

Preface to International Standards on Quality Control, Auditing, Assurance and Related Services – Issues Paper

Introduction

1. This Issues Paper provides an overview of the comments received and related issues on the exposed *Preface to International Standards on Quality Control, Auditing, Assurance and Related Services* (“Preface”) that have not yet been discussed by the IAASB.
2. It summarizes common or significant comments received and the proposed response, and is intended to facilitate the discussion of issues by the IAASB. The related and other additional editorial changes made to the proposed Preface are identified in the marked version thereof in Agenda Item 6-B. A listing of all comments received and the proposed disposition is included for informational purposes as Agenda Item 6-D.

Background

3. At the May 2003 IAASB meeting (New York), the IAASB commenced review of the comments received on the exposure draft (ED) Preface and of the proposed revisions thereto. At that meeting, the IAASB agreed that:
 - the proposed Preface should not be held back until the bold and ordinary type lettering issue has been resolved. The Preface should be independent from this issue and should be finalized at the next IAASB meeting;
 - the proposed two-thirds voting majority should be retained;
 - the proposed Preface should be changed to provide for a quorum of 12 members to be present in person at a meeting; and
 - the proposed Preface should be changed to indicate the preference that members should be present in person, then by way of telephone link and lastly, by way of proxy.
4. Staff has processed the changes recommended by the IAASB at its May 2003 meeting. These changes have been black lined and highlighted in the marked version of the Preface in Agenda Item 6-B for reference by the IAASB. The remaining changes identified in the marked version of the Preface are the proposed revisions carried forward from the agenda material presented at the May 2003 IAASB meeting.

Overview of Comments Received and Related Issues

5. The following material represents the remaining issues the IAASB is asked to consider in its approval of the revised Preface. It has been carried forward, with only minor updates, from the agenda material presented to the IAASB in May 2003.

SIGNIFICANT CONCERNS

6. The most significant remaining issues put forward by respondents to the proposed Preface pertain to: (1) voting; and (2) the restructuring of the handbook. These issues are addressed first, with the other remaining specific issues addressed in the order the related paragraph(s) appears in the Preface.

VOTING (PREFACE PARAGRAPHS 25-26)

7. *Approval Requirements for Other Pronouncements – Discussion Papers.* Some respondents also suggest that the process for approval of non-authoritative material, including discussion papers, follow a less time-consuming process, and that the need for the

IAASB to ‘approve’ discussion papers is not necessary. It was suggested that the public interest can be met either through a ‘negative clearance’ mechanism or a voting process that does not require the involvement of the entire IAASB.

Staff Comment: Paragraph 25 of the revised Preface states that the approval of discussion papers requires only a majority of members present. It is believed that such a mechanism is effective and that a ‘negative clearance’ mechanism would be a less transparent alternative. The proposed voting process for discussion papers and other pronouncements is also comparable to the voting rules adopted by the IASB. Accordingly, no change is recommended.

Does the IAASB agree with the approach taken?

8. ***Dissenting Opinions.*** One respondent believed that all dissenting views should be included in the minutes, and not be at the option of the members as proposed, in the interest of improved transparency. One other respondent further suggested that dissenting opinions be included in exposure draft to further the debate by commentators

Staff Comment: The option to exclude the view of dissenting opinions in IAASB minutes has been removed as suggested in order to strengthen the transparency of IAASB processes. The suggestion to include dissenting opinions in exposure drafts was not adopted to avoid giving greater weight to dissenting views on an exposure draft than to the supportive views.

Does the IAASB agree with the proposed change to require the inclusion of dissenting opinions in the minutes? Does the IAASB agree with the position taken to continue the exclusion of dissenting opinions in exposure drafts?

HANDBOOK RESTRUCTURING

9. A total of 16 respondents addressed the proposed restructuring of the handbook. The majority of respondents (11) indicated that they believe the proposed restructuring is understandable and effective. One respondent felt there was no need to group standards differently as this may lead to confusion. The remaining respondents expressed concern with the proposed restructuring in relation to:
- The confusion that may arise from the number of categories and acronyms;
 - The proposal to continue to include review engagements under the “umbrella” of ISAs;
 - The separation of audit and other assurance engagements; and
 - The definition of related services.
10. ***Categories and Acronyms.*** Four respondents commented on the proliferation of acronyms and abbreviations that will arise from the proposed restructuring, and on the proposed numbering system. The consistently expressed concern was that the restructuring may be confusing to individuals not familiar with the work of the IAASB and that it might not be easy to explain to users, regulators and practitioners.

Staff Comment: While the proposed restructuring does introduce a number of new acronyms, there is benefit to codifying a structure to the various standards, practice statements and other pronouncements issued by the IAASB. A number of alternatives were considered by Staff in developing the proposed structure; the proposed model

considered to be the most meaningful. Greater familiarity with the proposed structure gained over time may reduce the concern over the proliferation of acronyms. Accordingly, no change has been made.

Does the IAASB agree with the position taken?

11. **Review Engagements.** Two respondent expressed concern over the concept of including reviews under the same series of standards as audits and, in particular, the resultant communication that a review, which is not an audit, was conducted in accordance with ISAs. These respondents recommended that standards for review engagements be addressed under a newly established separate category of “Standards for Review Engagements” or, alternatively, grouped within the category of “Other Assurance Engagements.”

Staff Comment: Staff acknowledges that there may be benefit to splitting reviews of financial statements from audits of financial statements, whereby a separate framework governing the conduct and reporting of a review engagement is established. To accomplish this, the box in the appendix to the exposed Preface outlining the proposed structure of the handbook would be amended as follows:

- ISA 100 would be modified to include only audits of historical financial information;
- A separate category International Standards for Review Engagements (ISREs) 1500 (an ISA – 100 type category) would be created to address reviews of historical financial statements; and
- ISREs would be re-labeled 1600-1699 (current ISA 910).

However, Staff notes that there is not strong overall support for such a change in the responses to the exposure draft, and that such a change may add little or no practical benefit that cannot be accomplished through the proposed development of ISA 100 (to be derived from ISA 120 and ISA 200). Further, establishment of a new category would be contrary to those respondents who claim there are already too many categories and acronyms.

ISA 910 paragraph 26 (d) presently requires the review report to include a reference to International Standards on Auditing *applicable to review engagements*. Although clarity in reporting may be enhanced by provided a reference to “International Standard for Review Engagements”, Staff is not aware of any circumstances in which the present structure has caused confusion.

On balance, Staff is of the opinion that there is insufficient support to establish a new category for review engagements.

Does the IAASB agree with the position taken?

12. **Audit and Assurance.** Two respondents expressed concern over the separation between auditing standards and other assurance engagement standards. The views were that the proposed structure is likely to result in duplication in relation to “topics that apply to all subject matters,” such as use of experts, planning and using the work of another auditor, and that such separation is artificial and unwarranted.

In contrast, one respondent strongly recommended that auditing and assurance standards be clearly separated, as IAASB’s auditing standards are of particular importance. The concept

of an “assurance framework,” addressing both sets of standards, does not further the objectives of the IAASB.

Staff Comment: **The IAASB has recognized the potential for overlap in some standards in its prior deliberations. However, it has been demonstrated that the standard setting process for auditing standards is significantly slowed and made more complex when attempting to develop standards that would be applicable to both audit and other assurance engagements in general. At this time, the ability for IAASB to concentrate on the development of auditing standards, separate and distinct from other assurance standards, may outweigh the conceptual arguments and the risk of potentially duplicative guidance. Accordingly, no change is proposed.**

Does the IAASB agree with the position taken?

13. **Related Services.** Three respondents noted that the proposed restructuring was unclear as to what would be included under related services and expressed concern that the term “related services” may be inappropriate given that compilation and agreed-upon procedures are not considered “related to” assurance services. One of these respondents highlighted the issue that the term could be confusing in light of the interaction of the independence framework in the *IFAC Code of Ethics for Professional Accountants* and the assurance framework, noting that a reader may presume, for example, that by virtue of being a “related service,” the threats and safeguards regarding independence associated with an agreed-upon procedure or compilation engagement would be the same as that for an audit. It was suggested that the name of the category be changed to “Non-assurance Services Framework” or simply omitted from the structure of the handbook.

Staff Comment: **The intention of the term “related services” was to address other services provided by professional accountants that are ordinarily undertaken in association with the provision of auditing and assurance services. Paragraph 4 of the current ISA 120 establishes the distinction between audits and related services (agreed-upon procedures and compilations) by virtue of the intention to express assurance.**

Staff does not believe the proposed change to “Related Services Framework” is appropriate. It may result in problems in relation to the mandate of the IAASB and may inappropriately imply that the IAASB will seek to expand the breadth of such standards beyond those contemplated (e.g., to include consulting engagements).

Staff however has redefined the definition of International Standards on Related Services in paragraph 10 of the revised Preface to state “ISRS are to be applied to compilation engagements and engagements to apply agreed upon procedures to information, and other related services engagements.”

Does the IAASB agree with the position taken and the proposed change?

OTHER SPECIFIC ISSUES

Introduction (Preface Paragraphs 1-3)

14. **IAASB Relationship with IFAC.** Two respondents expressed the view that the public interest dimension should be further emphasized in the Terms of Reference and that the IAASB should not be seen as setting the standards “on behalf of IFAC” but rather characterized as being an “independent standard setter.”

Staff Comment: Recent discussions between the IAASB and the IFAC Board have clarified the IFAC Board’s view that the IAASB acts on behalf, or under the auspices, of IFAC. Paragraph 2 however has been amended to define the IAASB as being responsible for developing and issuing pronouncements “under its own authority.” The proposed revision retains the fact that the IAASB is a part of IFAC, but strengthens and clarifies the fact that the IAASB independently issues pronouncements. This change is intended to minimize any perceived limitation on its public interest role.

A corresponding change has been made to the first paragraph of the revised Terms of Reference, stating that the IAASB “functions as an independent standard setting body under the auspices of IFAC.”

Does the IAASB agree with the proposed changes?

15. ***Working with National Standard Setters.*** Some respondents felt the Preface would be improved if it included greater prominence of, and a stronger message regarding, the IAASB’s relationship with national standard setters, their importance to the convergence and endorsement process and of the joint work they often undertake with the IAASB. Respondents to the proposed Terms of Reference also recommended that the objective of convergence of international and national standards and the cooperative role of the IAASB with national standard setters should be strengthened and clarified.

Staff Comment: A new paragraph has been added at the end of the introduction section based on the suggestion of the respondents. This addition also further explains and elaborates on the first sentence in the fourth paragraph of the proposed Terms of Reference, which otherwise is not addressed in the proposed Preface.

Does the IAASB agree with the additional paragraph addressing the work with national standards setters?

16. ***Relationship of IAASB Pronouncements with Local Laws and Regulations and the Obligations of Member Bodies.*** Paragraph 3 of the exposed Preface discusses the relation of IAASB pronouncements with local laws and regulations as well as the obligation of member bodies in relation to adoption and compliance with IAASB pronouncements. Some respondents noted that the discussion was confusing. A perceived “weakening” of the IAASB pronouncements as being overridden by local laws and regulations was also noted. Some respondents expressed confusion with the reference to member body obligations in the text of the exposed Preface.

Staff Comment: In relation to the discussion on laws and regulations, paragraph 3 has been strengthened to clarify that a professional accountant should not represent compliance with IAASB pronouncements unless the professional accountant has complied with all of the requirements of such pronouncements.

The discussion regarding member body compliance and the related footnote has been deleted. The IFAC Board is expected to issue a series of Statement of Members Obligations to address the requirement of membership with IFAC. Accordingly, reference to member body obligations in the revised Preface is considered unnecessary and has been removed.

Does the IAASB agree with the approach taken?

IAASB (Preface Paragraphs 4-7)

17. ***Nomination Process, Term, etc. for Membership on the IAASB.*** Three respondents suggest that information about the membership requirements of the IAASB be expanded to include items such as: qualifications to be a member; nomination process of the Chair and Vice-Chair, term served by the Chair, reappointment and succession, description of the roles and responsibilities of the Chair, Vice-Chair, TAs, CAG, etc. Comparable suggestions have also been made by respondents on the exposed Terms of Reference.

Staff Comment: Paragraph 5 of the revised Preface has been amended to include additional information about the basis for IAASB member selection and the terms of their appointment. As an editorial matter, this paragraph has also been redrafted to clarify that all candidates put forward for appointment are considered by the IFAC Nominating Committee.

Details of the nominating process and the roles and responsibilities of the Chair, however, are the responsibility and authority of the IFAC Board. They are considered to be matters separate from the intended purpose and scope of the proposed Preface. Accordingly, no change has been made in this regard.

Does the IAASB agree with the approach taken?

Authority Attaching to ISAs (Preface Paragraphs 8-16)

18. ***Materiality.*** Differing views were expressed concerning the exclusion of a discussion of materiality from the exposed Preface. One respondent recommended that the phrase “ISAs need only be applied to material matters” be reinstated in the Preface, one respondent was unclear as to the rationale for its exclusion, one respondent supported the exclusion from the Preface but agreed with the presentation of the matter in the proposed Operations Policy, and one recommended its exclusion entirely.

Staff Comment: The rationale for excluding the concept of materiality from the exposed Preface was based on the fact that ISAs are intended to be applied in the audit of financial statements on matters irrespective of their materiality. For example, ISA 545, *Auditing Fair Value Measurements and Disclosures*, is applicable to all audits irrespective of the materiality of fair values to the overall financial statements. The application of specific basic principles and essential procedures however will vary depending on the materiality of the matter being considered. Consequently, it was not considered appropriate to establish a “blanket” statement on materiality for IAASB engagement standards. Further, paragraph 15 of the revised Preface makes it clear that any limitation of the applicability of a specific standard is made clear in the introductory paragraph to that standard.

No change is recommended.

Does the IAASB agree with the position taken?

19. ***Justifying Departure from Standards.*** Paragraph 14 of the Preface requires professional accountants to be prepared to justify a departure from engagement standards. Some respondents recommend that the paragraph should be amended to require the professional accountant to fully disclose the details of that departure in their report, including the reason(s) for the departure(s).

Several respondents also suggested that the phrase “in extremely rare circumstances” used in paragraph 14 when describing the need to depart from engagements standards to be replaced by the phrase “in exceptional circumstances,” which is consistent with the terminology used elsewhere in IAASB pronouncements.

Staff Comment: The auditor’s reporting obligations are established by subject specific engagement standards (in the case of auditor’s reports, ISA 700). Establishing reporting requirements in the proposed Preface is not considered appropriate. Accordingly, no change has been made in this regard. The phrase “in extremely rare circumstances” has been changed to “in exceptional circumstances” as suggested.

Does the IAASB agree with the position taken and the proposed change?

20. **Public Sector Perspective.** One respondent disagreed with retention of the present practice of using Public Sector Perspectives (PSPs) to vary the application of a standard in the public sector, and felt that public sector issues should be dealt with in engagement standards themselves such that all engagement standards are fully applicable in both public and private sectors.

Staff Comment: IFAC/IAASB are presently developing processes with the International Organization of Supreme Audit Institutions (INTOSAI), the objectives of which are to obtain INTOSAI support and input during the development of exposure drafts and to remove the need for PSPs. The IAASB will be asked to consider proposed operating procedures with INTOSAI in July 2003. The IFAC Public Sector Committee and the use of PSPs are expected to continue until October 2003.

To avoid the need to re-expose the Preface in the near future, a footnote has been added to paragraph 16 of the Preface which highlights the possible change in the IAASB’s relationship with the Public Sector Committee and the use of PSPs as a result of developments with INTOSAI.

Does the IAASB agree with the proposed change and the wording of the proposed footnote?

Authority Attaching to Practice Statements (Preface Paragraphs 17-19)

21. **Authority of Practice Statements.** Several respondents indicated the need for a statement that practice statements do not establish new basic principles or essential procedures but serve to provide guidance on the application of standards. Several other respondents acknowledged the strengthening of the authority of practice statements in paragraph 19 of the exposed Preface and suggested that the authority of practice statements be clarified to explain that they also provide interpretive guidance. One respondent also felt the addition of the requirement that practitioners be aware of and consider practice statements may be overly onerous in the context of litigation.

Staff Comment: A new paragraph (17) was added to the revised Preface stating that practice statements do not establish new basic principles or essential procedures¹. The description of practice statements has also been amended to include the statement that

¹ The phrase ‘basic principles and essential procedures’ may require amendment depending on the conclusions reached by the IAASB on Agenda Item 5 – Proposal for Improving the Clarity of IAASB Standards.

practice statements provide interpretive guidance. This change is considered a logical amendment given the proposed paragraph 19, which expands the professional accountant’s compliance considerations regarding practice statements.

Editorial changes have also been made to combine and shorten the paragraphs that describe IAEPSs and IRSPSs.

Does the IAASB agree with the proposed changes?

Other Pronouncements (Preface Paragraph 20)

22. ***Interpretations.*** Two respondents suggest that the IAASB should establish a procedure for the publication of interpretive publications, with a modified or “negative clearance” due process for approval.

Staff Comment: The establishment of another tier of publications, “interpretation,” in addition to practice statements may result in confusion. As described above, the description of practice statements has been amended to include the statement that they provide interpretive guidance. Accordingly, no change has been made.

Does the IAASB agree with the position taken?

23. ***Discussion Papers.*** Two respondents suggest that the IAASB should not restrict its output to Discussion Papers only but should allow for the production of other material as appropriate. They have suggested a change in the title of the section dealing with Discussion Papers to “Authority Attaching to Other Pronouncements Issued by the IAASB.”

Staff Comment: Staff agrees with this suggestion and envisages that the IAASB may wish to issue other pronouncements in addition to Discussion Papers, including, for example, IAASB Audit Alerts, Audit Technique Studies, Research Studies or Staff Bulletins.

The caption to paragraph 20 of the proposed Preface has been changed from “Discussion Papers” to “Authority Attaching to Other Pronouncements Issued by the IAASB.” Amendments have also been made to establish Discussion Papers as an example of the type of non-authoritative document that may be issued by the IAASB.

Does the IAASB agree with the proposed change?

Working Procedures (Preface Paragraphs 21-23)

24. ***Task Force Assignment, Joint Task Forces and Staff-only Projects.*** Two respondents noted that the working procedures of the IAASB should be expanded to recognize the use of joint task forces with national standard setters and should also allow for the possibility of the IAASB not having members on a task force, or at least not necessarily chairing task forces. In addition, one respondent recommended that scope also should be provided for staff-only projects.

Staff Comment: These comments reflect the present practice of the IAASB, with the exception of using task forces that have no members of the IAASB. No change has been made to explicitly provide for staff-only projects or for non-IAASB members to act as a Chair of a task force. The current wording of paragraph 21 implicitly permits the use of alternate arrangements for task forces by virtue of the term “ordinarily” in the second sentence of paragraph 21.

Minor editorial changes to paragraph 21 of the proposed Preface have been made as suggested by the respondents to give recognition to joint projects.

Does the IAASB agree with the position taken and the proposed editorial changes?

25. ***Effective Date of Practice Statements.*** Several respondents expressed concern with the fact that practice statements are effective from the date they are issued. Respondents commented that, while practice statements do not introduce new requirements, an appropriate commencement date should be given to accommodate training requirements, implementation, and translation. Respondents also noted that this concern is compounded by the proposed paragraph 19 that states “professional accountants should be aware of and consider practice statements applicable to the engagement” and to justify departure there from. It was also noted that an effective date for practice statements would be particularly beneficial in the circumstance where a practice statement is not exposed for public comment, as permitted in paragraph 21 of the proposed Preface.

Staff Comment: This matter was briefly discussed by the IAASB at its March 2003 meeting in relation to the IAPS on Compliance with IFRSs. It was agreed that, subject to further debate, the practice of designating an “issuance date” to provide for necessary translation and communication of the content of a final practice statement would be adopted.

It is proposed that paragraph 22 of the proposed Preface be amended to state that practice statements will be effective 60 days after the end of the month they are approved by the IAASB.

Does the IAASB agree with the position taken and the proposed change?

26. ***Additional Clarification - IAASB Consultative Advisory Group, Forum of Firms and IAASB Technical Advisors.*** Many respondents requested that additional information be provided regarding the IAASB CAG, Forum of Firms and a description and role of technical advisors at the point they are introduced in the Preface.

Staff Comment: Additional information had been added through footnotes to paragraph 5 for the Forum of Firms, paragraph 21 for CAG and paragraph 26 for technical advisors.

Does the IAASB agree with the approach taken and the descriptions proposed for these terms?

27. ***The Decision to Re-exposure.*** One respondent observed that paragraph 22 was unclear as to whether a vote is required to decide on re-exposure, and recommended that the Preface explicitly require the IAASB to vote on whether an exposure draft should be re-exposed.

Staff Comment: The revised Preface has been amended as suggested to require a vote by the IAASB as to whether an exposure draft should be re-exposed. At least one other national standard setter follows a similar process.

Under the proposed revised wording in paragraph 22, a vote by the IAASB will, in most circumstances, be required as there ordinarily are substantive changes to a document arising from the public exposure process. The term “substantive change” however will not be defined, but rather left as a matter subject to the debate by the

IAASB based on the circumstances of the situation. As a practical matter, “substantive change” may ordinarily be interpreted to mean the establishment of significant new basic principles and essential procedures that were not otherwise contemplated in the exposure draft or that are responsive to substantial ED comments. The IAASB would then be asked if they agree that re-exposure is not necessary in light of these changes.

Does the IAASB agree with the proposed change?

Language (Preface Paragraph 26)

28. One respondent recommended that paragraph 26 clarify that the English language version of any approved pronouncement is the sole authoritative version.

Staff Comment: Minor change made to paragraph 26 as suggested.

Does the IAASB agree with the proposed editorial change?

Other

29. ***Appendices to Engagement Standards and Practice Statements.*** One respondent requested that the Preface include a definition of the nature of appendices to engagement standards and practice statements, and in particular, whether the guidance included in ISA appendices may be binding on the auditor.

Staff Comment: The description in paragraph 15 has been amended to explicitly include appendices as part of a Standard through the following statement: “Unless otherwise indicated, the entirety of the text contained therein, including appendices, is considered to be applicable to the purpose of the Standard”.

Does the IAASB agree with the position proposed change?

EDITORIAL CHANGES

30. Other editorial changes have been processed based on the observations and suggestions of the respondents to the exposure draft. These changes include the consistent use of “IAASB” and “the Board,” the use of the phrase ‘basic principles and essential procedures’ in place of the term ‘requirements’², clarifying the use of the term “papers,” referring to “auditing and other assurance engagements,” replacing “historic” with “historical,” and so forth.

Does the IAASB agree with the proposed editorial changes highlighted in the marked version of the draft Preface?

² See footnote 1.