

**Minutes of the Meeting of the****INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD****Held March 17-21, 2003****At the Sheraton Towers Southgate, Melbourne, Australia**

	<b>Members</b>	<b>Technical Advisors</b>
<i>Present:</i>	Dietz Mertin (Chair)	Wolfgang Böhm (Mr Mertin)
	Denise Esdon (Vice Chair)	Cédric Gélard (Mr Trémolière)
	John Archambault	Jon Grant (Mr Plaistowe)
	Philip Ashton	Diana Hillier (Mr Ashton)
	Ana Maria Elorrieta (except Mar 21)	Susan Jones (Mr Noonan)
	Jan Bo Hansen	Karen Lauf (Mr Kana)
	Gen Ikegami	Paul Lohnes (Mr Desautels)
	Suresh Kana	Emilio Palma (Mr Tizzano)
	John Kellas	Richard Mifsud (Mr McPhee)
	Ian McPhee	Sylvia Smith (Mr Kellas)
	Edmund R Noonan	George Tucker (Ms Esdon)
	Ian Plaistowe	Hans Verkruijsse (Mr Dassen)
	Roger Simnett	Yuichi Yamamoto (Mr Ikegami)
	Gérard Trémolière	Xi Wu (Mr Yang)
	Zhiguo Yang	
<i>Absent:</i>	Roger Dassen	John Fogarty (Mr Hansen)
	Denis Desautels	
	Roberto Tizzano	
	<b>Invited Guests</b>	
<i>Present:</i>	René Ricol, President, IFAC (Mar 17)	
	Ian Ball, Chief Executive, IFAC (Mar 17)	
	<b>IFAC Technical Staff</b>	
<i>Present:</i>	James Sylph (Technical Director)	
	James Gunn	
	Alta Prinsloo	
	Ashley Carpenter	
	Jan Munro	
	Michael Nugent	
	Ken Siong (except Mar 21)	
	Gill Spaul	

## 1. Chair's Greeting and Opening Remarks

Mr Mertin opened the meeting.

The minutes of the meeting of the IAASB held on December 8-12, 2002 in Miami, Florida were approved as circulated.

## 2. Quality Control

Ms Elorrieta presented a summary of actions undertaken by the Quality Control Task Force in response to decisions made by the IAASB during its December 2002 meeting.

Ms Elorrieta noted that the Task Force originally intended to issue the proposed quality control standards, *International Standards on Quality Control 1* (ISQC 1), and revised ISA 220, *Quality Control for Audit Work*, in conjunction with the IFAC Board's proposed *Statement of Membership Obligations – No 1* (SMO 1). Due to further deliberation required by the IFAC Board, SMO 1 will now be issued separately. Mr Sylph added that the IFAC Board agreed that the IAASB should consider its quality control standards in the absence of SMO 1.

Ms Elorrieta indicated that comment letters from the Officers of IFAC and the SMP Task Force were received only one week prior to this meeting. She indicated that the Task Force had not had an opportunity to fully address the content of these letters in advance of the meeting, but that she would raise key matters at the appropriate time during this meeting's discussions.

The IAASB reviewed the proposed revised ISQC 1 and commented on the matters raised in the accompanying issues paper. In addition to structural and editorial changes, the IAASB agreed that:

- Communication processes (identified in paragraph 7) constitute an important aspect of firms' system of quality control and therefore should be included within the preceding black letter paragraph.
- Additional guidance should be provided on how to implement the basic principle/essential procedure dealing with leadership and responsibilities within the firm (paragraph 12) in the context of small practices.
- Specific aspects (e.g., business reputation and practices, past experience with the client, etc.) that should be considered when conducting an evaluation of the integrity of a client, and the related documentation requirements, should be included in the explanatory material pertaining to client acceptance and continuance.
- Additional guidance pertaining to the rotation of engagement partner in the circumstances of small practices should be provided.
- The proposed section on independence should be described in the context of addressing threats to auditor independence, with appropriate reference to the relevant section of the IFAC Code. In addition, the proposed requirements for engagement partner rotation should recognize its objective of addressing the familiarity threat to auditor objectivity.
- The guidance on human resources should specify more precisely what qualities (i.e., competency and integrity) personnel should demonstrate.
- Guidance should be provided that specifies the requirement for the engagement partner to document the performance of, and findings arising from, engagement review activities.
- Explanation of the term "engagement quality control review" in relation to some of the more common names attaching to such a function should be addressed in the explanatory memorandum that would accompany the ED.

- Additional guidance should be provided on policies and procedures that require a period of time to elapse before an engagement quality control review partner can assume the responsibility and role of an engagement partner.
- The guidance dealing with the completion of an engagement quality control review should clarify that completion of the review includes the resolution of disagreements between the engagement quality control reviewer and the engagement team.
- The explanatory guidance surrounding monitoring should emphasize that monitoring activities are continuous and ongoing. In addition, clarification between the process of monitoring and the process of periodic inspection of completed engagements should be made.
- Additional guidance should be provided on the fact that a significant individual deficiency may be a factor that indicates the need for further investigation and corrective action. The explanatory material should also clarify that individual deficiencies found in any individual engagement, in and of themselves, do not indicate a deficiency in the firms' quality control system.

The IAASB then reviewed the proposed revised ISA 220. In addition to structural and editorial changes, the IAASB agreed that:

- Additional explanatory guidance that emphasizes the responsibility of the engagement partner to assume responsibility for the quality of the engagement should be provided in the introductory section of the proposed standard.
- Additional guidance on the implementation and documentation requirements of the actions required by the Standard should be provided.
- Clarification should be made of the interrelationship between the responsibilities of the engagement partner and the nature and extent of reliance that can be placed by the partner on the firm's quality control policies and procedures.
- The guidance which indicates that the engagement partner should perform an overall review of the engagement (paragraph 21) should be a black letter paragraph.
- Consideration should be given to confidentiality issues when consulting inside and outside the firm. In addition, guidance on dispute resolution should be provided.
- The guidance indicating that the engagement partner is to be satisfied that the engagement quality control review has been performed (paragraph 28) should be a black lettered paragraph.

The effective date of the proposed ISQC 1 and ISA 220 was agreed to be 31 July 2004.

With regard to the finalization of the proposed Standards, it was agreed that an electronic version of the revised proposed ISQC 1 would be distributed to members, with comment to be provided back to the Task Force by no later than 3 April 2003. The Task Force will present a revised ISQC 1 and ISA 220 to the IAASB at its May 2003 meeting for approval for exposure.

### **3. Assurance Engagements**

In the absence of Mr Dassen, Mr Noonan presented the agenda material on assurance engagements.

Mr Noonan provided a summary of action undertaken by the Assurance Task Force in response to previous decisions made by the IAASB and of the overall changes to the proposed Framework and ISAE since December 2002. Mr Noonan noted that a comment letter based on the published agenda papers had been received, which expressed concern over the definition of assurance

engagements and the introduction of mutual consent engagements, and argued for the concept of “incidental assurance” and a description of consulting engagements to be reinstated. Mr Noonan noted that the Task Force had considered these comments and that they resulted in no change in its views.

The IAASB reviewed and commented on the issues raised in the accompanying issues paper. The IAASB extensively discussed the concepts surrounding mutual consent engagements. Discussion included the impact on the public interest and whether the proposed hurdle for acceptance of a mutual consent engagement is appropriate, e.g., the responsibility for the practitioner to be satisfied about there being a rational purpose for the engagement. The IAASB also deliberated the proposed definition of assurance engagements, assurance engagements that can be accepted and non-assurance engagements.

The IAASB considered various options in order to achieve a common agreement on these matters, including:

- defining only those assurance engagements that can be accepted;
- retaining the definition of assurance engagements as proposed, but deleting the concept of mutual consent engagements;
- retaining the definition of assurance engagements as proposed, but deleting the concept of mutual consent engagements, and reinstating the concept of incidental assurance and the description of consulting engagement (as proposed to the IAASB in December 2002 but adding a requirement for such incidental assurance engagements for restriction of the report); and
- retaining, but revising the framework around, mutual consent engagements.

The IAASB agreed to the third option noted above. The restriction on the report was done at the behest of the Board.

The IAASB reviewed the proposed Framework and ISAE 2000. In addition to editorial changes, the IAASB agreed that the black letter guidance on obtaining written representations from the responsible party contained in IASE 2000 should be replaced by the higher level principle in ISA 580 which states “the auditor should obtain appropriate representations from management”, conformed appropriately to the terminology used in ISAE 2000.

The Assurance Task Force presented a redraft of the proposed Framework and ISAE based on the decisions and comments of the IAASB and highlighted additional editorial changes made by the Task Force. In addition to further editorial suggestions, the IAASB agreed that any written report issued for an engagement involving incidental assurance is to be restricted to, and not distributed beyond, the intended users.

Subject to the changes discussed and amending changes to the explanatory memorandum, the IAASB agreed unanimously to issue the proposed Framework and ISAE 2000 for public exposure with a three month comment period.

#### **4. Review of Interim Financial Information**

Ms Esdon presented a summary of action undertaken by the Task Force in response to previous recommendations made by the IAASB and of the overall changes to the proposed ISA from the December 2002 version.

In addition to proposed structural changes and other editorial matters, the IAASB agreed that:

- Additional explanatory material in the introductory paragraph of the revised ISA should be added to further explain the difference between the proposed ISA and ISA 910, *Engagements to Review Financial Statements*, and the circumstances when each ISA is to be used.
- The structure and content of the explanatory material pertaining to proposed paragraph 8 should be more aligned to the main points of that paragraph, specifically in relation to the consideration by the auditor of the identification and assessment of the risk of material misstatement.
- The proposed black letter paragraph requiring the auditor to obtain a written engagement letter should be conformed to the guidance presently contained in ISA 580, *Management Representations*.
- The proposed procedure for the auditor to obtain reports from other auditors (paragraph 14) should be clarified and guidance provided how this would be operationalized in practice.
- Specific inquiries about going concern should be added as a black lettered paragraph to the proposed ISA.
- The proposed guidance pertaining to the first year appointment (paragraph 11) should also address risk assessments in addition to the guidance on internal control. It was also agreed that additional guidance around other matters for consideration in a first time engagement, including the important elements of obtaining an understanding of the entity and its environment, should be added.
- The proposed guidance on management representation should state that the auditor also obtains a statement from management that it acknowledges their responsibility for the interim financial statements.
- The guidance pertaining to the situation where the auditor is unable to complete a review should be established as a black lettered paragraph, and additional guidance should be provided on how the auditor communicates such matters.
- The Task Force should consider providing reporting guidance when the preceding year's audited financial statements have a reference to a going concern issue, and to include guidance on the consideration of a using an emphasis of matter paragraph.

The IAASB discussed the proposed components of the auditor's reports and related illustrative example. The IAASB suggested that the title to report should be changed to "independent auditor's review" and that the introductory paragraph of the report should include a reference to the nature of the financial statements and the purpose of their preparation.

The Task Force agreed that it will present a revised ISA to the IAASB for approval as an exposure draft at the May 2003 meeting.

## 5. Compliance with IFRS

Staff presented a summary of comment letters received on the proposed IAPS, *Reporting By Auditors on Compliance with International Financial Reporting Standards*, that was exposed for public comment. Staff noted that three additional comment letters were received subsequent to the preparation of the presented agenda material. Staff indicated that the comments expressed therein were similar to those of other comment letters.

The IAASB reviewed the proposed revised IAPS, commented on the issues raised in the accompanying issues paper and proposed additional amendments.

In addition to editorial changes, the IAASB agreed that:

- The example opinion should illustrate when management asserts to compliance with IFRSs and a national financial reporting framework and the opinion on IFRSs is qualified and the opinion on the national financial reporting framework is unqualified.
- The proposed guidance should be amended to state that the reference to compliance with IFRS misleads readers of the financial statements because it contains materially inaccurate information, unless there is adequate quantification of the effects to the financial statements.

The IAASB deliberated the need to include an effective date on an IAPS given practical matters involving dissemination and translation of pronouncements. As an interim solution, the IAASB agreed that this IAPS will be approved with a 'deemed' issuance date of 1 June 2003. This alternative maintains the principle of Statements being effective upon issuance while providing time for necessary distribution and translation activities. It was agreed that a final decision on a policy regarding effective dates for Practice Statements will be addressed in May 2003 when the IAASB has an opportunity to fully consider comments received on the IAASB exposure draft, *Preface to the International Standards on Quality Control, Auditing, Assurance and Related Services*.

Staff revised the proposed IAPS as presented in the agenda papers to reflect the comments from the IAASB. Subject to minor editorial changes, the IAASB approved the IAPS for issuance as a final Practice Statement. There was one dissenting vote expressed by Mr McPhee and one abstaining vote by Mr Lohnes on behalf of Mr Desautels. Mr McPhee voted against the issuance of the IAPS as the example provided in revised paragraph 10 was considered unsound, in his view, in proposing that an auditor qualify the report on financial statements prepared in accordance with a national reporting framework when the note disclosure in relation to the departures from IFRS was accurate, and not misleading.

## 6. IAPS 1005

Staff presented a summary of action undertaken in response to previous decisions made by the IAASB and of the overall changes made to the proposed IAPS from the December 2002 version, as outlined in the covering agenda issues paper. Staff provided a summary of the comments received from the SMP Task Force Rapid Response Team. The IAASB agreed with Staff's proposed disposition.

In addition to editorial changes, the IAASB agreed that:

- Reference to holding a meeting to discuss fraud may be impractical in the situation of a sole practitioner and, consequently, should be deleted. The concept of the practitioner consideration of fraud should however be retained.
- Proposed guidance pertaining to assistance to the owner-manager by the auditor should be amended to conform to the wording of the IFAC Code of Ethics and that reference to the relevant section of the Code should be included.
- The proposed guidance referring to listed entities should be deleted given the infrequency of such issues addressed by small practitioners.
- The proposed guidance pertaining to ISA 545, *Auditing Fair Value Measurements and Disclosures*, should be expanded to provide additional guidance that the owner-manager remains responsible for the determination and underlying assumptions, and that the auditor takes steps to obtain the owner-manager's agreement and acknowledgement of responsibility.

Staff described the purpose and content of the proposed explanatory memorandum and asked the IAASB to provide comments on that document to Staff after the meeting.

Subject to the editorial changes, the IAASB agreed unanimously to issue the proposed IAPS for public exposure with a three month comment period.

## **7. The Auditor's Report on Financial Statements**

Mr Ashton presented an overview of the Task Force activities since December 2002. He indicated that the objective of the session is to revisit issues on which the IAASB had asked for further clarification, to address remaining issues and the proposed wording of the auditor's report, and to agree on a strategy on revising the guidance on modified reports.

The IAASB deliberated the proposed principle requiring the auditor to report on other reporting responsibilities in a separate section following the opinion paragraph (that is, to prepare a 'split report'), and questioned whether the prescription of format and structure of an audit report is appropriate in an international environment. The IAASB considered the advantages of greater consistency in reporting that could be achieved by prescribing a (split) report format and the need to retain flexibility in reporting options, recognizing recent U.S. thinking on its project on reporting on internal control. The IAASB agreed that the guidance should not require the use of 'split reports', but that they should be strongly encouraged.

The IAASB deliberated the Task Force recommendations that ISA 700 should be revised to address only financial statements prepared in accordance with IFRSs or standards set by recognized standard setting bodies, that 'true and fair view' opinions would be restricted to reports issued under revised ISA 700, and that all other situations would be considered 'other comprehensive bases of accounting' and would fall under the scope of revised ISA 800. The IAASB did not express strong support for the proposed recommendations and requested the Task Force to revisit the proposed definition of an appropriate financial reporting framework. The IAASB also requested the Task Force to further explore the definition of a financial statement 'component', including whether reports on a single financial statement fall under the scope of ISA 700 or ISA 800.

The IAASB agreed that the phrases "true and fair view" and "presented fairly, in all material respects" are to be regarded as equivalent terms. However, more guidance on the meaning of these terms and the judgments necessary for determining whether financial statements meet these phrases should be provided. The IAASB did support the need to provide additional guidance on what the auditor should consider in forming an opinion on the financial statements.

The Task Force provided an overview of the proposed changes to the wording of the auditor's report, and of what changes were recommended not to be made. The IAASB agreed:

- The title of the auditor's report should include the term 'independent' where needed in jurisdictions to clarify the meaning of auditor.
- To the expansion of the description of management responsibilities beyond only a broad statement of responsibility, and in particular, subject to a review of the wording, to the inclusion of a second sentence that further describes management's responsibilities.
- To the proposed changes to the auditor's report section pertaining to the auditor's responsibilities.
- The description of the audit process should be expanded and amplified to reflect current audit methodologies and recent developments in auditing standards (i.e., the proposed audit risk standards).

- To retain the concept that the audit report must be read within the context of the financial statements and related notes, but requested the Task Force to clarify the proposed language.
- That the reference to “overall presentation” should be revised to “overall presentation and disclosure” and to delete the current words “and practices” from “national standards and practices”.

The Task Force agreed to reconsider some of the wording relating to the proposed description of the audit process, including the proposed use of the term “design and perform” in place of “plan and perform”. In addition, the Task Force agreed to consider changing the words “accounting policies” to “accounting principles” in the proposed illustrative auditor’s report.

The IAASB discussed retention of the phrase indicating that the audit provides a “reasonable basis” for the opinion. The IAASB asked the Task Force to reconsider its decision to retain the current wording, acknowledging the Task Force’s comment that this practice is consistent with the practice of a number of countries.

The Task Force presented a summary of some of the current issues with reporting on unconsolidated financial statements. The IAASB supported the Task Force recommendation that it approach the IASB to open preliminary discussion about a possible joint working group to discuss the need to revise IAS 27, which significantly limits the ability to present parent-only financial statements.

The IAASB agreed with the recommendation of the Task Force to “split” ISA 700 into two separate standards, and that the revised standard on modified reports would be accomplished following a two-phased approach.

The Task Force indicated that it will address the IAASB in May 2003 for purposes of reconfirming its approach in addressing the issues and recommendation of the IAASB. Mr Ashton noted that approval in May 2003 on the main issues is critical to meeting the project timetable.

It was agreed that a first draft of the package of the ED material will be presented at the July 2003 meeting, and a final draft for IAASB consideration of approval for exposure scheduled for the October 2003 meeting.

## **8. Planning and Supervision**

Ms Esdon presented a summary of the proposed approach to revise ISA 300, *Planning*, for purposes of obtaining feedback and guidance from the IAASB.

The IAASB deliberated whether the Standard should be extended to provide, and to delineate, guidance on planning and on supervision. Ms Esdon noted that the Task Force believes that: there is value in having a separate Standard on planning as planning is critical and essential to the audit; that a number of standard setters have a separate section on planning; the proposed change to require the development of a audit strategy and to document this aspect of planning are new principles that need to be considered; and that a revised Standard on planning and supervision is important to link critical elements of planning activities to the requirements of other ISAs.



The Task Force noted its intention not to be duplicative in the guidance to be developed, but to provide a frame of reference to some of the decisions that need to be made in when planning an audit.

The IAASB agreed that:

- A separate Standard on planning is important and the scope should include guidance on supervision. However, a decision on the title (whether it includes supervision) will be made at a later date.
- ISA 300 should be revamped as discussed and issued as a revised ISA.
- The Task Force should endeavor not to draft material that would be duplicative of the material in proposed ISA 220, *Quality Control for Audit Work*, the proposed audit risk Standards and other ISAs.
- The Task Force should consider inclusion of paragraphs addressing planning considerations on initial audits.
- A separate section should be drafted addressing required planning documentation.

The IAASB agreed with the Task Force recommendation that inclusion of matters to be considered in developing the overall audit plan be established as an appendix to the ISA. The Task Force agreed not to emphasize planning as a separate phase but noted that that certain important aspects of planning needs to be completed prior to the commencement of the audit work.

The IAASB suggested that the revised planning standard should take into consideration that audit planning includes an evaluation of information and findings noted from the conduct of reviews of interim financial information or from interim audit work. The IAASB also suggested that the Task Force reconsider the meaning and use of the term “audit program”.

The Task Force noted that consideration will be given to providing guidance on planning for the audit of smaller entities.

The Task Force requested the IAASB to provide to Staff any suggestions or major concerns on the draft outline in the agenda papers, and agreed to present a proposed revised ISA 300 for first read by the IAASB at the July 2003 meeting.

## **9. Fraud**

Ms Esdon noted that the Fraud Task Force has reconsidered its project timetable and that it will aim to present a document for first read by the IAASB at the May 2003 meeting and to present an exposure draft for approval at the July 2003 meeting. Ms Esdon also noted that the Task Force will further develop an approach to reposition guidance that refers to ‘error’ from extant ISA 240 and to incorporate it into other ISAs. The IAASB agreed to the proposed revised timetable as presented.

## **10. Audit Risk Conforming Changes**

Mr Kellas provided an overview of the work accomplished to date on the Audit Risk Conforming Changes project. Mr Kellas noted the previous decision of the IAASB that conforming changes will be posted to the intranet for review and comment by the IAASB, but that the conforming changes will neither be presented to the IAASB for deliberation nor exposed for public comment. Mr Kellas also noted that some ISAs, such as those addressing related parties, going concern and laws and regulations, may benefit from a full revision in the future in order to better align those Standards with the risk-based approach adopted in the proposed audit risk standards. Those

Standards however were not considered to be incompatible with the proposed audit risk standards.

### **11. Update on the AIPCA Project on Reporting on Internal Control**

Mr. Tucker provided an update of the U.S. ASB's project on reporting on internal controls, a project commenced in response to Section 404 of the Sarbanes Oxley Act.

Mr. Tucker provided a summary of the main aspects of the proposed standards. The two main documents are (1) a proposed new auditing standard, addressing the requirement to report on internal control as part of an audit of financial statements, and (2) a proposed revision of the attestation standard dealing with reporting on internal financial controls. The implementation date for the proposed standards is set for years ending on or after 15 September 2003 to coincide with the effective date of the related requirement in the Sarbanes Oxley Act.

The proposed exposure drafts were approved by the U.S. ASB in February 2003 and are available from the AICPA website. The comment period has been set to end 15 May 2003. The intention is to vote on the final standards at the June or July 2003 meeting of the US ASB.

In response to Mr. Tucker's update, a member questioned whether the standards identified what suitable criteria should be used. Mr Tucker noted that the definition of internal control has been taken from COSO, but that the standards do not prescribe a specific suitable criteria to be used, but does refer to COSO as an example. It was indicated that in the case of multi-location audits, different sets of criteria may be used.

Mr Lohnes indicated that the CICA has recently approved a project to develop a Canadian equivalent to the U.S. Standards.

### **12. IAASB Work Program**

The IAASB agreed to hold an additional fifth meeting in 2003 in order to accelerate the timetable for the projects on the auditor's report and the auditor's consideration of fraud and to advance the development of a number of other projects. The next meeting is scheduled to be held in New York on May 11-13.

### **13. Closing**

Mr. Mertin thanked Mr Mifsud, CPA Australia and the Institute of Chartered Accountants in Australia for their hospitality, generous support and gracious efforts in organizing the meeting. Mr Mertin thanked the members, technical advisors and technical staff of the IAASB for their efforts and closed the meeting.