

## **Discussion Paper**

### **2005-2006 IAASB Project Planning Considerations**

#### **Objectives of the Discussion Paper**

1. To assist the IAASB to identify and prioritize new projects to be undertaken in 2005-2006.

#### **Scope of the Discussion Paper**

2. This paper identifies possible project priorities based on preliminary staff assessments and feedback received from IAASB. It focuses on planning matters for technical projects (i.e., development or revision of standards and practice statements) rather than on other activities of the IAASB, such as addressing reforms, issues of convergence, endorsement of ISAs, strategic partnership, and communications. Proposals on these broader strategic activities of the IAASB are outlined in the draft IAASB 2005-2006 Action Plan in Agenda Item 3-B.
3. There are a number of competing priorities affecting the final determination of the projects to be undertaken by the IAASB in 2005-2006. Flexibility in the planning process is needed in order to be able to respond to new events and circumstances as they arise. The purpose of this paper is to help set the direction of IAASB's efforts, and to serve as a basis when further consulting on project priorities with the PIOB, IAASB CAG, national standard setters over the next three-to-six months (as outlined in Agenda Item 3). The decisions on future project priorities in December will not restrict IAASB's future considerations or re-prioritization as circumstances dictate. Further, it is acknowledged that commencement of any project is subject to IAASB approval of a formal project proposal.

#### **Background and Planning Considerations**

##### *IAASB Agenda Capacity*

4. The IAASB meeting schedule has capacity for the commencement of approximately six or seven new projects in 2005-2006. This capacity assumes some, but not much, slippage in the progress of current projects.
5. The Clarity exposure draft and consultation paper approved for issue by the IAASB in September seeks views on whether a "prospective approach" or a "modified prospective approach" is more desirable in terms of applying the proposed drafting conventions. In the event there is strong demand for any approach that entailed redrafting current standards, that would reduce available capacity and the number of new projects that could be undertaken.
6. Capacity would also be affected by the IAASB's need to consider such other activities as are referred to in paragraph 2 above – convergence and the needs of smaller practitioners, in particular.

##### *Factors Affecting the Assessment of Project Priorities*

7. Several factors affect the assessment of the projects to be considered and their priority. These include:

- The objectives of the IAASB and developments in the environment affecting IAASB's initiatives and related actions. In particular, the importance of the continued focus on the maintenance and development of auditing standards relevant to historical financial information, while balancing the need to respond to the growing demand for standards on assurance engagements.
  - The impact of any European Commission adoption process for ISAs (when known).
  - The date of last revision of ISAs by the IAASB and planned or completed revision of equivalent standards by national standard setters.<sup>1</sup>
  - Significant differences between ISAs and some national standards (including those identified in the findings from the FEE survey on ISA + in the EU, "A Summary of Country-Specific Audit Requirements."<sup>1</sup>)
  - Views expressed by stakeholders of the IAASB,<sup>1</sup> including matters raised in previous discussions of the IAASB and IAASB CAG.
8. These factors and others, not separately discussed, but emerging from comments from IAASB members referred to below, raise strategic questions. Should IAASB focus on updating existing standards, or on achieving an appropriate balance between that activity and tackling new issues? In answering that question, IAASB should have regard to concerns emerging from the Wong report about the extent and frequency of changes in international standards, and their effect on translation and implementation. To what extent should IAASB concern itself with conceptual issues, such as a framework? This might produce long term benefit but in the short term might delay the introduction of new or revised standards.

*Preliminary Consultation on Possible Project Priorities with the IAASB*

9. In September, the IAASB Steering Committee considered a preliminary staff assessment of project priorities for 2005-2006. This assessment, revised taking account of the views of the Steering Committee, was circulated electronically in October to the IAASB for comment. IAASB members were asked for their views on the project priorities, and whether there are other projects that have not been identified but which should be considered.
10. In total, 14 members (taking in combination both Steering Committee members and those IAASB members responding to the request for comments) and two technical advisors have provided views on project priorities for 2005-2006 at the time of drafting this agenda paper.

<sup>1</sup> Staff analysis and related correspondence have been previously circulated to the IAASB. Printed copies will be available for reference at the December IAASB meeting.

## Preliminary Findings

### “Consensus” Views

11. While unanimous views were not expressed by IAASB members on any one project priority, nearly all members supported the commencement of the following three projects: (i) revision of ISA 620, *Using the Work of an Expert*; (ii) revision of ISA 402, *Audit Considerations Relating to Entities Using Service Organizations*; and (iii) Reporting on Internal Control. To a lesser extent, support was expressed for a project to revise ISA 505, *External Confirmations*, but there were also strong reservations about the need for such a project. Topic-specific factors influencing the proposed prioritization are outlined below:

1. Using the Work of an Expert (revision of ISA 620)	<ul style="list-style-type: none"> <li>• Complex estimation models, the movement of accounting standards toward fair-value reporting, and IT complexity and related risks inherent in internal controls increasingly require the use of experts both by management and auditors. Concerns have been raised by a number of IAASB task forces about the current ISA regarding the treatment of experts, the coverage of experts employed or contracted by the audit firm, and the treatment of employee auditors with special skills who are subject to supervision under revised ISA 220 on quality control.</li> <li>• The CICA has finalized a revision to its assurance standard on the use of experts, and the US ASB also has undertaken a project to revise its standard for submission to the US Public Company Accounting Oversight Board (PCAOB).</li> <li>• Guidance on the use of experts at the ISA level is critical to the development of subject matter assurance standards and the consideration of experts, particularly on assurance on sustainability and internal control reporting.</li> </ul>
2. Using Service Organizations (revision of ISA 402)	<ul style="list-style-type: none"> <li>• The use of service organizations is becoming increasingly prevalent worldwide, and particularly so in certain industries. Recent reviews of equivalent national standards and guidance by the Canadian, US and UK auditing standards boards have identified a number of areas where expanded guidance may be needed.</li> </ul>
3. Reporting on Internal Control	<ul style="list-style-type: none"> <li>• Beyond the US, other jurisdictions such as Canada and France are advocating separate reporting on internal control by independent auditors. The European Commission (EC) has re-emphasized the need for auditors to report to the audit committee material weaknesses in internal control (although this does not extend the scope of the audit of the financial statements).</li> <li>• FEE has commenced a project to consider the future of reporting on internal control by management and related assurance work by auditors.</li> <li>• At present, there are a number of internal control frameworks espoused by various groups in different jurisdictions. An international perspective on conducting assurance engagements within such frameworks, and on the consideration of the suitability of the criteria for reporting thereon, may serve the public interest and further the consistency in practice internationally.</li> <li>• See discussion below highlighting additional views expressed by IAASB members.</li> </ul>
4. External Confirmations (revision of ISA 505)	<ul style="list-style-type: none"> <li>• Reviews of ISA 505 (or equivalent national standard) by IOSCO, the US Panel on Audit Effectiveness, and the US ASB identified several areas where guidance on the use of external confirmations could be strengthened. Such areas <i>inter alia</i> include: (i) the need to consider the circumstance or procedures for which the use of confirmations is required (and if so, to articulate precisely the considerations that should be present to overcome the presumption that it is necessary to send confirmations); (ii) matters of reliability; (iii) additional</li> </ul>

	<p>guidance on the use of confirmations to agree terms of agreements, including side-agreements; and (iv) issues of control over the process arising from electronic commerce developments.</p> <ul style="list-style-type: none"> <li>• See related discussion below highlighting additional views expressed by IAASB members.</li> </ul>
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12. With respect to a project on Reporting on Internal Control, it was observed that the single greatest challenge currently facing the profession stems from the requirements of the Sarbanes Oxley Act in relation to internal control, and that assurance in relation to internal control over financial reporting is, or is becoming, an issue in many other jurisdictions. It was noted also that if IAASB fails to engage in the global discussions on the role of auditors in relation to internal control now, particularly in the context of a wider range of audits than is covered by the PCAOB, it risks losing an important opportunity to demonstrate its relevance to regulators and stakeholders and its ability to represent the public interest.
13. In terms of proceeding with a project on Reporting on Internal Control, it was noted that the IAASB needs to be clear as to the scope and objectives of such a project, as well as the impact that different corporate governance and internal control frameworks may have on the development of an international standard. It was therefore suggested that the project may need to begin with a discussion paper or consultation paper that could help to define the scope of any subsequent standard-setting project.
14. With respect to the revision of the ISA on external confirmations, several members expressed support for a project based on the factors identified above. However, some members questioned whether the ISA is deficient or outdated since its issue four years ago, and noted that several of the identified issues are already covered in one way or another in the current standard. It was also noted that the existence of a variety of cultural environments around the world may continue to preclude the required use of confirmations by an international standard.
15. In terms of proceeding with a project to revise the ISA on external confirmations, staff suggests that further study be undertaken to explore the extent to which areas of possible improvement warrant revision of the ISA or, as appropriate, the development of a Practice Statement.

#### **Action Requested**

The IAASB is asked to agree that consideration of the above four projects (subject to the parameters described above) should form part of the Board's immediate priorities for 2005-2006.

#### **Reasonable Assurance**

16. The issue of the meaning of "reasonable assurance" has been raised as a matter of concern by a number of parties, including the IAASB CAG on a number of occasions; IOSCO; FEE and the Transition Oversight Staff of the former US Public Oversight Board. Ten of the 38 respondents to the ISA 700 exposure draft raised reasonable assurance-related issues. Refining the definition of "reasonable assurance" remains an unresolved matter that is important to all assurance related services, including the audit of historical financial information. Some national standard setters have identified this as a priority issue and expressed interest in collaborating on a project.
17. It is uncertain whether, and if so how, the IAASB could address the issues surrounding "reasonable assurance" in 2005-2006. Several IAASB members however believe that the IAASB

needs to formulate a strategy for dealing with this issue on a priority basis, possibly as part of a wider project to establish a framework for audit and assurance.

### **Action Requested**

Subject to additional study by staff and the IAASB Steering Committee, the views of IAASB are sought on whether capacity should be reserved within the project schedule of the IAASB in 2005-2006 for purposes of addressing the issue of “reasonable assurance.”

### **Mixed Views**

18. Several members expressed strong support for the commencement of projects on standards or guidance for other assurance services and ISA-related topics. Mixed views, however, were expressed on: (i) the priority to be given to the different possible projects; and (ii) the balance between developing standard for historical financial information and standards for assurance services.

### *Assurance and ISA-related Projects*

19. The projects recommended for consideration as part of IAASB 2005-2006 priorities, and topic-specific factors influencing the proposed prioritization are as follows:

Reporting on Sustainability Reports	<ul style="list-style-type: none"> <li>• Sustainability reporting is becoming more mainstream to investment decisions and demand for assurance thereon has increased, with the prediction that this trend will accelerate over time. Regulators in some countries already require the issue of a sustainability report.</li> <li>• Practice continues to develop, albeit in some instances in an inconsistent manner. There has been concern by some that the current quality of assurance services being reported may be in neither the public's nor the profession's best interests.</li> <li>• FEE has issued a “Call for Action Paper” that includes a call on standard setters to accelerate the development of a sustainability assurance standard.</li> <li>• An IAASB-PAIB Panel of Experts has been set up to become closely involved with GRI's next revision of their Guidelines (due 2006), to concentrate on ensuring their general acceptance as “suitable criteria” on which an assurance report could be issued. The issue of international guidance near the time of issue of the revised GRI guidelines would benefit this developing field.</li> </ul>
Reporting on Prospective Financial Information	<ul style="list-style-type: none"> <li>• A number of national standard setters have indicated their intention of developing guidance on providing assurance over prospective information in response to growing demand from a variety of organizations.</li> <li>• The standard on the examination of prospective financial information (ISAE 3400) is outdated. Given the common association of practitioners with such information, revision of the standards and guidance ought to be a high priority.</li> </ul>
Auditor Involvement with Prospectuses, including Pro-forma Financial Information and Comfort Letters	<ul style="list-style-type: none"> <li>• A new regime for prospectuses will become effective in the EU in July 2005, with an anticipated need for guidance on auditing and reporting considerations by the auditor.</li> <li>• Practices on comfort letters vary between jurisdictions, and there appears to be lack of clarity on what comfort is being expressed and the nature of the assurance being provided. [Note: The IAASB's current project on comfort letters may deal with some of these developments.]</li> </ul>

20. Based on the input received from IAASB members, there appears to be clear demand for one or more of the above topics to form part of IAASB's 2005-2006 project priorities. There was, however, no consensus on which of the possible projects should be given a higher priority relative to the others. There was also concern that some of the underlying issues are highly dependent on local regulation, making international consensus difficult to achieve – see below.

*Balance Between Developing Standards for Historical Financial Information and for Standards for Assurance Services*

21. One member noted that the majority emphasis in 2005-2006 should be to update the remaining ISAs for conformity with the audit risk model. This member cautioned that such work may be jeopardized if IAASB resources are used on assurance projects where there is not sufficient international commonality as to what is required of preparers to provide a platform upon which to develop international standards (as much of the detailed requirements, if any, are determined by national regulations). IAASB needs to be very clear as to what can usefully be provided; it is unhelpful to have generalized international standards on assurance that are unused.
22. Accordingly, it was suggested that revision to ISA 545, *Auditing Fair Value Measurements and Disclosures*, and ISA 250, *Consideration of Laws and Regulations*, to align them with the audit risk model and developments in other ISAs, might need to be considered as part of IAASB's project priorities.

**Action Requested**

The IAASB is asked to consider the above matters and to indicate:

- Whether the combination of the ISA-related (see paragraphs 11 and 17) and other assurance-related projects considered above provide an appropriate balance between developing standards for audits of historical financial information and in responding to the demand for standards on other assurance services.
- Which two (if any) of the three assurance projects identified in paragraph 19 above should form part of the Board's immediate priorities in 2005-2005 and their relative priority.

**Other Possible Projects**

23. Staff's preliminary assessment of project priorities identified several other possible projects for consideration. On balance, members were not of the general view that the identified projects warrant priority attention in 2005-2006. The projects identified were:
- Auditor's Reports – Related Matters, Including Revision of ISA 720, *Other Information in Documents Containing Audited Financial Statements*
  - On-line Business Reporting / XBRL Reporting
  - Audits of the Financial Statements of Banks (revision of IAPS 1006)
  - Auditing Matters in the International Insurance Industry (possible new IAPS)
24. In terms of other possible projects, one IAASB member was of the view that the most important project that the IAASB should undertake is the development of a proper conceptual framework for assurance engagements. The priority (in terms of timing) among other projects was placed

comparatively low, however, because almost all of the time invested would be at the task force level (presumably mostly outside experts and other knowledgeable stakeholders) until towards the final phases of the project.

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