

**Minutes of the 25<sup>th</sup> Meeting of the  
INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD**

**Held on February 13-16, 2007 in New York**

**Voting Members****Technical Advisors**

Present:	John Kellas (Chairman)	Kelly Ånerud (Mr. Larsson)
	Denise Esdon (Deputy Chair)	Philip Ashton (Ms. Hillier)
	Phil Cowperthwaite	Michele Caso (Mr. Tizzano)
	Craig Crawford	Josef Ferlings (Mr. Kinney)
	John Fogarty (February 13-14, 16)	Cédric Gélard (Mr. Trémolière)
	Jan Bo Hansen	Jon Grant (Mr. Rainey)
	Diana Hillier	Jennifer Haskell (Mr. Hansen)
	Susan Jones	Shahid Hussain (Mr. Yusuf) (February 14-16)
	William Kinney	Maria Manasses (Ms. Jones)
	Kjell Larsson	Richard Mifsud (Mr. McPhee)
	Ian McPhee	Greg Shields (Mr. Cowperthwaite)
	Marcel Pheijffer	Sylvia Smith (Mr. Crawford)
	Makoto Shinohara	George Tucker (Ms. Esdon)
	Roberto Tizzano	Hans Verkruijsse (Mr. Pheijffer)
	Gérard Trémolière	Sharon Walker (Mr. Fogarty)
	Abdullah Yusuf	Yuichi Yamamoto (Mr. Shinohara)

Apologies: Will Rainey  
David Swanney

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**Non-Voting Observers**

Present: David Damant  
Jennifer Rand

Apologies: Hisashi Yamaura  
Jean-Philippe Rabine

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**Public Interest Oversight Board (PIOB) Observer**

Present: Fayezul Choudhury (February 13-14)

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**IAASB Technical Staff**

Present: Jim Sylph (Executive Director), James Gunn, Kathleen Kerrigan, Daria Koukhar, Michael Nugent, Alta Prinsloo, Ken Siong

## **1. Opening Remarks and Minutes**

### **WELCOME AND INTRODUCTIONS**

Mr. Kellas welcomed Mr. Fayeul Choudhury as the PIOB observer to the meeting.

Apologies were received from Messrs. Rainey, Swanney, Rabine and Yamaura.

Proxies were noted as follows: Mr. Grant for Mr. Rainey, and Mr. Kellas for Mr. Swanney.

Mr. Kellas introduced new IAASB members appointed from January 1<sup>st</sup>. They are Ms. Susan Jones (technical advisor Ms Maria Manasses), Mr. William Kinney (technical advisor Mr. Josef Ferlings) and Mr. Abdullah Yusuf (technical advisor Mr. Shahid Hussain). He also welcomed Mr. Michele Caso as the new technical advisor for Mr. Tizzano.

### **MINUTES OF PREVIOUS MEETING**

The minutes of the public session of the previous IAASB meeting were approved.

The approved close-off version of ISA 805, which was approved at the December 2006 meeting, was distributed with the minutes of the public session for that meeting.

### **OTHER MATTERS**

#### *Public Interest Declarations*

Mr. Kellas reminded members that they had all submitted their annual public interest declarations and he emphasized that they were expected to act in the public interest and not in the interest of the firms, professional bodies or organizations that nominated them.

#### *National Standard Setters*

Mr. Kellas informed the IAASB that the IAASB-National Standard Setters (NSS) meeting is scheduled for March 29-30, 2007 in New York. Topics to be discussed include: the Clarity project, including the direction being taken for ISA 200; national and convergence-related issues; audit quality; input to IAASB's future strategy and work program; guidance on audit documentation for audits of small and medium sized entities (SMEs) and developments with respect to other implementation guidance; and alternative assurance services.

#### *IAASB Strategy Review*

Mr. Kellas informed the IAASB that the Strategy Review Questionnaire was sent to major stakeholders, with a closing date for comment of February 23, 2007.

A forum will be held on April 13, 2007. The morning session will address the future strategy and work program of the IAASB, and the afternoon session will address alternative services for SMEs. The forum will be attended by preparers, auditors and users. Individuals representing these constituencies have been invited to present at the forum. A few IAASB members have been asked to attend the forum. Other IAASB members are welcome to attend; however, space may be limited.

Another forum is planned for June 28, 2007 in Brussels. This forum will be followed by an IAASB Consultative Advisor Group (CAG) meeting.

*IAASB CAG Review*

Mr. Kellas informed the IAASB that the IAASB CAG is planning a self-review of its activities and working procedures and that a questionnaire to be completed by the IAASB will be distributed during the week following the IAASB meeting.

The next IAASB CAG meeting is scheduled for April 2-3, 2007 in New York.

**2. Related Parties**

Mr. Trémolière summarized the main issues arising from the IAASB's discussion of the previous draft of proposed ISA 550 (Revised and Redrafted), "Related Parties" in December 2006. He then led a review of the revised draft.

**INQUIRIES OF MANAGEMENT AND RELATED PARTY DEFINITION**

The Task Force proposed that, in obtaining an understanding of the nature of the entity as required by ISA 315 (Redrafted), "Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment," the auditor should discuss with management regarding the identity of the parties that control or significantly influence the entity and that the entity controls or significantly influences, as well as the nature of any business undertakings between the entity and these parties. The Task Force also proposed that, where the applicable financial reporting framework establishes related party requirements, the auditor should obtain from management the names of the related parties that management has identified to meet those requirements, and inquire of management regarding the nature of any transactions with these related parties.

Some members noted that the distinction between these two sets of requirements was unclear as they overlapped to some extent. They also noted that the rationale for requiring the auditor to inquire of management in the latter case but to discuss with management in the former was unclear. In addition, it was not apparent why under the first set of requirements the scope of the auditor's discussion with management should be limited to only parties that control or significantly influence the entity and parties that the entity controls or significantly influences, and not include all the parties that meet the proposed definition.

The IAASB concluded that the order of the two sets of requirements should be reversed and that they should both focus on inquiries of management. Thus, where the framework establishes related party requirements, the auditor should inquire of management regarding the identity of the entity's related parties, and the nature of any related party transactions (effectively a completeness test). Where the framework establishes no related party requirements (or does so inadequately), the auditor should inquire of management regarding the parties that would be considered related under the proposed ISA.

The IAASB also agreed to narrow the proposed definition of a related party to include a party that controls or significantly influences the entity as opposed to a party that has the ability to exert such control or significant influence. This would ensure a more focused inquiry into those parties that are actually controlling or significantly influencing the entity where the framework establishes minimal or no related party requirements, as the purpose of the auditor in such a case is not to perform a

completeness test. In addition, the IAASB agreed that the proposed definition of a related party should be clarified to make clear that the framework may add to the definition but not subtract from it. The IAASB agreed that the explanatory memorandum accompanying the re-exposure draft should include a specific question seeking respondents' views on the appropriateness of the proposed definition.

#### OTHER MATTERS

In addition to editorial changes, the IAASB also agreed the following:

- The paragraph in the introductory section describing the auditor's responsibility to obtain reasonable assurance that the financial statements are free from material misstatement should be deleted as it duplicates similar material in proposed revised and redrafted ISA 200, "Overall Objective of the Independent Auditor, and Concepts Relevant to an Audit of Financial Statements."
- The description of the auditor's responsibility in the introductory section to identify, assess and respond to the risks of material misstatement arising from related party relationships and transactions should not be limited to considerations of material misstatements caused by error only, as such misstatements could also be caused by fraud.
- The second and third parts of the objectives pertaining to (a) concluding whether the financial statements achieve fair presentation/are not misleading, and (b) the identification of fraud risk factors, should be clarified to indicate that they apply regardless of whether the applicable financial reporting framework establishes related party requirements. In addition, the second part of the objective should more specifically refer to the need to obtain an understanding of related party relationships and transactions *insofar as the financial statements are affected by those relationships and transactions*.
- The definition of "arm's length transaction" should be clarified to indicate that the buyer and seller are in fact unrelated, consistent with the description of the term in International Financial Reporting Standards.
- The introductory paragraphs that direct the auditor to the requirements to perform specific risk assessment procedures and to design responses to the assessed risks, in the context of the overall requirements of ISA 315 (Redrafted) and ISA 330 (Redrafted), "The Auditor's Responses to Assessed Risks," should be reworded to eliminate the "shall" formulation so as to avoid introducing duplicate requirements.
- The requirement for the auditor to obtain an understanding of the controls that management has established should include a requirement to understand controls to authorize and approve transactions with related parties. In addition, the requirement to understand controls to authorize and approve transactions and arrangements outside the normal course of business should be limited to significant transactions and arrangements.
- In relation to circumstances where the auditor has become aware of significant transactions outside the normal course of business, the Task Force should reconsider the proposed requirement for the auditor to understand the business rationale of such transactions to avoid any inconsistency with, or repetition of, a similar requirement in ISA 240 (Redrafted), "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements."

- The proposed guidance regarding implicit arm's length assertions, and related references to explicit assertions, should be deleted. The explanatory memorandum should ask for respondents' views as to whether the ISA should specifically address the audit of implicit arm's length assertions.
- The requirement to communicate with those charged with governance should be clarified in that the auditor should not repeat the communication if all of those charged with governance are involved in managing the entity and are aware of the matters already communicated to them in their management capacity.
- The Task Force should delete from the list of illustrative circumstances in which it may be appropriate to obtain written representations from those charged with governance circumstances in which they are responsible for the financial statements, as such example is not of direct relevance to related parties.

#### APPROVAL OF RE-EXPOSURE DRAFT

Mr. Trémolière explained that the Task Force had concluded that re-exposure would be necessary as the changes to the exposure draft in response to respondents' comments were significant and substantive. In particular, the proposed revised objectives are now more outcome-based and better reflect the three distinct responsibilities of the auditor with regard to related parties. The requirements have been revised to address respondents' concerns about the open-ended nature of some of the original proposals and the lack of integration with the audit risk and fraud ISAs. And the revised draft now proposes a more principles-based definition of a related party as compared to the original proposal which relied significantly on the detailed definition in International Accounting Standard 24.

The IAASB concurred and approved the proposed ISA 550 (Revised and Redrafted) for issue as a re-exposure draft with a 120-day comment period. Mr. Kellas, as proxy for Mr. Swanney, abstained on his behalf in the absence of further specific instructions.

### **3. Laws and Regulations**

Mr. McPhee presented the proposed ISA 250 (Redrafted), "The Auditor's Responsibilities Relating to Laws And Regulations In an Audit of Financial Statements," noting that redrafting work is being supported by staff of the Australian Auditing and Assurance Standards Board and its Technical Group.

#### OBJECTIVE

The IAASB discussed the wording of the objective proposed by the Task Force and concluded that it should focus on whether the financial statements have been misstated due to non-compliance with laws and regulations, rather than on compliance with laws and regulations that may have a material effect on the financial statements.

#### RELATIONSHIP WITH AUDIT RISK ISAS

In relation to the structure of the redrafted ISA, the IAASB agreed that no major restructuring of the ISA was required, but emphasized the importance of capturing the tone and guidance of the extant

ISA in the redrafted ISA. In particular, the IAASB asked the Task Force to consider whether greater clarity could be introduced in relation to the auditor's responsibilities in respect of laws and regulations that are directly concerned with the applicable financial reporting framework, and in respect of other laws and regulations.

#### DISPOSITION OF PRESENT TENSE

The IAASB reviewed the Task Force's recommendations on the treatment of the present tense items and, with one exception, agreed with the proposed changes. The IAASB did not agree with the Task Force's proposal to elevate to a requirement the auditor's evaluation of the potential effects on the financial statements of possible non-compliance with laws and regulations, as this was a duplication of the existing requirement for the auditor to obtain further information to evaluate the possible effect on the financial statements when coming across a possible instance of non-compliance.

#### OTHER MATTERS

In addition to editorial changes, the IAASB agreed the following:

- The statement that the auditor is entitled to assume the entity is in compliance with laws and regulations in the absence of audit evidence to the contrary should be retained.
- The proposed documentation requirements should be revised to better align with the extant requirements of ISA 250.
- Reference in the Application and Other Explanatory Material to proposed ISA 580 (Revised), "Written Representations," should be clarified to indicate that proposed ISA 580 is currently in exposure.

#### WAY FORWARD

The IAASB asked the Task Force to present a revised draft at the April 2007 meeting for approval as an exposure draft. The primary focus of the discussions at the next meeting will be around the articulation of the auditor's responsibilities in respect of laws and regulations that form part of the applicable financial reporting framework, and in respect of other laws and regulations that may have a material effect on the financial statements.

### **4. Audit Evidence**

Mr. Fogarty presented proposed ISA 500 (Redrafted), "Audit Evidence," noting that since the IAASB last discussed this ISA in October 2005, a significant amount of text regarding the use of assertions had been moved into ISA 315 (Redrafted). He also noted that the objective and scope of this ISA need to be closely synchronized with those of ISA 200. In addition, some material may be moved into ISA 500 as a result of the redrafting of ISA 530, "Audit Sampling and Other Means of Testing." As ISAs 200 and 530 were not scheduled for approval at this meeting, the Task Force was not seeking approval for the issue of the redrafted ISA as an exposure draft.

#### SCOPE AND OBJECTIVE

The objective stated in the draft ISA was "to obtain information that is capable of providing sufficient appropriate audit evidence for the purposes of drawing conclusions." It was noted that introducing the phrase "information that is capable of providing" would add a layer of complexity to existing terminology and unnecessarily raise issues about the difference between information and

evidence. An alternative discussed was “to obtain sufficient appropriate audit evidence,” perhaps with the addition of “to draw conclusions on which to base the audit opinion.” This latter phrase was seen by some members as a helpful indicator that the audit process requires the auditor to draw together a series of conclusions from various parts of the audit. However, it was argued that the objective “to obtain sufficient appropriate audit evidence” is too broad for ISA 500 and, rightly, belongs in proposed revised and redrafted ISA 200. Other suggestions made included:

- Distributing the content of ISA 500 into other ISAs, particularly ISA 200. It was noted that in previous discussions the IAASB had been reluctant to “overload” ISA 200. It was argued then that users of ISAs would reasonably expect to see an ISA on audit evidence, and that even if there are only a few requirements in the final ISA, there is a good amount of useful guidance that it would be appropriate to keep in a separate ISA on audit evidence. The IAASB agreed to keep ISA 500 as a separate ISA.
- Departing from the usual clarity format by having an ISA with no separate objective or with no requirements. The IAASB agreed that it would be appropriate for ISA 500 to follow the usual clarity format.

#### REQUIREMENTS

It was noted that the draft contained a definition of “relevance,” but did not provide much discussion about this aspect of appropriateness. The IAASB agreed that there should be a requirement regarding relevance with appropriate supporting guidance, for example, on the direction of testing.

The IAASB discussed proposed requirements for the auditor to perform procedures in addition to inquiry, and to obtain evidence from sources other than the entity’s accounting records. It was agreed that these matters would be better dealt with in a discussion of the concept of sufficient appropriate audit evidence. It was noted that the current draft of proposed revised and redrafted ISA 200 includes a discussion of this concept, which was largely derived from extant ISA 500. It was agreed the discussion in ISA 200 should be repeated in the introduction of redrafted ISA 500, enhanced by the addition of the aforementioned requirements regarding procedures other than inquiry and sources of evidence other than the accounting records.

#### ISA 501

The IAASB discussed whether the content of ISA 501, “Audit Evidence—Additional Considerations for Specific Items,” should be subsumed in ISA 500. The IAASB agreed that ISA 501 should remain as a separate ISA.

#### OTHER MATTERS

In addition to editorial changes, the IAASB asked the Task Force to consider:

- The treatment of requirements in the current draft regarding the reliability of information used as evidence and, in particular, the accuracy and completeness of information produced by the entity.
- Whether the list of types of information that may be used as evidence (such as minutes of meetings and analysts’ reports) that is currently in the draft application material, is needed.

## WAY FORWARD

The Task Force was asked to present a revised draft for approval at the April IAASB meeting, when proposed revised and redrafted ISA 200 will also be presented. It was noted that proposed redrafted ISA 500 will not likely be released, however, until the July meeting pending any final changes that may be necessary due to finalization of proposed redrafted ISA 530 at that meeting.

## 5. Audit Sampling and Other Means of Testing

Mr. Fogarty introduced the topic and summarized the main issues identified by the Task Force. He then led a review of the proposed redrafted ISA 530.

### SCOPE OF ISA 530

Mr. Fogarty noted that the extant ISA 530 represents a mixture of tests of controls, other means of testing and audit sampling. He indicated that it was the Task Force's view that limiting ISA 530 to audit sampling only would allow for a more coherent and focused ISA. The IAASB agreed that by eliminating requirements and guidance that are unrelated to audit sampling, ISA 530 would be more coherent. With regard to ISA 500, the proposed transfer of the non-sampling material from ISA 530 would add some additional content to the proposed redrafted ISA 500, which was one of the areas of concern raised during the earlier discussion of that ISA at the meeting.

### OBJECTIVE

The IAASB deliberated the wording of the objective of the auditor, and possible alternatives for its form and content. It agreed that reference to obtaining sufficient appropriate audit evidence in the objective is not necessary in this ISA and therefore should be removed. It was also noted that it would be difficult to draft an outcome-based objective for this particular standard. The IAASB asked the Task Force to consider linking the objective to the reliability of audit evidence and the evaluation of the results of audit procedures performed.

### DEFINITIONS

#### *Error*

The IAASB debated whether the term *error* should be replaced with the suggested terms *deviation* or *misstatement*, or both, as appropriate. The Task Force's view was that the definition of error in extant ISA 530 is inconsistent with its use in proposed ISA 450 (Redrafted), "Evaluation of Misstatements Identified during the Audit" and therefore could cause confusion. In order to define the concept and to bring the terminology in line with other ISAs, the Task Force constructed the terms *tolerable rate* and *tolerable misstatement*. Some members were in favor of removing the term *error* and were of the view that the term *tolerable deviation rate*, if introduced, would be clearer than tolerable error. One member noted that the term *error* was confusing as it is intended to encompass both intentional and unintentional errors, and that the term *misstatement* was more comprehensive. Another member expressed concern that the term *tolerable misstatement* may suggest that fraud, being included in the definition of misstatement, can be tolerated.



A member supported using the term *tolerable error* as this term specifically relates to audit sampling, and therefore it would not be confusing for the auditor to think in terms of *error* for the purposes of ISA 530 alone. The IAASB discussed whether the concept of *tolerable rate of occurrence for a population being tested* should be introduced, which could be applied to both tests of controls and substantive tests. The IAASB asked the Task Force to consider this concept further and to provide additional guidance on its application.

#### *Anomalous error*

In view of the discussion above, the IAASB discussed whether the term *anomalous error* should be replaced by *anomaly* consistent with its common use English meaning. The Task Force noted that anomalous error is used in the extant ISA 530. However, it questioned whether, in reality, there is such a thing as an anomalous error. It was noted that there is an element of contradiction embedded in the concept itself, because if the auditor has found an anomaly in the selected sample then the sample would not be representative. Some members noted that translation difficulties could arise if the term *anomaly* were used. Further if anomalies really do exist, they should be rare. Extant ISA 530 does not address the rarity of anomalies.

The IAASB acknowledged that the term “anomalous errors” exists in the literature and that such errors are recognized as being possibilities in audit practice today. Accordingly, it would be inappropriate to delete the term from ISA 530 in the course of redrafting it. The IAASB asked the Task Force to consider emphasizing the rarity of occurrence of anomalies in practice and to retain the concept in the redrafted ISA 530.

#### *Audit sampling*

The IAASB asked the Task Force to consider further the definition of audit sampling in the context of selection and evaluation, rather than in the context of the application of audit procedures.

#### *Non-sampling risk*

The IAASB asked the Task Force to consider extending the list of examples of non-sampling risk and moving the discussion of non-sampling risk to the main body of the standard for clarity.

#### *Tolerable misstatement*

The IAASB generally did not support the definition of *tolerable misstatement* as redrafted based on extant ISA 530 as it did not link very well to the terminology and concepts embedded in proposed ISA 320 (Revised and Redrafted). In particular, it was unclear whether the proposed definition of *tolerable misstatement* referred to planning materiality or overall materiality. The IAASB asked the Task Force to reconsider the definition of tolerable misstatement, concentrating on basic principles.

#### OTHER MATTERS

The IAASB agreed a number of editorial changes to the proposed redrafted ISA 530. It also asked the Task Force to present a revised draft for approval as an exposure draft at the July 2007 meeting.

## 6. External Confirmations

Mr. Crawford summarized the main issues discussed at the September 2006 IAASB meeting and the Task Force's recommended approach to preparing the first draft of the proposed revised ISA 505, "External Confirmations." He noted that the IFAC Small and Medium Practices (SMP) Committee had provided generally favorable feedback on this draft.

### RELATIONSHIP WITH THE AUDIT RISK ISAS

Mr. Crawford noted one particular area of difficulty that the Task Force faced at the outset of the project – how to contextually link the proposed revised ISA 505, which in large part is a procedural ISA, with the audit risk ISAs. The Task Force proposed to include appropriate context in the Introduction section of the ISA to provide a link from the risk assessment process to the procedural requirements and application material in the proposed ISA. The IAASB agreed with this approach.

In relation to the proposed requirement for the auditor to seek external confirmations in the context of the existing audit risk model, it was noted that the proposed ISA did not build sufficiently on the fraud concepts incorporated within ISA 240 (Redrafted). It was argued that the requirements should link more closely to fraud considerations. In this respect, it was noted that internal evidence is often easier to obtain but may be less reliable because it is subject to management override, whereas external confirmations may provide more opportunity of detecting fraud. Obtaining evidence from outside the entity also provides a different perspective than evidence obtained from inside the entity which may assist the auditor in detecting fraud. The IAASB asked the Task Force to consider this further.

### SEEKING EXTERNAL CONFIRMATIONS

The IAASB deliberated the Task Force's approach to drafting the proposed ISA 505 which was intended not to *discourage* the auditor from seeking external confirmations. The Task Force's approach was in recognition of concerns that auditors were over-relying on confirmations that may be unreliable.

It was noted that the draft did not go far enough in encouraging the auditor to seek external confirmations. In particular, some members felt that the proposal that the auditor should seek external confirmations when that is the only means of obtaining evidence in response to an assessed risk could be interpreted to mean that the only time that the auditor seeks external confirmations is when it is the only means of obtaining audit evidence. The IAASB generally agreed that this proposal and the related guidance would appear to undermine the use of external confirmations. It was also noted that the auditor obtains audit evidence from different sources, which all have certain weaknesses, and external confirmations, if balanced in a right way, can serve as a complementary source of obtaining audit evidence. Accordingly, the IAASB asked the Task Force to reconsider the tone of the draft to encourage the use of confirmations.

In discussing the proposed requirements regarding the seeking of external confirmations, the IAASB acknowledged that it may be difficult to articulate requirements when there are few clear cut rules for using external confirmations. It was suggested that the ISA could articulate the concept of a spectrum within which there will be circumstances when external confirmations will be effective and when they may prove unreliable. Another approach suggested was to describe what the auditor does when the auditor decides that it is appropriate to use external confirmations, i.e. having regard to what the

auditor must do effectively and the need to control the entire process at all times. The IAASB asked the Task Force to give these matters further consideration.

#### NEGATIVE CONFIRMATION

The Task Force proposed not to prohibit the use of any kind of audit technique in the ISAs, including the use of negative confirmation. However, it proposed to place restrictions on their use and to highlight their limitations. Concern was raised that this type of confirmation represents a weak form of audit evidence, even though it is still used in some jurisdictions. The IAASB agreed with the Task Force's approach but asked the Task Force to reduce the emphasis given to this type of confirmation by not defining what a negative confirmation is, and by addressing the related guidance in a separate section at the end of the document.

#### OTHER MATTERS

In addition to editorial changes, the IAASB agreed the following:

- The objective should refer to external confirmation as a means of obtaining 'audit evidence' as opposed to 'sufficient audit evidence'. In addition, the Task Force should reconsider whether the objective should involve a consideration of requesting external confirmations in response to assessed risks, as this may imply that the auditor would seek external confirmations for every type of assessed risk.
- The Task Force should consider whether the guidance describing the factors the auditor would consider when selecting audit procedures to address the assessed risks of material misstatement would be more appropriate in the proposed redrafted ISA 500.
- The Task Force should consider defining the term 'confirming party'.
- The term 'external confirmation' should be used consistently, as there are currently three different uses of the term: the definition in the Glossary, in the proposed revised ISA 505, and in proposed redrafted ISA 500.
- The definition of 'exception' should be aligned with the way it is described in the Application and Other Explanatory Material section of the ISA.
- The Task Force should consider whether the terms 'response' and 'reply' are used consistently to facilitate translation and understanding.
- The ISA should make clear that an external confirmation is generally in written form and there may be circumstances when an oral confirmation may be acceptable.
- The Task Force should identify the key drivers of an effective confirmation process.
- The Task Force should clarify that legal letters are outside the scope of the ISA.
- The Task Force should reconsider whether the Appendix on "Assertions Addressed by Accounts Receivable and Bank Confirmations," is needed given other suggested changes to the draft.

#### WAY FORWARD

The IAASB asked the Task Force to consider its comments and to present a revised draft for approval for exposure at the July 2007 meeting.

## **7. Going Concern**

Ms. Esdon introduced proposed ISA 570 (Redrafted), “Going Concern,” noting that the Task Force had carefully challenged each present tense sentence in the extant ISA. She indicated that the Task Force was recommending that a number of conditional present tense sentences be elevated to requirements in the draft because, even though the stated conditions may not exist in virtually all cases, when they do exist, the requirements are virtually always applicable. She also noted that a response from the IFAC SMP Committee had recently been received, and outlined matters noted in the covering memorandum relating to the placement of text regarding limitations or clarifications of the auditor’s responsibility, and conforming amendments.

### **OBJECTIVE**

The IAASB discussed the objective as stated in the draft. It was agreed that the objective would be more clearly stated if it (a) referred to the auditor “concluding” with respect to material uncertainties, (rather than “obtaining sufficient appropriate audit evidence”), and (b) included consideration of implications for the auditor’s report when a material uncertainty exists.

### **DISPOSITION OF PRESENT TENSE**

The IAASB discussed whether the following present tense sentences in the extant ISA should be elevated to a requirement: “In evaluating management’s assessment, the auditor considers the process management followed to make its assessment, the assumptions on which the assessment is based and management’s plans for future action. The auditor considers whether the assessment has taken into account all relevant information of which the auditor is aware as a result of the audit procedures.” It was agreed that, apart from considering whether management has taken into account all relevant information of which the auditor is aware as a result of the audit, such procedures are not necessary in the majority of cases where the entity is profitable and there is no sign of going concern issues. It was agreed, therefore, to move the guidance contained in the first sentence of this paragraph to the application material rather than to elevate it to a requirement.

### **OTHER MATTERS**

In addition to editorial and other minor changes, including some restructuring of requirement paragraphs, the IAASB agreed:

- The intent of the sentence added by the Task Force stating that there may be some circumstances where special purpose financial statements are prepared in accordance with a financial reporting framework for which the going concern basis is not relevant (e.g., some financial statements prepared on a tax basis in particular jurisdictions). This sentence had been added for consistency with changes made to ISA 700, “The Independent Auditor’s Report on General Purpose Financial Statements” since ISA 570 was last revised.
- The ISA is being redrafted to adopt the clarity conventions and not revised, and as such it was not appropriate to amend a major aspect of the ISA such as the twelve month timeframe because that would change the intent of the extant ISA.

- The IAASB reached the same conclusion regarding a small number of other issues raised by members and the IFAC SMP Committee, as they would result in a change of the content of the extant ISA, when the intent of this project was to redraft the ISA in accordance with Clarity redrafting conventions.
- That business risks are covered by the term that has been retained, i.e., “events or conditions,” and need not therefore be included separately.
- Describing the management’s assessment of the entity’s ability to continue as a going concern as “preliminary” at certain places in the draft was discussed, and it was agreed that this may be confusing. The word “preliminary” was therefore deleted.
- Because the application material regarding inappropriate application of the going concern basis contains some guidance regarding an alternative basis, the IAASB agreed to delete the sentence in the Introduction section that mentions that the ISA does not deal with the auditor’s consideration of financial statements prepared on a basis other than a going concern basis, such as a liquidation basis. The IAASB also agreed that it is unnecessary to include the adjective “authoritative” in reference to alternative bases in the application material.

#### APPROVAL

The IAASB approved the proposed ISA 570 (Redrafted) for exposure. Mr. Kellas, as proxy for Mr. Swanney, abstained on his behalf in the absence of further specific instructions.

### **8. The Independent Auditor’s Report**

Ms. Hiller presented proposed ISA 700 (Redrafted). She noted that comments were received from the IFAC SMP Committee and the Financial Audit Guidelines Subcommittee of INTOSAI.

The IAASB supported the Task Force’s view that the construct “the auditor’s report shall ...” is more appropriate than the construct “the auditor shall ...”

#### INTERRELATIONSHIP BETWEEN REPORTING ISAS

An IAASB member suggested that the proposed redrafted ISAs 700, 705, “Modifications to the Opinion in the Independent Auditor’s Report” and 706, “Emphasis of Matter Paragraph(s) and Other Matter(s) Paragraph(s) in the Independent Auditor’s Report” be combined.

One view was that, because ISAs 705 and 706 also apply to auditors’ reports issued under proposed ISA 800, “Special Considerations—Audits of Special Purpose Financial Statements and Specific Elements, Accounts or Items of a Financial Statement,” they should not be combined with ISA 700, which deals with auditors’ reports on general purpose financial statements. An alternative view was that, as proposed ISA 800 includes the requirements and guidance of ISA 700 by reference, it should not be a problem to include ISAs 705 and 706 in ISA 700. However, some members were concerned about the effect that the suggested combination might have on jurisdictions that have adopted the ISAs in the structure that exists today.

It was agreed that the proposed redrafted ISAs should not be combined as suggested, and that the clarification of their interrelationship in the Introduction section of proposed ISA 700 (Redrafted) was sufficient.

## EFFECTIVE DATE

The Task Force proposed an effective date of December 15, 2009. Reporting standards have historically become effective at a point in time (rather than being linked to when an engagement begins). The proposed date would allow for implementation of the revised and redrafted performance standards before auditors' reports prepared in accordance with ISA 700 (Redrafted) were issued. Mr. Kellas noted, however, that ISA 700 is effective and that auditors' reports should already be in the form prescribed by ISA 700. Applying the clarity drafting conventions to ISA 700 does not affect the form of the auditor's report. As a result, it is not necessary to have a later effective date for the redrafted ISA, nor is it necessary to use different wording for the effective date than that used in the other redrafted ISAs (i.e., "This ISA is effective for audits of financial statements for periods beginning on or after ..."). It was agreed to use the same wording and date for ISA 700 (Redrafted) as for the other redrafted ISAs (provisionally December 15, 2008).

## OBJECTIVE

The IAASB debated meaning of the words "a written report that explains the basis of the opinion" in the second objective. The phrase "to express the auditor's opinion and the basis for that opinion" was considered as an alternative. There was concern that the alternative wording might suggest a tailored explanation of the basis for the auditor's opinion in the specific circumstances of the engagement, which is not what is intended. The auditor's report includes standard wording that explains what an audit involves, as well as the following sentence: "We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion." Therefore, it was agreed that the proposed redrafted ISA should retain the wording of the objective as proposed by the Task Force.

## REQUIREMENTS VS. APPLICATION MATERIAL

Ms. Hillier explained that the Task Force had debated whether to move some of the text in the Forming an Opinion on the Financial Statements section to the application material. However, the Task Force concluded that the requirements were less understandable without the subparagraphs. Although there were mixed views among IAASB members, the majority of IAASB members were of the view that the text should be retained in the Requirements. However, it was agreed that the Task Force should consider:

- The interrelationship between the text in this section and proposed ISA 450 (Redrafted);
- Possible overlap between the first two paragraphs of this section (paragraphs 8 and 9) with regard to proposed ISA 450 (Redrafted); and
- Whether to refine the list of matters to be included in the auditor's evaluation whether the financial statements are prepared and presented in accordance with the specific requirements of the applicable financial reporting framework (paragraph 9).

## MISLEADING TEST

The ISAs do not include a requirement for the auditor to evaluate whether financial statements prepared and presented in accordance with a compliance framework are not misleading; while proposed ISA 700 (Redrafted) requires the auditor, when forming an opinion on financial statements prepared and presented in accordance with a fair presentation framework, to evaluate and conclude

whether those financial statements achieve fair presentation. It was agreed that a requirement should be drafted for consideration at the July 2007 IAASB meeting. It was also agreed that there should be greater alignment of the auditor's actions when the financial statements do not achieve fair presentation (paragraph 13) and when the financial statements are misleading (paragraph 14).

#### OTHER MATTER(S) PARAGRAPHS

At present, Other Matter(s) paragraphs are discussed in both ISAs 700 and 706. The ISA 700 and ISA 705/6 Task Forces discussed whether Other Matter(s) should be addressed in only one ISA or in both ISAs and, if in both ISAs, whether the split in the types / examples of other matters in each ISA made sense. The Task Forces concluded that both ISAs should include discussion of Other Matter(s) paragraphs. The majority of IAASB members agreed with the Task Forces' proposal. It was agreed that proposed ISA 700 (Redrafted) should be amended to require subheadings and to indicate that an Other Matter(s) paragraph should be appropriately headed. The heading should describe the content of the paragraph.

#### OTHER REPORTING RESPONSIBILITIES

Ms. Hillier explained the matter raised by the IDW with regard to Other Reporting Responsibilities. ISA 700 is not entirely clear in relation to whether there can be multiple opinions on the financial statements in part 1 of the auditor's report, and whether there can be opinions related to the financial statements in part 2 of the auditor's report. The IAASB concluded that proposed ISA 700 (Redrafted) should be flexible in this regard and that the existing text provides for such flexibility. The majority of IAASB members agreed not to change the existing text relating to Other Reporting Responsibilities.

#### OTHER MATTERS

In addition to editorial changes, the IAASB agreed that:

- The Auditor's Opinion section in the Requirements should include, as essential explanatory guidance, that the phrases "give a true and fair view" and "present fairly, in all material respects," are equivalent for purposes of the ISAs.
- The requirement in the Auditor's Report for Audits Conducted in Accordance with Both International Standards on Auditing and Auditing Standards of a Specific Jurisdiction or Country section in the requirements should be expanded to deal with conflict between the ISAs and national law or regulations. As drafted, it only deals with conflict between the ISAs and national standards.
- The Supplementary Information Presented with the Financial Statements section should be reconsidered as some members were of the view that the proposed wording of the requirements did not faithfully represent the principles in ISA 700.

#### WAY FORWARD

The IAASB asked the Task Force to consider its comments and to present a revised draft for approval for exposure at the July 2007 meeting.

## 9. Modifications

Mr. Hansen introduced the topic, noting that there had been relatively few changes in the redrafted ISAs 705 and 706 from their closed-off versions, mainly because the Task Force had drafted the wording in the closed-off versions with the clarity drafting conventions in mind.

### *Proposed Redrafted ISA 705*

#### PRESENT TENSE AND USE OF “WOULD”

The IAASB debated whether it is appropriate to use either the present tense or the “would” formulation when reiterating a requirement, such as in “... when there is a scope limitation, the auditor qualifies the opinion/would qualify the opinion.” The IAASB concluded that where such a statement reiterates a requirement that is set out elsewhere in that particular ISA, it should refer to the specific paragraph that establishes the requirement, for example, “Paragraph xx of this ISA requires the auditor to ....” Likewise, if the requirement is contained in another ISA, the statement should refer to that ISA, for example, “ISA XXX requires the auditor to ....”

#### OTHER MATTERS

In addition to editorial changes, the IAASB agreed that:

- The introductory section should be made consistent with that of the proposed redrafted ISA 706.
- The effective date paragraph should be conformed to the wording agreed for the proposed redrafted ISA 700 discussed during this meeting.
- The objective should include reference to the auditor expressing appropriately the modified opinion.
- In relation to the section dealing with the consequence of an inability to obtain sufficient appropriate audit evidence because of a management-imposed scope limitation, the Task Force should consider reversing the steps required so that the auditor should first determine whether it is possible to perform alternative procedures, and if not, then to request management to remove the limitation.
- The requirement to include a description of the financial effects of a material misstatement in the basis for modification paragraph should be clarified so that this description includes a quantification of the financial effects.
- The Task Force should consider whether a definition of pervasiveness could be established based on the guidance on pervasiveness in the application material.
- The Task Force should reconsider the illustrative examples to confirm whether references to “disagreement with management” should be replaced with “material misstatement of the financial statements.”

### *Proposed Redrafted ISA 706*

#### OBJECTIVE

The IAASB noted that the proposed objective was not supported by the requirements and, accordingly, instructed the Task Force to make it consistent with the requirements. The IAASB also



asked the Task Force to consider whether the objective should indicate that the emphasis of matter paragraph should highlight clearly the matter being emphasized.

It was noted that in the UK, some investors had called for auditors to state in their audit reports that they have nothing that they wish to emphasize. It was therefore questioned whether, in order to alleviate those investors' concerns, there should be a requirement for the auditor to include an emphasis of matter paragraph in the auditor's report in circumstances where the matter is of fundamental importance to users' understanding of the financial statements. Some members pointed out that the IAASB had debated at length the issue of whether to require the inclusion of emphases of matter paragraphs in audit reports in specific circumstances, and concluded that this could not be mandated because of the subjectivity involved and the need to allow auditors to exercise appropriate professional judgment. The IAASB reaffirmed its decision that no new requirement was needed.

#### OTHER MATTER

In addition to editorial changes, the IAASB agreed that:

- In relation to circumstances where the auditor considers it necessary to communicate matters other than those that are presented and disclosed in the financial statements, the Task Force should delete the precondition "where this is not prohibited by law or regulation" because the requirement would in any event not apply if it were prohibited by law or regulation.

#### WAY FORWARD

The IAASB asked the Task Force to present revised drafts of the redrafted ISAs 705 and 706 for approval for issue as exposure drafts at the July 2007 meeting, when other reporting ISAs that have been redrafted will also be considered for approval as exposure drafts.

### 10. Special Reports – ISA 800

Ms. Smith presented proposed ISA 800 (Revised and Redrafted), "Special Considerations—Audits of Special Purpose Financial Statements and Specific Elements, Accounts or Items of a Financial Statement."

#### OBJECTIVE

The Task Force proposed the following revised objective at the meeting: "The objective of the auditor is to apply the other ISAs by (a) addressing the special considerations that are relevant to the appropriate acceptance, and planning and performance of, and reporting on the audit of special purpose financial statements or an element, account or item of a financial statement, and (b) in the case of an audit of an element, account or item of a financial statement, adapting the other ISAs as necessary in the circumstances." It was agreed that the Task Force should consider whether (b) is necessary, as proposed ISA 200 (Revised and Redrafted) deals with the adaptation of the ISAs.

#### OTHER MATTERS

In addition to the above and editorial comments, the IAASB agreed that:

- The Scope of this ISA section should include a reference to proposed redrafted ISAs 705 and 706; similar to the reference in proposed redrafted ISA 700.

- The Task Force should consider whether to clarify that financial statements prepared for a special purpose in accordance with a general purpose financial reporting framework are deemed to be special purpose financial statements and, therefore, fall within the scope of proposed ISA 800 (Revised and Redrafted).
- The proposed effective date should be December 15, 2008.
- The reference to ISA 210, “Terms of Audit Engagements” in the Considerations when Determining the Acceptability of the Applicable Financial Reporting Framework section in the Requirements should be moved to the application and other explanatory material section of the ISA (paragraph 9).
- Paragraphs 11 and 16, which deal with the application of the requirements of proposed ISA 200 (Revised and Redrafted) in audits of special purpose financial statements and specific elements, accounts or items of a financial statement, special considerations in such audits, and the adaptation of the ISAs in audits of specific elements, accounts or items of a financial statement, should be aligned with the proposed new wording of the objective. Consideration should be given to moving some (or all) of the revised text to the application material.
- Paragraph 18, which requires the auditor to discuss with management whether another type of engagement may be more practicable when the auditor has concluded that an audit of a specific element, account or item of a financial statement may not be practicable, should be moved to the application material. It represents client service, or helpful advice to an auditor.
- The use of the word “important” in the application material (paragraphs A16 and A19) should be reconsidered as it may imply a requirement.

#### WAY FORWARD

The IAASB asked the Task Force to consider its comments and to present a revised draft for approval for exposure at the July 2007 meeting.

### 11. Special Reports – ISA 805

Ms. Smith presented proposed ISA 805 (Revised and Redrafted), “Engagements to Report on Summary Financial Statements.”

#### SUMMARY FINANCIAL STATEMENTS IN DOCUMENTS RELATING TO SECURITIES OFFERED TO THE PUBLIC

Ms. Smith indicated that, as directed by the IAASB when the close off document was approved in December 2006, the Task Force considered the appropriateness of excluding from the scope of the ISA auditors’ reports on summary financial statements in documents relating to securities offered to the public. As the proposed ISA was not developed with offering documents in mind, there was some concern that the consequences of including such reports in the scope of the ISA might not have been well understood. The requirement that the auditor’s report on summary financial statements should be included in a document that refers to the fact that the auditor has reported on those summary financial statements was causing a problem in a particular jurisdiction.

Ms. Smith summarized the matters considered by the Task Force, including proposed alternatives to avoid excluding offering documents from the scope of the ISA completely. After debate, it was

recognized that the circumstances causing the concern may need to be further clarified. Accordingly, Mr. Kellas asked the Task Force to reconsider whether it is necessary to refer in the ISA to documents relating to securities offered to the public.

#### OTHER MATTERS

In addition to editorial changes, the IAASB agreed that:

- The proposed effective date should be December 15, 2008.
- The explanatory memorandum accompanying the proposed redrafted ISA should ask respondents to comment on the objective.
- The Task Force should reconsider paragraph 9(b). It deals with engagement acceptance criteria, but requires the auditor to determine whether the financial statements *are made available* to the intended users of the summary financial statements without undue difficulty. At the engagement acceptance stage, it is unlikely that the summary financial statements will have already been prepared.
- The Task Force should reconsider paragraph 13, which deals with the timing of work and subsequent events. The reference to “in these circumstances” is not clear. It may also be appropriate to move some of the text to the application material.
- Paragraph 16, which deals with the addressee of the auditor’s report, should be moved to the application material and aligned with similar text in proposed ISA 700 (Redrafted).
- Paragraphs 17 and 18, which deal with auditor’s reports required by law or regulation, should be aligned with ISA 210 and ISA 700 (Redrafted).
- The requirements in the Auditor Association section of the proposed ISA (paragraphs 28 and 29) should be amended to clarify that they apply when the auditor *becomes aware* of the matters addressed in these paragraphs.

#### WAY FORWARD

The IAASB asked the Task Force to consider its comments and to present a revised draft for approval for exposure at the July 2007 meeting.

#### **12. Next Meeting**

The next meeting of the IAASB has been scheduled for April 16-20, 2007 in Sydney.

#### **13. Closing Remarks**

Mr. Kellas thanked the American Institute of Certified Public Accountants for hosting the meeting, and its staff for the assistance with the meeting arrangements.

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