representatives' attention to the description of the IAPS authority which had been approved by the IAASB at its June 2010 meeting. He noted that an IAPS is not intended to create new requirements, but rather to educate and assist auditors in applying the requirements in the ISAs when dealing with complex financial instruments, in particular the requirements of ISA 540.

The Representatives commented as follows:

- Mr. Attolini noted that the SMP Committee has some concern about the length of the document, and believes that the IAPS is not likely to be relevant in most SME audits. He expressed concern that SMPs would need to read the document to determine its relevance. He appreciated that paragraph 5 of the proposed IAPS clarified that “In particular, this IAPS does not deal with simple financial instruments such as cash, trade accounts receivable and trade accounts payable” but, in his view, this was inconsistent with other material in paragraph 3 of the proposed IAPS that noted that “Many of the considerations in this IAPS can also be applied to simpler financial instruments.” He suggested the Task Force could better align these views within the IAPS, as there is a concern that regulators in some jurisdictions may expect SMPs to apply the IAPS to simpler financial instruments. Mr. Gutterman suggested this could be clarified within the Scope Section rather than the Background Section. Mr. Fogarty explained that the intent of the statement on the authority of the IAPS is not that the auditor has to read every IAPS that exists, but rather to determine which IAPSs may be relevant. The paragraphs referred to by Mr. Attolini were intended to identify ways in which an auditor could discern whether the IAPS applies. Mr. Fogarty agreed that, without a definition of complex financial instruments, it may be more difficult to determine this, in particular because simple financial instruments can become difficult to value when market conditions change. In his view, the matter of whether regulators would expect SMPs to apply the IAPS should be discussed in individual jurisdictions.
- Ms. Blomme supported the proposed scope of the IAPS in light of its authority.
- Mr. Robberecht agreed that the IAPS appropriately did not impose additional requirements. He questioned the intent of paragraph 18 of Agenda Item E.1 which states: “In preparing financial statement disclosures, management complies with the requirements of the applicable financial reporting framework in their jurisdictions and such other information that may be needed for fair presentation, for example describing significant risks to inform investors.” In his view, this may imply that there are additional requirements placed on management in addition to those of the applicable financial reporting framework. Mr. Fogarty noted that this was premised on the assumption that the framework is a fair presentation framework, and suggested the IAPS could be clarified to note the IAPS does not apply to a compliance framework.

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RESTRUCTURING OF THE IAPS AND FURTHER MATERIAL THAT COULD BE ADDRESSED

The Representatives commented as follows:

- Ms. Sucher supported the restructuring of the IAPS, noting the sections will help auditors navigate the document. She also supported the Task Force's decision to include additional material on valuation adjustments. In her experience, this has been a key area of audit risk during the global financial crisis. Finally, she noted that there have been a lot of challenges coming out of the crisis that have been addressed in the IAPS.
- Mr. Windsor noted there had been a great improvement in the IAPS since it was last discussed with the CAG and noted it would be a positive addition in its current form. He suggested that the material in Section II could be expanded upon to deal with hedge accounting. Ms. Sucher supported this view, noting that regulators have been concerned with how the accounting requirements have been applied. He also stressed the importance for originators of financial instruments of recognition and derecognition, however, he recognized that addressing this in the IAPS would be a significant addition. Ms. Sucher agreed, noting that while different accounting frameworks may treat Day 1 profits differently, auditors need to pay careful attention to how this has been done. She recommended that the IAPS be exposed as planned, but suggested the Task Force could look at developing this material in anticipation of receiving further comments on exposure. Mr. Fogarty explained that a number of these topics are very specific to accounting and regulatory frameworks and so the Task Force has been cognizant of limiting the amount of framework-specific guidance. Mr. Ratnayake suggested incorporating principles-based information, for example about Day 1 profits, could be useful.
- Ms. Sucher suggested the guidance in Table 5 relating to the financial reporting framework mirrored what is currently being discussed by the accounting standard-setters. However, it is not clear when the accounting proposals would be finalized.
- Mr. Baumann supported the IAPS, echoing Mr. Windsor's comment that it will be an excellent addition to the literature. He questioned whether, in light of the references to accounting frameworks, the IASB or Financial Accounting Standards Board (FASB) had reviewed the draft. Mr. Fogarty had noted that it had not been reviewed by IASB or FASB representatives, but a number of experts familiar with the accounting requirements had been involving in reviewing the IAPS.
- Mr. Hallqvist suggested repetition could be minimized in the document by including a decision tree of the most common situation an auditor may encounter and then expand the guidance based on what might be done. In his view, this would shorten and clarify the IAPS. Mr. Fogarty noted that the Task Force had aimed to simplify what most agree is a very complex subject. In his view, designing a decision tree would be quite difficult, and the current structure of the IAPS is aimed at allowing people to navigate through the guidance based on how familiar they are with the material in Section I. Mr. Damant supported this view.
- Regarding the auditor's procedures, Ms. Blomme noted that experts within FEE had

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suggested that analytical procedures may be quite useful when the auditor is dealing with a large pool of similar transactions. She also suggested reference could be made to the importance of looking at bank confirmations for derivatives or currency forwards that may only materialize in the financial statements at the end of their contractual lives, to assist both the entity and the auditor in identifying these types of transactions at their initiation.

- Ms. Bastolla questioned whether the requirement in ISA 540 for the auditor to determine whether to use specialized skills or knowledge in the audit was intended to encompass internal audit. If so, in her view, this was inconsistent with the material included in relation to ISA 610¹⁰ regarding whether or not such individual would be considered a part of the engagement team. Mr. Fogarty clarified that the material in the IAPS dealing with specialized skills or knowledge did not relate to internal audit. Ms. Hillier noted the material within the IAPS, in particular paragraph 110, is consistent with proposed revised ISA 610.
- Mr. Uchino noted the material in the IAPS was well-organized. In particular, he supported the emphasis on the fact that the nature and extent of internal control that exists at an entity influences the auditor's determination of the balance between tests of controls and substantive procedures. He also supported including matters for the auditor to consider, including those on an entity's risk management practices, based on the experiences noted in Japan where risk management practices were not functioning as intended.
- Ms. Sucher suggested material that appeared to have been deleted regarding the auditor's review of whether narrative information in the financial statements is consistent with the entity's risk assessment and control procedures should be reinstated.
- Mr. White supported the discussion within the IAPS about communication with those charged with governance and others. He suggested that earlier communication with risk committees and audit committees regarding financial instruments could be further emphasized. Mr. Koster agreed, noting the matters cited in the IAPS should always be matters of governance interests. He also suggested the auditor should endeavor to communicate frequently with regulators.
- Mr. Koster noted the depth of the paper was impressive. However, in his view, the expectation gap in relation to what the auditor does in relation to complex financial instruments has grown to be more significant in light of the global financial crisis. He suggested further consideration could be given within the IAPS to more clearly differentiate the auditor's responsibilities from that of management. In his view, auditing complex financial instruments may become more forensic driven, in particular as it becomes more necessary to dig into an entity's valuations. He noted concerns expressed by regulators that auditors cannot simply accept a valuation and questioned what more needs to be done to direct auditors to do the appropriate level of work. Mr. Damant was of the view that the IAPS appropriately does so.
- Mr. Koster also questioned whether the guidance for auditors on developing a point estimate or range to be compared with that of management may be stepping into the role of

¹⁰ ISA 610, *Using the Work of Internal Auditors*

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management. In his view, there may be risks if auditors to create an independent model. Mr. Fogarty explained that the material is consistent with ISA 540. However, he noted that in practice this may not be common because the auditor may not have all the information necessary to do so. Mr. Koster suggested this could be further clarified in the IAPS, highlighting in particular the need for the auditor to consider whether creating an independent model is practicable.

Mr. Fogarty drew attention to paragraph 89 of Agenda Item E.1, which states: “Multiple sources of evidence may help corroborate management’s valuation of complex financial instruments. However, these sources of evidence may be circular, or act to reinforce a misleading trend of misconception. For example, if both management and the auditor have used the same expert (such as a pricing service) to arrive at a valuation, other procedures may need to be performed to corroborate the valuation.” He explained that it is common for both preparers and auditors to refer to services such as Bloomberg and others in valuing complex financial instruments.

The Representatives commented as follows:

- Mr. Gutterman noted that relying on the same expert would not be good practice, as the expert’s work would not be considered to be independent.
- Mr. Peyret noted the view expressed in some regulatory reports, in particular relating to testing of impairment, that the auditor should do more than just test management’s process.
- Mr. Baumann suggested that the paragraph should further stress that if the auditor uses the same source of information that management has used, it is still necessary for the auditor to understand the assumptions and key inputs that were used, rather than simply relying on management’s process.
- Mr. Hallqvist suggested field testing of the IAPS might be appropriate, in particular to determine whether, if the IAPS had been applied, discoveries would have been made in relation to high-profile cases noted during the financial crisis. Mr. Fogarty noted that, while field testing is not planned due to the practicalities involved, the discussions held with experts included consideration of whether those experts would find the material in the IAPS useful to educate newer staff on the fundamentals of auditing complex financial instruments.

Mr. Fogarty explained that the IAASB would be asked to approve the IAPS at its September 2010 meeting. Mr. Gutterman noted the Working Group’s consensus that the pronouncement had been significantly improved and that it is important to move toward exposure. In his view, the IAPS as it currently standard will be extremely helpful in many jurisdictions in advance of the upcoming audit season, and will surely be improved through the process in arriving at a final pronouncement. Mr. Damant encouraged the MOs to respond to the exposure draft when it is issued, whether in respect to general views or specific inputs, as the topic is complex and vital in his view.

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Report Backs (Item I)

To UPDATE CAG Representatives on the exposure drafts of Assurance Reports on the Process to Compile Pro Forma Financial Information Included in a Prospectus (ISAE 3420) and Using the Work of Internal Auditors (ISA 610).

Mr. Gunn drew attention to the matters noted in the report backs on ISAE 3420¹¹ and ISA 610 in the CAG agenda material. With respect to ISA 610, Mr. Hallqvist noted that the function of internal audit depends on the corporate governance of the entity. He commented that a key factor in assessing internal audit is the extent to which the internal audit function is subject to management decisions on salary and employment benefits, and also noted that he prefers the internal audit function to report to the audit committee, and for the audit committee to encourage interaction between internal and external audit.

Clarity ISA Implementation Monitoring (Item F)

To DISCUSS the process of monitoring the implementation of the Clarity ISAs.

Mr. Grant introduced the topic, describing the two phased approach to the Clarity ISA implementation monitoring project and the activities undertaken to date. He explained that other group such as the International Forum of Independent Audit Regulators (IFIAR) and IFAC's Compliance Assessment Program, were critical to the success of the project, as the focus was determining if changes are needed to ISAs or additional guidance is required. For this reason, ongoing dialogue with IFIAR will continue. He also noted that the firms surveyed to date were larger firms, so it is not yet clear how well the SME guidance in the ISAs has been received.

Mr. Grant explained that, while many countries surveyed have modified the ISAs, the extent of modifications varies. He also noted that most countries adopting the ISAs had referred to these as "national standards" without reference to ISAs. Mr. Grant noted that the IAASB has issued a policy paper¹² limiting the use of the term ISA when the standards have been modified in a jurisdiction, but not all countries are using this guidance as many of the auditing standard setters are not IFAC Member Bodies and, as such, are not obligated to follow the policy paper.

Mr. Grant noted that the results so far indicated that the implementation challenges centered on three standards, ISA 320,¹³ ISA 600¹⁴ and ISA 700.¹⁵ He further explained that countries had

¹¹ ISAE 3420, *Assurance Reports on the Process to Compile Pro Forma Financial Information Included in a Prospectus*

¹² *Modifications to International Standards of the International Auditing and Assurance Standards Board (IAASB) - A Guide for National Standard Setters that Adopt the IAASB's International Standards but Find It Necessary to Make Limited Modifications*

¹³ ISA 320, *Materiality in Planning and Performing an Audit*

¹⁴ ISA 600, *Special Consideration—Audits of Group Financial Statements (Including the Work of Component Auditors)*

¹⁵ ISA 700, *Forming an Opinion and Reporting on Financial Statements*

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commented that materiality may pose a particular implementation challenge due to the standard's articulation of high-level principles, but that none of the issues were sufficiently urgent to require immediate action by the IAASB. Mr. Grant also noted that firms had identified a narrow problem with ISA 600 in that the group auditor may have difficulty when dealing with significant components that are accounted for under the equity method, in that the group auditor may not have adequate access to the component auditor. He explained that the likely consequence was a modified audit report, which is a particular problem in some jurisdictions which do not permit modified audit reports for listed entities. He also noted that the Forum of Firms (FoF) is putting together guidance to build awareness amongst auditors of the need to incorporate this issue into the planning phase of the audit. Mr. Grant informed the CAG that there was a process in place to collect evidence to determine if the problem was significant, and that the IAASB would then further consider whether ISA 600 needs to be modified. Finally, he noted that there were some countries not using the ISA 700 reporting format, and that this issue has been passed to the Audit Reporting TF.

Mr. Grant explained that some countries had been concerned about the impact of Clarity ISAs on the audits of SMEs but that there was no evidence to this effect so far. He noted that the areas of concern relate to the length of the ISAs and the number of requirements so a key activity is to determine if these concerns are warranted. He also noted that translations of the Clarity ISAs had shown that some concepts and terms created difficulties in translations, and that the IAASB needed to remain mindful of this.

Mr. Grant reported that further work is underway to survey SMEs and SMPs over three years: the year before implementation of the Clarity ISAs, the year of implementation, and the year after implementation. The objective would be to monitor costs, perceived benefits and any problems of a standard-setting nature. He noted that there is a need to separate issues arising from training, support and standard-setting. Mr. Grant informed the Representatives that many National Standard Setters (NSS) are devoting resources to developing techniques and help for practitioners. He invited the Representatives to raise any ideas about how the CAG could assist in sharing the IAASB's messages on Clarity.

Mr. Grant outlined the projects reporting timeframes. Phase 1 has already been reported to the IAASB and there will be a communication about the findings in the coming months. Mr. Grant noted that Phase 2 will be addressing 2011 year ends.

The Representatives commented as follows:

- Mr. Damant explained that many countries use a national title for their versions of ISAs due to pre-existing laws that may determine the name. Ms. de Beer commented that this was a common practice in Africa, and that South Africa had changed their law to permit the use of ISAs as a title. Mr. Grant responded by agreeing that this was often the case, and so the Task Force intends to approach the global firms to suggest to them to refer to ISAs in their audit reports as well as national standards, where appropriate.
- Mr. Baumann noted that the concern regarding ISA 600 and significant components that are accounted for under the equity method may require a rapid response to avoid firms accepting audit engagements that they will not be able to complete. Mr. Grant explained that not all

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auditors believe that there is a problem. Ms. Hillier further explained that there were no short term solutions but that the FoF intends to publish a communication highlighting the challenges and some possible solutions. Ms. Hillier commented that there may be need to discuss the reporting issues with regulators to see if there is a more permanent solution that can facilitate transparent reporting. Ms. Sucher pointed out that a group auditor does not have to work with component auditors under ISA 600 as they can choose to perform the necessary procedures themselves. Ms. Borgerth explained that ISA 600 did not work well for her company which relies on obtaining audit reports from 200 other companies. Ms. Borgerth further explained that delays in obtaining audit evidence from the other auditors means that the market needs to be educated about the reasons for any modification to the audit opinion. Mr. Grant thanked Ms. Borgerth for her input, noting that this sort of input is important to Phase 2 of the project. Mr. Hallqvist noted his view that companies should use the same auditor and the same accounting system across all group entities to minimize audit difficulties.

- Mr. Peyret noted that accounting quality was important to audit quality (AQ) and that the auditors needed to have comfort about the quality of shared service centers.
- Mr. Koster noted that information on the translation challenges would be useful for the Middle East.
- Mr. Ashmelash noted that implementation support for developing nations in particular would be useful.
- Ms. Sucher expressed her view that some jurisdictions made modifications to the ISAs to enhance AQ. Mr. Grant noted that the jurisdictions that made modifications indicated that they wanted to retain additional existing national requirements and that there was no clear theme from the modifications made.
- Mr. Diomeda asked whether Malta and Slovakia were chosen as part of the Phase 2 survey because these two countries adopted the clarified ISAs without waiting for European Commission (EC) endorsement. Mr. Grant agreed that some countries were adopting the clarified ISAs without waiting for the EC and asked Mr. Johnson to comment on FEE's work in this area. Mr. Johnson commented that SME issues are a focus area in Europe, and that FEE is working with member bodies to enhance and develop software and training to support implementation. These initiatives will also help manage some of the concerns around proportionality of ISAs. Mr. Johnson also noted that the UK and Belgium both have local institutes that are working with software providers, and that FEE is trying to extend this across Europe. Mr. Attolini supported Mr. Johnson's comment on software.
- Mr. Johnson further noted that FEE was working to bring together all the literature on SME application of the clarified ISAs to demonstrate that the clarified ISAs are capable of proportional application as this was often put forward as a barrier to implementation. FEE is working to bring together the key training staff of the member bodies to share experiences. Mr. Gunn noted that it is important to draw attention to the IAASB Staff Publication, *Applying ISAs Proportionately with the Size and Complexity of an Entity*, which has been shown to be helpful.

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- Mr. Attolini asked if the implementation monitoring TF will be monitoring the use of other material, such as the IFAC's SMP Committee's *Guide to Using International Standards on Auditing in the Audit of Small- and Medium-sized Entities*. Mr. Grant noted that a parallel survey could be considered to determine who is using the SMP's guide.

IASB / IAASB Liaison (Item H)

To UPDATE CAG Representatives on the IASB / IAASB liaison initiative.

UPDATE ON KEY IAASB – IASB LIAISON ACTIVITIES

Ms. Hillier informed the CAG that representatives of the IAASB have been observing meetings of the IASB Expert Advisory Panel (EAP) on impairment of financial assets at the invitation of the IASB. Ms. Hillier noted that audit issues were often being raised by others of the EAP, indicating a general awareness of the need for IASB standards to be capable of being audited.

Ms. Hillier explained that the IAASB has working groups looking at relevant IASB standards for auditability/verifiability issues. She drew attention to the Appendix to Agenda Item H, which lists the IASB projects that have IAASB working groups. She noted that there was frequent contact between the IAASB and the IASB, including talks between the IAASB Working Groups and the relevant IASB Project Manager.

The IAASB has submitted responses to the IFRS Foundation on the IFRS Taxonomy for XBRL and to the IASB on the Exposure Draft on Liabilities. Ms. Hillier drew attention to the Agenda Paper H.1 as a sample of the type of IAASB response, noting that the IASB had indicated that they found the responses helpful. She commented that IAASB Working Groups would write comment letters only where concerns are identified.

The Representatives commented as follows:

- Mr. Upton supported the IAASB Working Group's approach of suggesting wording rather than merely listing concerns. He suggested the IAASB should consider focusing on application of IASB standards as well as measurement issues, and whether a standard is capable of being audited consistently. He also commented that the IASB has heard of concerns regarding the volume of disclosures, particularly around sensitivity disclosures, and also suggested the IAASB should form a working group on the Revenue Recognition ED. Ms. Hillier noted the IAASB intends to do so. Mr. Peyret agreed that Revenue Recognition is an important topic and noted that a publication of the audit of revenue recognition had been issued in France.
- Mr. Gutterman asked if the IAASB Working Groups wanted volunteers from IAASB CAG to assist in forming their views. Ms. Hillier acknowledged that it may be useful, but no CAG Representatives have participated in the IAASB Working Groups so far.
- Mr. Windsor commented that that the IAIS response to the IASB ED on Insurance Contracts includes comments on whether particular items are auditable. He agreed to pass the IAIS comment letter to the IAASB.

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- Mr. Baumann commended the IAASB for their efforts in liaising with the IASB and noted that the PCAOB Standing Advisory Group (SAG) has expressed concern about the pace and volume of changes to accounting standards and the ability of preparers and auditors to analyze and respond to these changes. He acknowledged that part of the concern was due to the nature of the changes from the US perspective, in that the US profession needed to understand the implications of moving from over 200 revenue recognition rules to a single standard.
- Mr. Roussey asked if the IAASB has considered pursuing a limited assurance standard on management commentary.

DISCLOSURES

Ms. Hillier updated the Representatives on the proposed project on the audit of financial statement disclosures, as raised by the CAG at earlier meetings. She noted that many new IASB standards contained critical new disclosures and disclosure issues, and that the European Financial Reporting Advisory Group (EFRAG) has a thought leadership project to develop a disclosure framework which the IAASB is observing.

Ms. Hillier noted that the IAASB has formed a Working Group to investigate a possible project on disclosure and the IAASB would consider the matter of disclosures at its upcoming meeting. The Working Group has identified a number of perceptions regarding auditing disclosures, including auditors' performance and role relative to disclosure. Ms. Hillier explained that the key issues or perceptions identified were:

- Risk assessments at the assertion level are the same for disclosures, but there may be a perception that auditors may not pay the same level of attention;
- Challenges are encountered when evaluating misstatements and determining how to weight disclosure misstatements compared to other misstatements;
- The need for both preparers and auditors to exercise judgment has two aspects. The first is that some commentators maintain that preparers and auditors need to exercise more judgment in reducing unnecessary disclosures. The second aspect is the perception that preparers and auditors should exercise more judgment in including additional disclosures to achieve fair presentation;
- The appropriate approach for auditors regarding the audit of sensitivity disclosures needs to be determined, including consideration of whether the auditor's procedures should be limited to auditing management's process in preparing the disclosures;
- It may be unclear how the concept of sufficient appropriate audit evidence applies to auditing disclosures, given that some disclosures are necessary even if the disclosures may not be reliable; and
- The boundaries of financial reporting are becoming blurred.

Ms. Hillier explained that the Working Group believes the way forward is to issue a Discussion Paper to better understand the expectations of stakeholders, including users and regulators,

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analyze whether there are the gaps in the ISAs and provide a platform for the IAASB to participate in the wider contemporary debates on disclosures. The Discussion Paper will articulate issues from an audit perspective. It is anticipated that the Working Group will present a draft of the paper to the IAASB at its December 2010 meeting.

The Representatives commented as follows:

- Mr. Damant noted that one reason for the concerns about the audit of disclosure is that capital markets judge future cash flows, and the financial statements are only evidence for this rather than the whole answer. He explained that disclosures were critical to a proper assessment of future cash flows.
- Messrs. Attolini, Baumann, Kuramochi, Roussey, and Upton, and Ms. Sucher, supported the IAASB pursuing the audit implications of disclosures.
- Mr. Baumann noted that the PCAOB is looking at the audit of disclosures and considering many of the same issues, and suggested this may be a key project for the IAASB and the PCAOB to work on together. He noted the increasing importance of disclosures and that the PCAOB was evaluating whether additional guidance was needed. He also noted that auditors traditionally record all unadjusted differences for assessment at the final stages of the audit, but the increasing importance of disclosures raises the question of whether this is best practice.
- Mr. Upton supported Mr. Baumann's comments on unadjusted differences and also noted that he is aware that preparers sometimes maintain that proving to an auditor that a disclosure is immaterial is extremely difficult; as a result many financial statements may contain immaterial disclosures. Mr. Kocktvedgaard responded to Mr. Upton by noting that preparers often have as much difficulty convincing regulators about the immateriality of disclosures as they have convincing auditors.
- Ms. Sucher commented that fair presentation is a focus area for the UK FSA, and that they consider "true and fair" to be a dynamic concept. She recommended that the Working Group also consider audit process issues, such as the timing of the review of disclosures and the appropriate person within the audit team to be reviewing disclosures. Ms. Hiller noted that it was important to consider the timing of the review of disclosures from both the perspective of the preparers and auditors.
- Mr. Kuramochi commented that IOSCO supports this project, and noted that the Japanese Financial Supervisory Agency (JFSA) is currently deciding if Japan should move to IFRS and one of the key issues is the enforceability and auditability of IFRS. He noted that it was important that unauditable disclosures were highlighted.
- Mr. Attolini noted that the project may help to prevent an expectation gap from developing, and that there may be different ways in which the auditor can approach the audit of disclosures. However, he expressed concern that the project should not increase the burden on smaller entities, and suggested that the IAASB should consider the need for guidance on proportionality in this area. Mr. Damant noted that IFRS for SMEs may partly address this issue.

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- Mr. Upton noted that auditors may attempt to make a measurement or disclosure more robust through auditing and gave sensitivity disclosures as an example. He disagreed with this approach as auditing cannot improve the quality of the inputs.

IAASB Future Strategy and Work Plan – 2012-2014 (Item G)

To DISCUSS a draft consultation paper planned for issuance in December 2010.

Prof. Schilder introduced the topic and noted that there were over 100 responses to the IAASB's online strategy survey. There were many messages but the overwhelming thrust of the comments was that commentators were satisfied with the overall work of the IAASB, that the IAASB needs to ensure that the clarified ISAs are adopted and implemented effectively, and that this should occupy more than 50% of the IAASB's time. Prof. Schilder noted that this theme was reflected in the draft strategy paper included in the CAG papers.

REPORT BACK

Prof. Schilder drew attention to matters noted in the report back in the CAG agenda material.

OVERALL ISSUES REGARDING THE PROPOSED STRATEGY CONSULTATION PAPER

The Representatives commented as follows:

- Mr. Roussey asked if it was possible to include in the strategy consultation paper a summary of the performance of the IAASB in delivery on the previous strategy. In his view, doing so would enhance the credibility of the IAASB by illustrating the significant work effort of the last three years, and may mitigate some of the criticism that may arise from the MG report. Prof. Karim suggested that reports that the IAASB provides to the PIOB could be used for this purpose.
- Mr. Koktvedgaard noted that the IAASB needed to co-ordinate well with the other IFAC standard-setting boards.
- Mr. Bradbury suggested that the wording describing the shared standard-setting relationship and the interaction between the PIOB and the CAG could be better described. He preferred previous language that referred to the IAASB as a standard-setting body designated by, and operating under the auspices of, IFAC. This language also noted the IAASB is subject to the oversight of the PIOB. Mr. Bradbury also highlighted that there was repetition of material in the first four pages. Further, he noted that the diagram on page 9 which describes the IAASB's relationship with its stakeholders could be presented in a more sophisticated format. Prof. Schilder requested that Mr. Bradbury provide his suggestions regarding the possible improvements to the IAASB staff directly.
- Mr. Robberecht asked for clarification on paragraph 9, 4th bullet of the draft consultation paper on the proposed IAASB Strategy and Work Program for 2012-2014, which states as one of the other international pronouncements developed by the IAASB being "ISQCs are to be applied for all services falling under the ISAs, ISAEs and ISRSs" as in the past the

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IAASB referred to ISQC 1 or equal high-quality standards. Mr. Robberecht explained that the EC has not ~~adopted yet taken a decision on the possible adoption of the ISAs~~ but also has not rejected them, and that, in addition to being a member of the IAASB CAG, it is actively assisting in translations while also participating in the Monitoring Group, financing the PIOB, and being an observer to the IAASB meetings. He noted that the forthcoming EC Green Paper will discuss adoption as one part of AQ. Prof. Schilder explained that, while the IAASB was disappointed about the delay, the IAASB has been focusing its outreach efforts on those European countries that have not adopted ISAs yet. Prof. Schilder also noted that a theme of his discussions in many countries had been that they were concerned about Europe failing to lead in ISA adoption. He commented that there needed to be communication supportive of ISAs to give the message that Europe, while delaying, was still interested in ISAs. Mr. Robberecht noted that ~~listed companies in the European Union (EU) would still use auditors as the major firms have aligned with ISA~~the question of a possible ISA adoption in practice is mainly an issue for the audits of non-listed companies as the Forum of Firms has committed to the consistent application of the ISAs. Mr. Fleck supported Prof. Schilder's comments about the importance of EC recognition of ISAs, noting that the EC needs to show leadership in the financial crisis by requiring the best available standards. Mr. Fleck disagreed with Mr. Robberecht's comment about the de facto adoption of ISAs for listed companies in the European Union (EU) because he believes that the issue is important for domestic audits, not just transnational audits. Ms. Blomme supported Mr. Fleck's comments.

LIST OF POSSIBLE ACTIONS

Prof. Schilder invited Representatives to comment on whether the list of possible actions was consistent with the IAASB's three areas of strategic focus and whether it responds to issues facing the accounting profession; whether Representatives had any items to add to the list; and how additional actions they may identify should be prioritized.

The Representatives commented as follows:

- Mr. Kuramochi noted that the JFSA is considering requiring assurance on prospective financial information. Prof. Schilder noted that comments on the ED on ISAE 3420 may help with any revision of the assurance standard dealing with prospective financial information.¹⁶ Ms. Hillier noted that ISAE 3400 had been adopted only by a few jurisdictions, though many jurisdictions have developed differing version so the IAASB needs to understand the issues before proceeding.
- Regarding the development of industry-specific guidance, while supporting the proposals to develop or revise the banking guidance, Mr. Windsor suggested that the IAASB should undertake a project regarding the audit of insurance companies, with actuaries as part of the audit team. He further noted that the IASB insurance project makes this a good time to consider the audit implications. Ms. Blomme noted that she had a greater appreciation for the

¹⁶ ISAE 3400, *The Examination of Prospective Financial Information*

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need for the projects on IAPS 1004¹⁷ and IAPS 1006¹⁸. Mr. Kocktvedgaard noted that the IAASB needed to be cautious in choosing to develop sector-specific guidance and standards, and should look at whether there are any broader issues that can be considered, such as insurance contracts rather than insurers. Prof. Schilder acknowledged that broader projects are preferred.

- Mr. Cassel expressed support for ISAs, noting that International Organization of Supreme Audit Institutions (INTOSAI) includes the ISAs in its recently finalized International Standards for Supreme Audit Institutions (ISSAI) and that implementation guidance was a key concern for INTOSAI. He also noted that the projects that most interested INTOSAI were: reporting by auditors, with the critical question of how to make the reports interesting to read and how to limit the expectation gap; and assurance on corporate governance statements and internal control. Mr. Pannier supported Mr. Cassel's comments, noting that there needed to be focus on the public sector, including the costs and benefits of using ISAs, and that case studies would be helpful in this regard. Mr. Damant supported Mr. Cassel's comment on the need for projects related to corporate governance.

Mr. Damant asked Representatives to arrange for their MOs to provide the IAASB with thorough and detailed responses to the Consultation Paper when it is issued in December 2010.

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Other Information in Documents Containing Audited Financial Statements (Item M)

To DISCUSS matters highlighted by the Task Force since the last CAG meeting or brought forward by CAG Representatives at previous meetings and obtain further input from the CAG.

Mr. Gélard introduced the project, noting the CAG had discussed the project at its March 2010 meeting. He explained that, in advance of the CAG, teleconferences had been held with the Working Group as well as the Basel Committee on Banking Supervision. In addition, he reported that a survey had been sent to CFA Institute members, responses to which will inform the Task Force's further discussions.

REPORT BACK

Mr. Gélard drew attention to matters noted in the report back in the CAG agenda material.

WHAT DOCUMENTS SHOULD BE INCLUDED IN THE SCOPE OF ISA 720?¹⁹

Mr. Gélard reported that the CAG Working Group had suggested the Task Force should make clear what is meant by the term "annual report" in extant ISA 720, because this term may mean

¹⁷ IAPS 1004, *The Relationship Between Banking Supervisors and Banks' External Auditors*

¹⁸ IAPS 1006, *Audits of the Financial Statements of Banks*

¹⁹ ISA 720, *The Auditor's Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements*

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different things in different jurisdictions. The Task Force has therefore endeavored to provide a description of the key features of documents intended to be covered by ISA 720.

The Representatives commented as follows:

- Mr. Damant suggested the standard should be clear on what is, and what is not, considered to be other information. For example, he cited the summary and shorter results in the beginning of an entity's annual report. In his view, this is often where an entity will aim to present its results in the best possible light. He also supported the standard covering preliminary announcements, as these are extremely important to investors and are often price-sensitive.
- Mr. Koktvedgaard supported the distinction made by the Task Force to clarify that the other information included in the scope of the revised ISA should be that which relates to the financial statement objectives. In his view, it would not be appropriate to suggest that the auditor has to deal with other information for which it would be impracticable to expect that the auditors would have knowledge.
- Mr. Koktvedgaard ~~questioned~~ asked whether corporate governance and Corporate Social Responsibility (CSR) statements, as well as Sharia law requirements, would be considered to be in the scope of proposed revised ISA 720. In the Working Group's view, if such information is included in the glossy annual report, the standard should address the auditor's ~~should have some~~ responsibility for reading this information. He explained the view that the standard also has to address the situation where same principle should apply if these matters are published on an entity's internet at the same time as the financial statements, with the timing of the release being the critical point in scoping in this information. Mr. Gélard clarified that both scenarios would be covered by the proposed revised standard.
- Mr. Robberecht questioned whether, based on the proposed description of the key features of documents covered by ISA 720, eXtensible Business Reporting Language (XBRL) would be included in the scope of the standard. Mr. Gélard replied that he did not believe this to be the case. Ms. Blomme suggested further thought may need to be given to the matter. While she understood the IAASB had previously communicated its position that ISA 720 was not meant to apply to XBRL, reading the description of documents proposed to be included in the revised ISA, auditors and users may interpret XBRL now to be included in its scope. Mr. Koktvedgaard agreed that this particularly may also be the case when jurisdictions require the final financial statements to be published in XBRL only (that is, if XBRL is the only format of the financial statements made publicly available, most users would assume that it had been covered by ISA 720). He also noted that, if XBRL information also accompanies the audited financial statements and is published on the internet at the same time the financial statements are issued, it would appear to be included in the scope of the proposed revised ISA.
- Mr. Johnson supported the inclusion of the preliminary announcement within the scope of ISA 720. In his experience with the UK listing rules, the auditor typically agrees in writing to the issuance of the preliminary announcement. He would suggest therefore that, if the auditor is not complete at that time, that the auditor is taking a risk in relation to the numbers that are issued. He explained that in a number of audit firms, there is a stipulation that the audit must

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be complete before clearance can be given on the preliminary announcement to mitigate the risk that the audit may find differences after the preliminary announcement has been made. He supported Mr. Damant's view that investment decisions increasingly are being made on information other than the audited financial statements and noted that information that may be provided in a preliminary announcement could be misleading if presented inappropriately.

- Mr. White questioned whether the proposed revised standard deals with what the auditor would do having looked at a preliminary announcement and later finding differences. He suggested that this topic should be specifically addressed to advise auditors of appropriate actions should this circumstance occur. Ms. Sucher suggested there may be guidance in the UK that may be relevant for inclusion in the revised ISA.
- Ms. Blomme cautioned that often the securities listing rules determine the extent to which an auditor is associated with other information. She encouraged the Task Force to determine whether the revised ISA could better explain that certain jurisdictions may have different requirements for auditors, in particular in relation to preliminary announcements and corporate governance statements.
- Mr. Koktvedgaard did not agree that preliminary announcements should be covered in the scope of ISA 720, as there is not a requirement for the auditor to audit the preliminary announcement. He noted in practice that if there is a problem with the preliminary announcement that is discovered during the audit, it is management's responsibility rather than the auditor. Mr. Gélard noted that, while there is no obligation for the auditor to audit a preliminary announcement, regulators in particular jurisdictions (for example, France) expect the auditor to be associated with the preliminary announcement and indicate what percentage of the audit has been completed. In his view, work on other information is a continuum of effort and is performed in light of the auditor's knowledge obtained to date. Mr. Baumann expressed the view that it would likely be difficult for the auditor to make a statement about the percentage of the audit that has been completed at the time of a preliminary announcement.
- Ms. Sucher questioned the Task Force's assertion that the annual financial report as prepared in the EU in accordance with the Transparency directive would be excluded from the scope of the revised ISA. Mr. Gélard explained that it is often arrives after the entity has issued its financial statements and annual report publicly. Ms. Sucher agreed, noting that at that time the auditor would have finished the audit and would therefore not have any responsibility for the transparency report. She suggested, however, that it might not be clear to people reading either the annual report or the transparency report that the work effort is different. Mr. Damant suggested the application material could clarify explicitly why certain items have been excluded from the scope.
- Mr. White also questioned whether the ISA takes into account that an entity may prepare multiple annual reports using different frameworks (for example, under IFRS and home country GAAP). Mr. Gélard noted that, if financial statements presented under each framework were audited, then the auditor would have a responsibility for both annual reports.

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WHAT ARE THE AUDITOR'S RESPONSIBILITIES RELATING TO OTHER INFORMATION?

The Representatives commented as follows:

- Mr. Baumann asked for clarification as to what the auditor does if, in reading the other information, he finds it to be misleading. Mr. Gélard explains that the auditor first discusses the matter with management and requests the information to be changed and, if management does not agree, then raises the matter with those charged with governance. Mr. Baumann supported this position.
- Mr. Cassel noted that it is important for the auditor to understand the reason for any misstatements in other information. In his view, in the public sector, management may have more incentive to include information that may be misleading in the annual report. Management might, for example, want to give the impression that costs were higher than the actual costs in order to get more financial resources to their agency. In his view, the revised ISA should seek to give as much guidance as possible to auditors as to what should be done if both management and those charged with governance will not change information that the auditor has deemed to be misleading. Ms. Sucher agreed, noting that IOSCO had previously encouraged the IAASB to avoid phrases such as “The auditor shall take further appropriate action and procedures necessary under the circumstances.” In her view, it is important for the IAASB to provide as much guidance as possible, while acknowledging that judgment may be required in the circumstances.
- Mr. Kuramochi noted IOSCO's support for the direction taken on the auditor's responsibilities for other information extracted from the audited financial statements. He suggested the revised standard should seek to be as explicit as possible in the type of procedures and the level of supporting document that is necessary in dealing with other information that is not extracted from the audited financial statements. In his view, this is important for enforceability and investor protection. He also believed that the financial statement user view would be helpful in determining what procedures should be done by auditors. He suggested that, if this question was not included in the CFA Institute survey, a question should be posed in the exposure draft. Mr. Gélard noted this had been included in the CFA Institute survey.
- Mr. Kuramochi also questioned what the Task Force's view would be in relation to other information included in prospectuses, which is dealt with under ISAE 3400. He suggested that, for prospective financial information, the auditor could check for consistency with the entity's business plan we can also check consistency with their business plan.
- Mr. White observed that, in many cases, the other information will be contained in a portion of the annual report that is subject to particular disclosure standards, whether prescribed by the accounting framework or other regulatory requirements. He believed that the auditor's responsibility is broader than just reading and considering the disclosures, because the auditor is looking at whether management has adequately responded to the disclosure requirements.

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- Mr. Hansen noted that challenges in defining the auditor’s responsibilities without becoming too prescriptive. In his view, it is difficult to define whether other information is inconsistent with the financial statements. He suggested the auditor’s approach may differ depending on whether the other information was qualitative or quantitative. Mr. G elard confirmed that the Task Force is aiming to provide examples of what would be considered obviously misleading, in particular when information is omitted or misstated. Mr. Uchino suggested the auditor’s knowledge of how management is operating the entity would be important in this regard.
- Ms. Sucher questioned whether the proposed standard will contain a “stand-back” provision for the auditor to consider the other information. She noted this is covered in some ways in ISA 700 and, in her view, it is important for the auditor to look at the financial statements as a whole to determine whether the financial statements and other information make sense. Mr. G elard confirmed that the Task Force is considering introducing a requirement for the auditor to consider whether there are any remaining matters relating to the other information that could undermine the credibility of the audited financial statements and the auditor’s report, or make the other information obviously misleading.

THE AUDITOR’S OBJECTIVES UNDER ISA 720 AND THE TITLE OF THE ISA

Mr. Damant suggested the title of the standard could be changed further, given the negative connotation that might result in dealing with “other information” when, in his view, this information is critical.

WHAT ARE THE AUDITOR’S RESPONSIBILITIES REGARDING THE DISSEMINATION OF DOCUMENT BY THE ENTITY?

Mr. G elard explained the Task Force’s view that the electronic dissemination of the annual report is a broader issue than ISA 720 and, accordingly, is not distinctly addressed within the standard. Similarly, the Task Force has determined not to require the auditor to verify the other information on the entity’s website when posted for the first time.

Assurance on a Greenhouse Gas (GHG) Statement – ISAE 3410 (Item N)

To DISCUSS matters highlighted by the Task Force since the last CAG meeting or brought forward by CAG Representatives at previous meetings and obtain further input from the CAG.

Ms. Mc Cabe and Prof. Simnett introduced the topic noting that, based on feedback received on the public consultation paper,²⁰ the IAASB had decided to incorporate requirements for limited assurance engagements as well as reasonable assurance engagements into one ISAE. Other feedback received on the consultation paper indicated that the clear majority of respondents were generally satisfied with how most issues had been dealt with and expressed a strong demand for the ISAE to proceed.

²⁰ Consultation Paper, *Assurance on a Greenhouse Gas Statement*, issued in October 2009

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WORK EFFORT FOR A LIMITED ASSURANCE GHG ENGAGEMENT

The Representatives commented as follows:

- Ms. Sucher noted that, in theory, while it has different facets and cannot be quantified, limited assurance is a continuum from meaningful to reasonable. Ideally, however, the ISAE for GHG engagements should be clear about the minimum procedures necessary that tip a limited assurance engagement into a reasonable assurance engagement to ensure consistency between practitioners. Ms. Blomme responded that practitioners are doing GHG engagements now without a subject matter-specific ISAE using ISAE 3000 which is very generic. The draft ISAE 3410 puts practical considerations into a subject matter-specific standard. Practitioners consulted by FEE, who are looking for a consistent approach, are broadly happy with the draft in that respect.
- Mr. Pannier commented that the project is timely, particularly as the G20 has GHGs on its agenda. He agreed with the emphasis in the draft on risk assessment for both reasonable assurance and limited assurance engagements, noting in particular a concern about potential fraud. He also noted that, while there is a place for limited assurance engagements which the draft appears to properly describe, it might be expected that most engagements will move to reasonable assurance in time.

SAMPLE REPORTS

The Representatives commented as follows:

- Mr. Damant noted that he agrees with the reasons given in the agenda paper for the description of procedures for a limited assurance engagement being more detailed than for a reasonable assurance engagement.
- Ms. Blomme commented that having a more detailed description of procedures for limited assurance may give the impression that more is done than in a reasonable assurance engagement. She also noted that some of the report wording in the draft ISRE 2400 may be appropriate to adapt for the sample report in this ISAE. Prof. Schilder noted that the limited assurance description with respect to the extent of the practitioner's consideration of internal control may need particular attention to differentiate a reasonable assurance engagement from a limited assurance engagement. Mr. Koktvedgaard suggested that to address the above concerns, perhaps more should be said about the procedures performed in the report on a reasonable assurance engagement.
- Ms. Blomme noted that practitioners consulted by FEE had raised the issue of how to report when the engagement includes both limited assurance and reasonable assurance conclusions and suggested that an example of this be added.
- Mr. Koktvedgaard commented that the current sample reports require the reader to understand some auditing terminology and concepts, such as "reasonable assurance" and the importance of the firm following ISQC 1. Prof. Simnett responded that regulators and other standard-setters are now using some of this terminology, making it better understood beyond the accounting profession than in the past. Mr. Damant suggested that the Explanatory

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Memorandum accompanying the exposure draft may be an appropriate place for explaining these matters, together with an explanation of what GHGs are and the role of GHG statements, along the lines of the explanations included in the CAG agenda papers.

- Mr. Ratnayake noted the need to deal with the credibility of claims by companies that reduce their emissions and earn carbon credits.
- Mr. Koktvedgaard noted that some of the wording in the report regarding uncertainties may be difficult and the report should make it clear that, despite the uncertainties, the practitioner is satisfied with the GHG statement. He also questioned whether the draft differentiates between uncertainty with respect to actual emissions and measurement uncertainty. Prof. Simnett noted that the draft distinguishes between scientific uncertainty and measurement uncertainty, which is consistent with other authoritative sources.

REPORT BACK

Ms. Mc Cabe drew attention to matters noted in the report back in the CAG agenda material.

Open Session (Item O)

Prof. Schilder explained that the purpose of the Open Session was to allow the CAG to recognize Mr. Damant's achievements on the occasion of his retirement as Chair of the CAG. Prof. Schilder complimented Mr. Damant on the respect and supportiveness that he showed in participating in the IAASB and CAG meetings and the passion he showed in the course of his work. Prof. Schilder highlighted the efforts Mr. Damant had put into the CAG, including increasing the number of MOs, innovative meeting procedures and outreach to key regions. Prof. Schilder also commented on Mr. Damant's preparation and openness for dialogue, and thanked Mr. Damant on behalf of the IAASB, Staff, Representatives and Observers.

Mr. Damant commented that he likes the spirit and culture of the CAG and does not want the open discussion of the CAG inhibited. He highlighted the role of auditors in lowering the cost of capital by enhancing the quality of corporate reporting.

Prof. Schilder asked if Mr. Damant would consider assisting the IAASB in getting feedback from Russian stakeholders. Mr. Damant expressed a desire to assist.

Audit Quality (Item P)

To DISCUSS matters highlighted by the Task Force or brought forward by CAG Representatives.

Mr. Grant introduced the topic, noting that the project has been discussed by the IAASB on two occasions and was also discussed at the June 2010 IAASB-NSS meeting. He noted that the Task Force included two representatives of audit inspection agencies who are members of IFIAR. He also noted that working with IFIAR will be a particular focus of the project.

Mr. Grant noted that there were many views of what constitutes AQ but that there were some common features of most views. Many of these common features were highlighted in the UK Financial Reporting Council (FRC) publication on an AQ Framework, which may provide a

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useful point from which to further explore the topic. Some of the drivers of AQ are within the control of the auditors, but others are outside of their control. In particular, he noted that it was difficult to separate AQ from the corporate governance and accounting frameworks that surround it, as these formed an important part of the building blocks of AQ. He noted that no definition of AQ has widely agreed to date. He also highlighted recent debates about the role and effectiveness of the audit profession, and noted the EC Green Paper will likely reflect on AQ.

Mr. Grant noted that, while a focus on inputs to AQ is important, user perceptions of the quality of the outputs of the audit also need consideration. In addition, it was recognized that promoting greater communication with users about the audit, and what an audit involves and delivers, may be helpful in informing user perspectives on AQ.

PROPOSED WAY FORWARD

Mr. Grant noted that determining the appropriate scope of the AQ project is difficult as some of the possible AQ drivers or actions are beyond the remit of ISAs and the IAASB's Terms of Reference. He also noted that the IAASB members have two different schools of thought about the appropriate scope of the project. Some IAASB members believe the project should focus on the interaction between ISAs and AQ and should develop a communication (thought piece) on the links between ISAs and AQ. This would be a relatively short-term part of the project and would show that ISAs are only one part of AQ. Other IAASB members prefer a wider project that would involve developing a discussion paper that considers all factors in AQ, including those outside of the IAASB's remit. This approach would explore all the factors relevant to AQ including matters that are the responsibility of other parties, such as the IESBA, the International Accounting Education Standards Board (IAESB), audit firms and regulators. He noted that this is a more ambitious project with a longer time frame and that achieving a common understanding of AQ would assist in working with bodies such as IFIAR.

Mr. Grant noted that both versions of the projects could be pursued in parallel and that the narrow view is a way of moving the AQ project along quickly.

The Representatives commented as follows:

- Ms. de Beer, Ms. Sucher and Mr. Diomeda supported the wider scope for the paper. Ms. de Beer and Ms. Sucher noted the need for further work on the interactions between the auditing standards, ethical standards and education standards and compliance with these standards, including the IFAC Compliance Program. Mr. Diomeda noted that the project should identify key indicators of the global level of AQ, so that progress on AQ can be measured over time.
- Mr. Koktvedgaard noted that the IAASB should pursue the narrower project, but that the wider project should be undertaken by IFAC, referring the appropriate elements to the IAASB, IESBA and IAESB. Mr. Pannier noted that it was less a question of a narrow scope or wide scope and more a need to respond to the expectation of society to know what happened in the financial crisis. He supported a project focused on producing a paper in the near future that maps the drivers and weights those drivers.
- Mr. Cassel noted that a high-quality audit may be seen as one that has followed all applicable ISAs, but that doing so may not always be sufficient. In his view, the financial crisis

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presented auditors with challenges not addressed in the standards. Either there is the dilemma that ISAs when applied might seem to be inconsistent or there is a situation when an ISA might leave the auditor with very little guidance. He commented that the IAASB needed to work further with the IESBA in this regard. Mr. Damant and Mr. Ratnayake noted that the need for judgment in complying with requirements was critical, and that the exercise of judgment varied around the world. Mr. Grant noted that the proper application of ISAs requires a significant amount of judgment and that these judgments were influenced by other areas of the AQ framework such as training, firm culture and the tone at the top. Mr. Grant also noted that requirements of the ISAs need to be consistently applied, regardless of the jurisdiction and circumstances of the audit.

- Ms. Lang asked whether the project was limited to AQ, or also encompassed assurance quality which is particularly relevant to SMEs and SMPs. Mr. Grant noted that the project was starting with AQ but may need to expand to cover assurance quality as well in the future. Mr. Grant noted that the topic of assurance quality may be sufficiently large to make the overall project too slow in the short term. Ms. Lang noted that Prof. Schilder's slide on AQ was also relevant to assurance engagements as well as audit engagements. Prof. Schilder supported this and noted that many of the inputs and outputs to AQ were equally applicable to assurance engagements, but that there may be fewer layers of regulation and oversight for assurance engagements. Mr. Attolini noted that this was a key project from the perspective of the IFAC SMP Committee and believes that the project should include assurance and related service engagements and be applicable to the SMEs and SMPs as well as large clients and firms.
- Mr. Robberecht noted that the upcoming EC Green Paper will touch on AQ and that many of the drivers of AQ, such as auditor independence, training, oversight and governance, were already included as part of the European Statutory Audit Directive. He supported Mr. Grant's view—the IAASB view in paragraph 34 of the draft consultation paper on the proposed IAASB Strategy and Work Program 2012-2014 that ISAs that auditing standards are an important part of AQ are one component of the global package of AQ.
- Mr. Baumann noted that AQ had been the subject of intensive consideration over the past few years. The PCAOB had discussed AQ in a meeting but also did not define AQ. Mr. Johnson noted that AQ was too complex to define in any meaningful way and that a definition would fail to capture the full range of factors needed even if the definition was extensive. Mr. Johnson noted that it was possible to identify drivers and indicators of AQ despite the difficulty in defining AQ.
- Mr. Baumann noted that many of the factors considered in AQ may have unintended consequences or promote inappropriate behavior. Mr. Baumann gave the example the example that if AQ was measured by the number of restatements then firms have an incentive to avoid restatements even if warranted which would harm AQ. Mr. Baumann noted that the Big 6 firms have been asked how they measure AQ but, while there were various measures and actions, there was no overall answer. He noted that firms were best placed to know how to measure AQ and they should be tasked with responsibility to determine the measures of AQ. Mr. Damant supported considering internal measures of AQ developed by the firms. Mr.

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Grant noted that the project was not attempting to develop measures of AQ as this was a particularly difficult task, particularly in relation to outputs of AQ, but that looking at firms' internal measures of AQ may be useful. Mr. Grant supported the need to involve the firms, noting that transparency reports by firms as required in some jurisdictions include some aspects of AQ, though more needed to be done to gain a full AQ view of each firm.

- Mr. Johnson noted his view that the UK FRC framework of AQ did not give adequate weight to the impact of oversight and inspection of firms which had improved the rate of change within firms. Mr. Grant asked if it would be useful if the IAASB project included developing a global version of the UK FRC paper. Mr. Johnson supported this but noted that ultimately it was up to audit firms to improve AQ. Mr. Ratnayake noted that regulators and audit inspectors also have a key role in improving AQ and that different firms have displayed differing level of independence which affects AQ. Mr. Fleck supported Mr. Johnson's comment about the need to look at the firms, but also noted that the project needed to include the individual auditors as well as the firms involved in each audit. Mr. Johnson noted that firms have extensive internal inspections as well which should give a similar picture to the external inspections. Mr. Johnson noted that audit inspectors needed to work closely in developing consistent approaches to audit inspections.
- Mr. Johnson noted that a key consideration was ensuring that appraisal and compensation systems reinforced the right behaviors. Mr. Attolini noted that other considerations included the education of prospective auditors and the competitiveness of the job market for graduates, which has an effect on AQ.
- Ms. de Beer noted that the ultimate measure of AQ is user perceptions. These user perceptions are affected by audit and other failures. Ms. de Beer noted that further work needed to be done on user perceptions as this was often overwhelmed by the focus on internal factors within the firm and the audit process affecting AQ. Ms. Sucher noted that IOSCO has looked at user perceptions in the past, most notably via consultation papers on transparency and auditor communications. Mr. Fleck noted that user perceptions of AQ were more important than trying to define AQ but that people's judgment of AQ is influenced by their understanding of accounting and independence frameworks. Mr. Kuramochi supported Ms. de Beer's comment and noted that the IAASB should produce a paper explaining the role and responsibilities of the auditor to reduce the expectation gap.
- Ms. Sucher noted that the UK has recently focused on auditor skepticism and noted that it may be difficult to train auditors in skepticism. Ms. Sucher noted that there may be non-audit services that affect perceptions of AQ and skepticism.
- Mr. Hallqvist noted that the International Corporate Governance Network's (ICGN) main concern is material misstatement due to fraud, and that ICGN does not believe there are any inherent limitations to an audit. He noted his view that, while there may be time and cost limitations, any of the recent accounting frauds could have been detected if sufficient resources had been applied. He also noted that auditors should look for the precursors to fraud such as excessive performance pressure or management problems and then ask the entity's board for further funding to dedicate additional resources to fraud detection. Mr.

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Hallqvist noted that ICGN was doing further work on this and would continue to push for this at annual meetings. Mr. Damant noted that there were many outside the audit profession who believe that every audit is a forensic audit designed to detect fraud.

- Mr. Kuramochi noted that it had been reported that audit fees had declined as the economy slowed even though audit risk increased at that time. He also noted that, in Japan, some listed companies are moving to use smaller audit firms with a corresponding decrease in audit fees. In his view, existing IAASB projects like ISA 720 would likely increase auditor's work effort and so a corresponding increase in audit fees would be expected. Mr. Kuramochi noted that some criteria may need to be developed for the appropriate amount of hours spent on an audit. Mr. Hallqvist noted that there had been recent reports of auditors being criticized for signing audit reports before sufficient audit evidence had been gained, as well as criticism for selling non-audit services that conflict with the audit. Mr. Hansen noted that audit fees had been extensively discussed in the US recently and that NASBA will be issuing a paper on loss-making and low cost audits. Mr. Baumann noted that the PCAOB was looking at fee decreases on audit engagements. Mr. Koktvedgaard noted that AQ and audit fees may not be related as audit fees should decrease if the company has improved internal controls, for example, or if the audit fee had been too high in previous years.

Assurance Engagements Other than Audits or Reviews of Historical Financial Information (Item R) – ISAE 3000

To DISCUSS matters highlighted by the Task Force since the last CAG meeting or brought forward by CAG Representatives at previous meetings and obtain further input from the CAG.

Ms. Hillier introduced the topic, explaining that ISAE 3000 is being revised to take account of practical experience with the standard since it was issued in 2004, and with the IAASB's experience with related projects, such as the development of ISAE 3402.²¹ Ms. Hillier noted the Task Force's intention to develop the revised ISAE 3000 based on the assurance concepts currently embodied in the existing *International Framework for Assurance Engagements*.

The Representatives commented as follows:

- Mr. Hansen asked who makes the management representation in a direct reporting engagement, and whether they can be different from the engaging party. Ms. Hillier responded that there must always be 3 parties to an assurance engagement under ISAE 3000: the responsible party, the intended users and the practitioner; the other 2 parties noted in the agenda paper (i.e., engaging party and measurer/evaluator) may be one of these or someone else. Mr. Hansen suggested that it could be made clearer who the client is.
- Mr. Koktvedgaard noted that sub-paragraph (ii) of paragraph 42(c) of the draft mentions "reasonable assurance" in the context of qualifying a limited assurance report. He commented that this may be confusing and asked for the language to be reconsidered.
- Mr. White noted that the requirement in paragraph 26(a) of the draft regarding the need for

²¹ ISAE 3402, *Assurance Reports on Controls at a Service Organization*

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additional explanation in the assurance report was limited to cases when the report is prescribed by law or regulation. He commented that in all cases the practitioner's communication should be clear to avoid misunderstandings. Ms. Hillier agreed, noting that as part of engagement acceptance and continuance procedures, the practitioner needs to be satisfied with a range of things, such as criteria, available evidence etc., and that this would include the format and wording of the report if that is to be determined by others. The requirement in paragraph 26(a) is particularly aimed at phrases commonly imposed by law and regulations, such as "certify."

- Mr. Bauman noted that the table in the agenda paper depicting the basic work-flow for assurance engagements minimizes the difference between limited assurance and reasonable assurance. In his view, the difference could be vast, but this is not immediately evident from the table. ISAs have some 500 requirements, but ISAE 3000 has far fewer for limited assurance engagements. He asked if management could request the practitioner to do very little work and on that basis alone conclude that "nothing has come to my attention;" for example, is the required understanding of the entity the same and does the engagement team need to have a fraud risk brainstorming session as required for an audit? Ms. Hillier responded that ISAE 3000 is less directive, but does require practitioners to obtain a meaningful level of assurance and to retain the capacity to dig deeper if something comes to their attention.
- Mr. Fleck added that it is very difficult to explain in a limited assurance engagement what has been done and the value that intended users should attach to the output. In his view, it is important therefore that practitioners be satisfied at the engagement acceptance or continuance stage regarding the procedures to be performed and the way they will be described in the report.
- Prof. Schilder responded that limited assurance engagements for various subject matters are still evolving, and that flexibility is therefore needed, but that subject matter-specific ISAEs can be more prescriptive. Ms. Hillier added that, although the IAASB is revising ISAE 3000 in light of experiences to date, feedback has been very positive about the influence extant ISAE 3000, albeit a more high-level and less detailed standard than the ISAs, has had on practice in making practitioners think through all the significant issues in new areas where it is in the public interest for practitioners to be able to perform assurance engagements.
- Mr. Damant noted that determining the conditions under which non-accountants should be allowed to use ISAE 3000 is an important matter that the IFAC Board should also consider as it is broader than just ISAE 3000.

REPORT BACK

Ms. Hillier drew attention to matters noted in the report back in the CAG agenda material.

XBRL (Item Q)

Mr. Damant noted that, due to the timing of the meeting, the discussion on the topic of XBRL would be postponed until the March 2011 meeting. Representatives are invited to send any

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comments they wish to raise on the distributed agenda material to IAASB Staff Kathleen Healy.

PIOB Remarks

Dr. Marten thanked the CAG for welcoming him to observe his first CAG meeting. He noted the PIOB would be most interested to hear of the progress made on a number of agenda items. Regarding the limited assurance discussions, he noted the issue that audit profession and interested parties seem to have a clear view of what is meant by limited assurance and will need to balance that with the need for users and entities to have an understanding of it. He thanked the Representatives for their comments on the review and compilation standards, noting his view that it was particularly helpful to hear the views of SMEs and regulators.

He noted he will report back to the PIOB that the CAG was generally supportive of IAPS 1000, and was pleased to hear from IOSCO and IAIS in this regard. He also reported his impression that the CAG did not have major concerns over the possible content of the IAASB's future strategy and work program at this stage.

Dr. Marten also remarked that he was pleased to have had the opportunity to observe the CAG's discussion in its Closed Session, and will report back on the discussion to the PIOB.

Dr. Marten concluded by saying he was deeply impressed about the open and constructive atmosphere of the CAG, including its culture and turn. He strongly supported comments made by the Representatives and Prof. Schilder that this was largely due to the efforts of Mr. Damant during his Chairmanship. He closed by congratulating the Representatives on a successful meeting, and wishing Mr. Damant the best in his future endeavors.

Closing

Mr. Damant and Prof. Schilder thanked the CAG Representatives for their contribution to the meeting. Mr. Damant noted that the next IAASB CAG meeting is scheduled for March 8-9 in New York and will be chaired by Ms. de Beer.

Mr. Damant thanked Prof. Schilder and Ms. Hillier and the IAASB Task Force chairs for their contributions to the meeting.

Mr. Damant closed the meeting.