

International Auditing Practice Statements (IAPSs) Review of Status and Authority—Issues and IAASB Working Group Proposals

I. Matters to Be Discussed by the IAASB

1. While the IAASB will not be asked to approve the exposure draft (ED) of proposed revised IAPS 1012,¹ the Working Group nevertheless believes it is necessary that the IAASB agree on the proposed status and authority to attach to IAPSs at the June 2010 meeting and approve an ED on the various proposals in this paper. For this purpose, the Appendix to this paper includes a draft Explanatory Memorandum (EM) and ED to illustrate how the matters to be consulted on are proposed to be presented. Matters on which the IAASB has not yet concluded are shown in brackets.

Revised Proposal to Clarify the Status and Authority of the IAPSs

2. Reflecting upon the comments made during the May 2010 IAASB meeting, and preliminary feedback received from the IAASB-National Standard Setters (NSS) Liaison group, the Working Group has revised the wording to describe the status and authority of the IAPSs as follows:

International Auditing Practice Statements (IAPSs) are issued to provide practical assistance to auditors and to promote good practice. IAPSs do not impose additional requirements on auditors beyond those included in the ISAs, nor do they change the auditor's responsibility to comply with the requirements of all ISAs relevant to the audit. However, auditors should determine whether any IAPS is relevant to the circumstances of the audit and, if so, obtain an understanding of its content.

Depending on the nature of the topic(s) covered, an IAPS may assist the auditor in:

- (a) Obtaining an understanding of the circumstances of the entity, and in making judgments about the identification and assessment of risks of material misstatement;
- (b) Making judgments about how to respond to assessed risks, including judgments about procedures that may be appropriate in the circumstances; or
- (c) Addressing reporting considerations, including forming an opinion on the financial statements and communicating with those charged with governance.

Although none has been issued to date, the IAASB may also issue International Review Engagement Practice Statements (IREPSs), International Assurance Engagement Practice Statements (IAEPSs), and International Related Services Practice Statements (IRSPSs) to serve the same purpose for ISREs, ISAEs, and ISRSs respectively.

¹ See **Agenda Item 3**, Proposed IAPS 1012 (Revised), *Auditing Complex Financial Instruments*

3. The following provides an analysis of the changes to the wording and the Working Group's rationale for doing so:
- International Auditing Practice Statements (IAPSs) are issued to provide practical assistance to auditors and to promote good practice. – Modified from the extant *Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services* (the Preface) to remove the references to the IAPS providing interpretive guidance to be used in implementing the ISAs.
 - IAPSs do not impose additional requirements on auditors beyond those included in the ISAs, nor do they change the auditor's responsibility to comply with the requirements of all ISAs relevant to the audit. – Necessary to explain the relationship between the ISAs and IAPSs and clarify the intent of the IAPSs. The Working Group believes that it is also useful to retain the concept from the extant Preface that, regardless of the material contained in an IAPS, the auditor remains responsible for complying with the requirements of all ISAs relevant to the audit in order to claim compliance with ISAs.
 - However, auditors should determine whether any IAPS is relevant to the circumstances of the audit and, if so, obtain an understanding of its content. – While a few IAASB members seem to object to wording explicitly imposing a requirement on the auditor, Staff notes that current (the Preface) states: "Professional accountants should be aware of and consider Practice Statements applicable to the engagement ..." Accordingly, the wording above is not inconsistent with the obligation on the auditor regarding use of the IAPSs as currently intended in the Preface. Further, the IAASB's Terms of Reference include Practice Statements as "international pronouncements" of the IAASB, which are required to be developed following full due process. In the Working Group's view, developing an IAPS following due process and then not attaching an obligation to it is inherently inconsistent. Absent wording describing an obligation, an IAPS would need to be positioned as no more than a non-authoritative Staff publication, which may undermine its usefulness.
 - Depending on the nature of the topic(s) covered, an IAPS may: ... – Developed in response to suggestions from the UK Auditing Practices Board to clarify why the auditor should understand relevant IAPSs. The Working Group has included additional examples of what type of guidance IAPSs may offer, in response to one IAASB member's concern that discussing only the auditor's risk assessment may unnecessarily limit the IAASB in developing future IAPSs.
 - Although none has been issued to date, the IAASB may also issue International Review Engagement Practice Statements (IREPSs), International Assurance Engagement Practice Statements (IAEPSs), and International Related Services Practice Statements (IRSPSs) to serve the same purpose for ISREs, ISAEs, and IRSRs respectively. – Because the extant Preface allows for the future issuance of Practice Statements relating to the IAASB's other standards, the Working

Group is of the view that similar wording should be retained, but also wishes to clarify that there are currently no such pronouncements.²

4. The Working Group is of the view that the revised wording establishes an authority consistent with the Board's intent in issuing guidance like proposed IAPS 1012 while explaining the purpose and limitations of IAPSs, appropriately distinguishing them from the ISAs. In addition, given the IAASB's support for developing a hierarchy describing its standards and guidance (as discussed further in paragraph 5), including descriptions of the various types of standards and guidance that may be issued by the IAASB in one place will enhance auditors' understanding of how the material is to be viewed and promote awareness of it.

Matters for IAASB Consideration

1. Does the IAASB agree with the revised proposal on the status and authority of the IAPSs? If the IAASB does not agree, what further changes could be made in response to the IAASB's discussions to date?
2. Does the IAASB agree that the wording describing the possibility of Practice Statements for other standards should be retained? If so, is the manner in which this is done clear?

Placement of the Wording Describing the Auditor's Obligations

5. At its May 2010 meeting, the IAASB expressed general support for continuing to describe the auditor's obligations relating to IAPS in the Preface, and to develop a hierarchy explaining the relationship of the ISAs, IAPSs and Staff Publications.
6. The Working Group is of the view that it is important for respondents to the ED to understand the other options that may be available and the reasons why the IAASB has chosen to retain the status quo relating to the placement. According, the IAASB's deliberations are summarized in the draft EM in the Appendix.
7. The Working Group was also asked to explore whether a separate Preface to the IAPSs should be established, to further differentiate IAPSs from the ISAs. It was suggested that this Preface could discuss the authority of the IAPSs and the auditor's obligations relating to them, and explain the due process and criteria applied in their development. However, some IAASB members did not support doing so, noting that is important to link the ISAs with the IAPSs. The Working Group also concluded that developing a separate Preface for IAPSs would not effectively achieve the goal of raising awareness and promoting use of the IAPSs.
8. However, to more fully explain the contrast between IAPSs and ISAs, the Working Group has modified the proposed draft hierarchy that was presented to the IAASB at its March 2010 meeting. The revised proposal has been incorporated into the

² Should the IAASB agree to develop new pronouncements of this type in the future, it may be necessary to incorporate additional wording in the Preface relating to the specific roles of IREPSs, IAEPSs, and IRSPSs.

proposed amended Preface as shown in the Appendix to this paper.

9. Consistent with previous discussions, the Working Group also recommends an IAASB Policy Position be developed after approval of the amendments to the Preface as means to build sufficient awareness of the existence of, and obligations attaching to, the IAPSs.

Matters for IAASB Consideration

3. Does the IAASB agree with the proposed hierarchy as described in the Appendix?
4. Does the IAASB support the subsequent development of an IAASB Policy Position to communicate about the hierarchy when finalized?

Criteria for the Development of the IAPS

10. While the IAASB discussions favor the development of criteria, it was noted that the criteria as discussed at the May 2010 meeting may be equally applicable to the IAASB's determination whether to develop a new ISA.
11. The *Due Process and Working Procedures* requires a proposal to start a new project to be prepared based on research and on appropriate consultation within the IAASB, with consideration given to the costs and benefits of the anticipated output of the proposed project. Further, before approval, the IAASB considers and prioritizes the project proposal having regard to the public interest. A project proposal identifies, where applicable, who has recommended the project for consideration by the IAASB. Project proposals identify the objectives of the project and explain how achievement of those objectives would serve the public interest.
12. The Working Group is of the view that, in determining whether to undertake a project to develop guidance on a particular topic, a more structured consideration of the appropriate form of output in the circumstances could be undertaken through the application of criteria. For example, the decision to pursue an IAPS would be made only if that course of action is appropriate in the circumstances, and only after evaluating the merits of proposing new or modified requirements or application material in an ISA, or the development of a Staff publication.³
13. Accordingly, the Working Group proposes that new IAPSs should only be developed if they meet the following criteria (as amended for the May 2010 discussion):
 - There is divergent practice internationally or a need to raise awareness of issues being encountered in practice in particular areas, and therefore promulgating an

³ Staff publications are used to help raise practitioners' awareness in a timely manner of significant new or emerging issues or other noteworthy circumstances relevant to engagements addressed by IAASB pronouncements, to direct their attention to relevant provisions of IAASB pronouncements, or to provide clarification to emerging questions by referring to existing requirements and application material and background information such as that contained in staff Basis for Conclusions documents. The development of a new Staff Publication does not require approval of a formal project proposal; however, the IAASB has established parameters around their development.

IAPS would promote high-quality auditing practice, contributing to improved financial reporting;

- Such guidance would provide practical assistance to auditors in particular circumstances or industries, and would be applicable without significant modification for national circumstances;
 - Research and discussions with stakeholders who may have recommended the project for consideration by the IAASB have indicated that:
 - o Background and educational material is needed or the issue extends across a number of ISAs but does not necessitate the development of new requirements, and therefore promulgating an IAPS will be effective in promoting good practice; and
 - o There is not likely to be a need for new or modified requirements or application material in the ISAs, as in such circumstances it would be more appropriate to develop or revise an ISA rather than develop an IAPS; and
 - The need for guidance is widely acknowledged by stakeholders and the guidance would be expected to remain useful for the foreseeable future. In this regard, the IAASB should seek to become aware of whether any NSS have developed, or intend to develop, guidance on the topic under consideration to assist the IAASB in determining whether it is appropriate to develop international guidance on the topic.
14. As noted above, certain of these criteria can also be usefully applied in decisions on whether to develop new, or revise existing, ISAs. In approving the project proposal, the IAASB would need to concur with Staff's preliminary position or agree to revise the project proposal. However, over the course of the project, the IAASB could reassess the anticipated output of the project, if considered necessary. Finally, the EM of the ED for a new IAPS should explain how it determined an IAPS was necessary in undertaking the project.

Matters for IAASB Consideration

5. Does the IAASB agree with the changes to the proposed criteria and the manner in which the Working Group proposes such criteria should be used?

Other Matters

Documentation Requirement for IAPSs

15. At its May 2010 meeting, the IAASB asked the Working Group to give further consideration to whether the proposed obligation as described would impose a documentation requirement on the auditor. The Working Group does not believe it is appropriate to infer from reading the proposed revised Preface that a documentation requirement exists, in part because merely documenting that the auditor has determined a particular IAPS is relevant and has obtained an understanding of it is not meaningful.

16. In addition, ISA 230⁴ makes clear that it is unnecessary for the auditor to document separately compliance with matters for which compliance is demonstrated by documents included within the audit file. To analogize to the ISAs, while paragraph 19 of ISA 200⁵ requires the auditor to have an understanding of the entire text of an ISA, including its application and other explanatory material, to understand its objectives and to apply its requirements properly, the auditor is not required to document a statement asserting compliance with this particular requirement. Because the existence of IAPSs does not change the auditor's responsibility to comply with the requirements of all ISAs relevant to the audit, the Working Group believes that the audit file itself may provide evidence of the extent to which the auditor was aware of and incorporated relevant materials in the IAPS into the audit; however, the overall soundness of the audit relates to how the auditor has complied with the ISAs themselves, including the relevant documentation requirements therein.

Impact Analysis

17. As noted in the March 2010 agenda material, this project was initially selected as a pilot test for the impact analysis framework that IFAC is currently developing. However, given the nature of the project, the Working Group is of the view that the proposed template to be used for such an analysis would not necessarily provide meaningful information to readers because it is geared towards new or revised standards. The Working Group is also of the view that, given the change in direction in the project, the impact of the IAASB's decision about the status and authority is less measurable because it is merely a clarification of what was intended by the language currently included in the Preface. The Working Group's view of the key factors regarding impact analysis are:
- The alternative considered by the IAASB (i.e., to elevate IAPSs to a status and authority equivalent to that of application and other explanatory material) would have discrete cost implications in jurisdictions where the IAPSs are not currently used and national guidance of a similar nature does not exist.
 - The actual impact of clarifying the obligation in relation to IAPSs (by expanding on what was already included in the Preface) will vary depending on how national standard setters and auditors had interpreted the Preface.
 - Clarifying the auditor's obligation with regard to IAPSs will lead to increased consistency in practice related to use of the material and is intended to increase audit quality, in particular in the context of IAPS 1012 by highlighting issues that are known to be encountered in practice.
18. The Working Group considered whether it would be meaningful to make reference to the impact analysis in the ED without using the new format and template, and concluded that this may be confusing despite the IAASB's rationale for doing so.

⁴ See paragraph A7 of ISA 230, *Audit Documentation*.

⁵ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

Accordingly, no reference to the impact analysis has been made in the Appendix.

Matters for IAASB Consideration

6. Does the IAASB agree with the Working Group's position in regard to the question of the establishment of a documentation requirement?
7. The IAASB is also asked for feedback on the draft ED included in the Appendix. The Working Group intends to revise the draft ED based on the discussions during the meeting prior to its approval.

Appendix

EXPLANATORY MEMORANDUM

Introduction

This memorandum provides background to, and an explanation of, the proposals relating to the withdrawal of the extant International Auditing Practice Statements (IAPSs) and clarification of the status and authority of future IAPSs. The International Auditing and Assurance Standards Board (IAASB) approved these proposals in [June 2010] for exposure.

Background

The IAASB's *Strategy and Work Program, 2009-2011* includes a project to review:

- The appropriateness of the content of the IAPSs and determine whether they should be withdrawn or revised; and
- The authority of IAPSs and any other implementation guidance that the IAASB may develop.

The Extant IAPSs

There are currently six IAPSs that are effective:¹

- IAPS 1000, *Inter-bank Confirmation Procedures*
- IAPS 1004, *The Relationship Between Banking Supervisors and Banks' External Auditors*
- IAPS 1006, *Audits of the Financial Statements of Banks*
- IAPS 1010, *The Consideration of Environmental Matters in the Audit of Financial Statements*
- IAPS 1012, *Auditing Derivative Financial Instruments*
- IAPS 1013, *Electronic Commerce—Effect on the Audit of Financial Statements*

In general, all of the IAPSs are largely now out-of-date and inconsistent with the text of the clarified International Standards on Auditing (ISAs). Of the above, interest in revising and updating has been expressed only in relation to IAPSs 1004,² 1006³ and 1012 as they are currently being used in practice in some jurisdictions.

¹ These IAPSs are included in Part II of the 2010 IFAC *Handbook of International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements*.

² IAPS 1004 is a joint document of the International Auditing Practices Committee (the predecessor of the IAASB) and the Basel Committee on Banking Supervision (the Basel Committee). Both have approved and published the document, which is based on ISAs extant at October 1, 2001.

³ The IAPC bank audit sub-committee included observers from the Basel Committee; however, the IAPS has not been approved nor published by the Basel Committee. It is based on ISAs extant at October 1, 2001.

Over the last few years, numerous external parties have sought clarification about the level of authority, perceived and real, that attaches to IAPSs. Some have indicated that the current description of IAPSs in the *Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services* (the Preface) is unsatisfactory in that it does not call for any sort of substantive obligation to consider the material contained in an IAPS; it can be ignored as long as the auditor can describe how requirements have been met. Others have indicated that they expect use of certain of the IAPSs – for example, the IAPSs dealing with banks – and therefore have encouraged their revision, carrying at least the same authority as they have now. On the other hand, some national standard setters (NSS) have not adopted the IAPSs, choosing instead to issue additional practical guidance, tailored to national circumstances, through their own established vehicles.

Existing IAPSs have been developed and approved following the same due process as that afforded ISAs, and this is expected to remain unchanged under the due process approved by the Public Interest Oversight Board (PIOB). In light of this, assigning IAPSs and ISAs different authorities is viewed by some as inconsistent and confusing. The application of the same due process certainly suggests, in some quarters, that IAPSs have the same authority as their underlying ISA(s). This issue is compounded by questions about the relationship between the IAPSs and the application and other explanatory material of the clarified ISAs.

Rationale for the IAASB's Project to Review the IAPSs

The IAASB has heard calls for more guidance, foremost on auditing complex financial instruments. Accordingly, in June 2009 the IAASB approved a project proposal⁴ to revise extant IAPS 1012, in part to provide educational material on the topic and to highlight practical considerations that are currently posing challenges in audits of complex financial instruments. Consultation with stakeholders has indicated there is a real need for guidance material on this topic, at a level of detail above what would ordinarily be fit for an international standard (so as not to overburden or reduce the general applicability of the ISAs). Decisions relating to the scope and authority of proposed IAPS 1012 (Revised) likewise will be applicable to any future guidance to be developed as part of the IAASB's ongoing strategy. Equally, the IAASB Clarity project and the possible adoption of ISAs by the European Commission (EC) have revived this issue. These developments increase the urgency with which the IAASB needs to address the status and authority of IAPSs.

The IAASB's discussions have focused on are four highly-interrelated issues central to the way forward for IAPSs:

- (i) What, if anything, should be done with respect to the extant IAPSs?
- (ii) How should the authority and purpose of new IAPSs be described, to make clear that they contain important material to be considered by the auditor while at the same time keeping them distinguishable from the body of ISAs to which compliance is required?

⁵ IFAC's Standards-Setting Public Interest Activity Committees' Due Process and Working Procedures can be accessed at http://web.ifac.org/download/PIAC-Due_Process_and_Working_Procedures.pdf.

- (iii) Following from (ii), how should such a statement be positioned, to achieve the aim of expected use of IAPSs while not creating unnecessary complications relative to the body of ISAs?
- (iv) How could the IAASB best proceed to ensure that any new IAPS is carefully considered and unhelpful proliferation is avoided? The IAASB's deliberations and proposals on these matters are discussed in more detail below.

Proposal to Withdrawal the Extant IAPSs

The IAASB has agreed in principle that it is likely necessary to withdraw the six extant IAPSs, subject to the views on consultation. They are out-of-date and potentially misleading. More fundamentally, this is seen as necessary to create a clean slate approach to any new IAPS in relation to the issue of status and authority, and also allows the IAASB to determine what new IAPSs should be developed for the future.

The proposed treatment of the extant IAPSs is as follows:

- IAPS 1000, 1010, and 1013 – Withdrawal with no further action.
- IAPS 1004 – Withdrawal and explore how the relevant material in the IAPS may be maintained, not as an IAPS but in another form.
- IAPS 1006 – Withdrawal with consideration of the need for a future project to address the topic. The current IAPS is not adequate; for example, material regarding internal control is not based on a suitable internal control framework such as Committee of Sponsoring Organizations (COSO), and is often replaced with national guidance tailored to the domestic regulatory environment.
- IAPS 1012 – Withdrawal and replace with proposed revised IAPS currently under development.

The strategy questionnaire issued by the IAASB listed the current project to clarify the status and authority of IAPSs, and review the appropriateness and content of the existing IAPSs, including whether they should be revised or withdrawn. Any revision projects deemed necessary by respondents and approved by the IAASB would be factored into the strategic planning cycle for the period 2012-2014 and considered in the context of the IAASB's assessment of its relative priorities. Should respondents believe revisions to any extant IAPSs are necessary, it would be helpful for the IAASB to be aware of this view, as well as respondents' views as to the form of output that material should take in light of the IAASB's plans to evaluate the development of new IAPSs based on criteria (see further discussion below).

Criteria for the Development of New IAPSs

IAASB discussions have indicated the need for a vehicle to provide practical assistance to auditors, in particular when such guidance relates to more than one ISA and incorporating the guidance into an ISA in the form of application material would unbalance the ISA or result in the inclusion of material that is not applicable in virtually all engagements. For this reason, while the IAASB believes withdrawal of the extant IAPSs is appropriate at this time, the IAASB has agreed to allow for the possibility of developing new IAPSs in the future.

However, an important consideration in determining the status and authority of future IAPSs is the need to ensure that new IAPSs are developed only in appropriate circumstances. The IAASB therefore generally supported establishing criteria as to when an IAPS would be needed. A relatively high hurdle for that would help alleviate concerns that the issuance of IAPSs is an indication that the set of ISAs alone is incomplete or not adequate in particular circumstances. It should also mitigate the concern expressed by some that:

- It would be undesirable for there to be a proliferation of IAPSs in the future.
- It may not be appropriate for the IAASB to develop and issue authoritative industry-specific guidance that is significantly affected by regulations in a particular jurisdiction, in the absence of globally accepted regulations. The risk would be that the IAASB would spend significant time and effort to develop pronouncements that would not be used by many NSS, who would instead favor developing guidance tailored to their particular domestic regulatory environment.
- An IAPS would be developed when it would otherwise be appropriate for the matter to be addressed by developing non-authoritative guidance (such as a Staff Audit Practice Alert or Staff Questions & Answers publication).

[Recognizing these concerns, the IAASB proposes that new IAPSs should only be developed if they meet the following criteria:

- There is divergent practice internationally, or a need to raise awareness of issues being encountered in practice in particular areas, and therefore promulgating an IAPS would promote high-quality auditing practice, contributing to improved financial reporting;
- Such guidance would provide practical assistance to auditors in particular circumstances or industries, and would be applicable without significant modification for national circumstances;
- Research and discussions with stakeholders who may have recommended the project for consideration by the IAASB have indicated that:
 - Background and educational material is needed or the issue extends across a number of ISAs but does not necessitate the development of new requirements, and therefore promulgating an IAPS will be effective in promoting good practice; and
 - There is not likely to be a need for new or modified requirements or application material in the ISAs, as in such circumstance it would be more appropriate to develop or revise an ISA rather than develop an IAPS; and
- The need for guidance is widely acknowledged by stakeholders and the guidance would be expected to remain useful for the foreseeable future. In this regard, the IAASB should seek to become aware of whether any NSS have developed, or intend to develop, guidance on the topic under consideration to assist the IAASB in determining whether it is appropriate to develop international guidance on the topic.]

The *Due Process and Working Procedures*⁵ requires a proposal to start a new project to be prepared based on research and on appropriate consultation within the IAASB, with consideration given to the costs and benefits of the anticipated output of the proposed project. Further, before approval, the IAASB considers and prioritizes the project proposal having regard to the public interest. A project proposal identifies, where applicable, who has recommended the project for consideration by the IAASB. Project proposals identify the objectives of the project and explain how achievement of those objectives would serve the public interest.

[The IAASB is of the view that, in determining whether to undertake a project to develop guidance on a particular topic, a more structured consideration of the appropriate form of output in the circumstances could be undertaken based on the criteria set forth above when there is a possibility that the output would be a new IAPS. The decision to pursue an IAPS would be made only if that course of action is appropriate in the circumstances, and only after evaluating the merits of proposing new or modified requirements or application material in an ISA, or the development of a Staff publication.]

Certain of these criteria can also be usefully applied in decisions on whether to develop new, or revise existing, ISAs. In approving the project proposal, the IAASB will need to concur with Staff's preliminary position or agree to revise to the project proposal. However, over the course of the project, the IAASB can reassess the anticipated output of the project, if considered necessary. Finally, the explanatory memorandum (EM) of the ED for a new IAPS will explain how the IAASB determined an IAPS was necessary in undertaking the project.

Views on whether the IAASB's plans to evaluate the need for any new IAPSs against proposed criteria are appropriate, and whether the proposed criteria are in fact those against which such evaluations should be measured, are particularly welcome.

Proposal to Clarify the Status and Authority of Future IAPSs

Use of IAPSs varies widely by jurisdiction. Consultations with NSSs indicated that, in general, IAPSs are currently used by NSS in one of three ways:

- (i) Included in the auditing literature as an IAPS, with the same content as is included in the IAASB's Handbook;
- (ii) Included as guidance in the auditing literature under a different name, for example Practice Notes, with similar content and authority as the extant IAPSs;
- (iii) Not used, either because the IAPSs are considered unnecessary or not relevant, or because other jurisdiction-specific guidance exists, for example, that may be based on national law or regulation.

⁵ IFAC's Standards-Setting Public Interest Activity Committees' Due Process and Working Procedures can be accessed at http://web.ifac.org/download/PIAC-Due_Process_and_Working_Procedures.pdf.

The current Preface states:

International Auditing Practice Statements (IAPSs) are issued to provide interpretive guidance and practical assistance to professional accountants in implementing ISAs and to promote good practice ... Professional accountants should be aware of and consider Practice Statements applicable to the engagement. A professional accountant who does not consider and apply the guidance included in a relevant Practice Statement should be prepared to explain how: (a) the requirements in the ISAs; or (b) the basic principles and essential procedures in the IAASB's other Engagement Standard(s), addressed by the Practice Statement, have been complied with.

The IAASB has expressed divergent views on the intent of current Preface and agrees that clarification is needed. Some interpret the Preface to impose a strong obligation for the auditor to read, understand and apply the guidance in an IAPSs, while others view it as a “comply or explain” model that promotes awareness of IAPSs but does not directly impose an obligation on the auditor, because the compliance is in fact with the requirements of the ISAs rather than the IAPS.

In considering how to clarify the status and authority, some IAASB members feel strongly that, if the IAASB determines it is necessary to develop an IAPS and the expectation is that the IAPSs would be read, an obligation should attach to the description. In contrast, retaining the “comply or explain” model introduces a level of discretion that is less than helpful.

Others consider that, if the material in an IAPS is of such importance, it should be incorporated into the body of the ISAs. The rationale against doing so is that such material may affect a number of ISAs and include educational material that would not be appropriate for an ISA. Accordingly, the IAASB rejected a proposal to give IAPSs the same status as application and other explanatory material in the ISAs as this was seen to extend the ISAs, which is not desirable.

Further the majority of the IAASB believes that there is a distinction between application and other explanatory material (which is guidance that is necessary to understand how a particular requirement should be applied) and an IAPS (which is guidance to provide practical assistance but is not essential to the proper application of the requirements in the ISAs).

The intent of the IAASB in proposing changes is to:

- Clarify the purpose of IAPSs and the nature of the material contained therein;
- Explain that IAPSs do not impose additional requirements on auditors beyond the ISAs; and
- Ensure that auditors are aware of the existence of the IAPSs and have an understanding of any IAPS(s) that may be relevant to the circumstances of the audit.

The IAASB believes that using criteria when determining whether to develop new IAPSs and clarifying within each IAPS the relevance of the document and its target audience will assist in ensuring that the IAPSs are capable of providing practical assistance to auditors and promoting good practice as intended.

However, in clarifying the auditor's obligation with respect to the IAPSs, it is not the IAASB's intent to establish a documentation requirement (or suggest that documentation may be appropriate) addressing the auditor's determination as to whether any IAPS was relevant to the audit and, if so, the required understanding of its content.

Placement of the Wording to Describe the Auditor's Obligation

The IAASB also considered the question of where such wording should be placed, believing it is necessary to clarify the expectation and promote the use of IAPSs, but equally recognizing that doing so should be considered from a practical implementation point of view.

The IAASB discussed a range of options that could be considered, individually or in combination. These include from weakest to strongest in terms of:

- Continuing to use (only) the Preface to describe the authority of IAPSs.
- Relying on the IFAC Statement of Membership Obligation (SMO) 3⁶ and the IAASB Policy Position (June 2006), *Modifications to International Standards of the IAASB—A Guide for National Standard Setters that Adopt IAASB's International Standards but Find It Necessary to Make Limited Modifications*⁷ to highlight IAPSs and how they should be considered by IFAC member bodies and used by NSS.
- Describing the IAASB's views on the hierarchy of its standards and guidance in another manner, such as an IAASB Policy Position.
- Incorporating the auditor's obligation into ISA 200.⁸

[While the IAASB does not have a unanimous view on where the auditor's obligation regarding IAPSs should be described, it has agreed to continue to describe the auditor's obligations relating to IAPS in the Preface and develop a hierarchy explaining the relationship of the ISAs, IAPSs and Staff Publications.] The IAASB's proposals to describe the status and authority of the IAPSs are included in paragraph 23 of the amendments to the Preface. Views on both the proposed changes to the status and authority and how the distinction between the IAASB's authoritative pronouncements and non-authoritative material is described in the Preface are encouraged. Subject to the views on consultation, an IAASB Policy Position containing the proposed hierarchy will be developed.

In arriving at this conclusion, the IAASB recognizes there may be merit in including the

⁶ IFAC SMO 3 (Amended November 2006), *International Standards, Related Practice Statements and Other Papers Issued by the IAASB*. SMO 3 states that "Member bodies should use their best endeavors ...to assist with the implementation of International Standards [ISs] or national standards [NSs] and related other pronouncements that incorporate International Standards. This includes promoting the use of related Practice Statements, or the development of national pronouncements that incorporate related Practice Statements or that provide similar implementation guidance."

⁷ The Modifications Policy can be accessed at: web.ifac.org/publications/international-auditing-and-assurance-standards-board/policy-positions-and-papers.

⁸ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

auditor's obligation within ISA 200 at a future date because doing so may be most effective in ensuring that auditors are aware of the fact that there may be material in addition to the ISAs that is relevant to the conduct of an audit in particular circumstances. However, given the challenges of doing so in the context of jurisdictions that are currently adopting the clarified ISAs into law or regulation and the possible adoption of the ISAs by the EC, the IAASB does not believe proposing amendments to ISA 200 is appropriate at this time.

The IAASB also does not believe that using the SMOs to promote the use of IAPSs would achieve the same effect as including wording in the Preface, as certain NSSs who are not IFAC member bodies are not obligated to follow the SMOs. Views on whether SMO 3 will need to be amended in light of the proposed changes to the Preface would be welcome.

Effective Date

Subject to views on consultation, the IAASB intends to consider the withdrawal of the IAPSs at its December 2010 meeting. The proposed changes to the Preface would become effective when approved by the IAASB.

Guide for Respondents

The IAASB invites comments on any aspects of the proposals to withdraw the extant IAPSs and clarify the status and authority of future IAPSs discussed in this memorandum.

PROPOSED AMENDMENTS TO THE PREFACE TO THE INTERNATIONAL STANDARDS ON QUALITY CONTROL, AUDITING, REVIEW, OTHER ASSURANCE, AND RELATED SERVICES PRONOUNCEMENTS

Introduction

1. This preface to the International ~~Standards on~~ Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements (~~International Standards or IAASB's Standards~~) is issued to facilitate understanding of the scope and authority of the pronouncements the International Auditing and Assurance Standards Board (IAASB) issues, as set forth in the IAASB's Terms of Reference.
2. The IAASB is committed to the goal of developing a set of International Standards and other pronouncements which are generally accepted worldwide. IAASB members act in the common interest of the public at large and the worldwide accountancy profession. This could result in their taking a position on a matter that is not in accordance with current practice in their country or firm or not in accordance with the position taken by those who put them forward for membership of the IAASB.

The IAASB's Pronouncements

IAASB Authoritative Pronouncements

3. The IAASB's pronouncements govern audit, review, other assurance, and related services engagements that are conducted in accordance with International Standards. They do not override the local laws or regulations that govern the audit of historical financial statements or assurance engagements on other information in a particular country required to be followed in accordance with that country's national standards. In the event that local laws or regulations differ from, or conflict with, the IAASB's Standards on a particular subject, an engagement conducted in accordance with local laws or regulations will not automatically comply with the IAASB's Standards. A professional accountant should not represent compliance with the IAASB's Standards unless the professional accountant has complied fully with all of those relevant to the engagement.
4. The authoritative pronouncements of the IAASB comprise International Standards and Practice Statements. Both are issued following IAASB's stated due process and are contained in the IFAC *Handbook of International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements*.
5. The obligations associated with, and further description of, International Standards and Practice Statements issued by the IAASB are provided below.

Non-Authoritative Material

6. Non-authoritative material may be published on the IAASB website. This may include, for example, Staff Audit Practice Alerts, Staff Question and Answer (Staff Q&A) publications, Discussion Papers and other types of documents of a similar nature. Staff Publications are used to help raise practitioners' awareness in a timely manner of significant new or emerging issues or other noteworthy circumstances relevant to engagements addressed by IAASB pronouncements, to direct their attention to relevant provisions of IAASB pronouncements, or to provide clarification to emerging questions by referring to existing requirements and application material. Other material may be commissioned to promote discussion or debate on quality control, auditing, review, other assurance and related services issues affecting the accounting profession, or to present findings or describe matters of interest relating thereto.
7. Non-authoritative material does not form part of the IAASB's International Standards and Practice Statements. No general or specific obligation is imposed on professional accountants as a result of their publication on the IAASB website.

The Authority Attaching to International Standards Issued by the International Auditing and Assurance Standards Board

84. International Standards on Auditing (ISAs) are to be applied in the audit of historical financial information ...

[No amendments are proposed to paragraphs 5–9; however, these paragraphs will be renumbered accordingly]

International Standards on Auditing

1410. ISAs are written in the context of an audit of financial statements¹ by an independent auditor. They are to be adapted as necessary in the circumstances when applied to audits of other historical financial information. The authority of ISAs is set out in ISA 200.²

International Standards on Quality Control

1514. ISQCs are written to apply to firms in respect of all their services falling under the IAASB's Engagement Standards. The authority of ISQCs is set out in the introduction to the ISQCs.

¹ Unless otherwise stated, "financial statements" mean financial statements comprising historical financial information.

² ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*

Other International Standards

1642. Some International Standards identified in paragraphs 9–115–7 contain: objectives, requirements, application and other explanatory material, introductory material and definitions. These terms are to be interpreted in a directly analogous way to how they are explained in the context of ISAs and financial statement audits in ISA 200.
1743. Other International Standards identified in paragraphs 9–115–7 contain basic principles and essential procedures (identified in bold type lettering and by the word “should”) together with related guidance in the form of explanatory and other material, including appendices. The basic principles and essential procedures are to be understood and applied in the context of the explanatory and other material that provides guidance for their application. It is therefore necessary to consider the entire text of a Standard to understand and apply the basic principles and essential procedures.

[No amendments are proposed to paragraphs 14–18; however, these paragraphs will be renumbered accordingly]

The Authority Attaching to Practice Statements Issued by the International Auditing and Assurance Standards Board

International Auditing Practice Statements

19. ~~International Review Engagement Practice Statements (IREPSs), International Assurance Engagement Practice Statements (IAEPSs) and International Related Services Practice Statements (IRSPSs) are issued to serve the same purpose for implementation of ISREs, ISAEs and ISRSs respectively.~~
20. ~~Professional accountants should be aware of and consider Practice Statements applicable to the engagement. A professional accountant who does not consider and apply the guidance included in a relevant Practice Statement should be prepared to explain how:~~
- ~~(a) The requirements in the ISAs; or~~
 - ~~(b) The basic principles and essential procedures in the IAASB’s other Engagement Standard(s), addressed by the Practice Statement, have been complied with.~~
23. International Auditing Practice Statements (IAPSs) are issued to provide interpretive guidance and practical assistance to auditors professional accountants in implementing ISAs and to promote good practice. IAPSs do not impose additional requirements on auditors beyond those included in the ISAs, nor do they change the auditor’s responsibility to comply with the requirements of all ISAs relevant to the audit. However, auditors should determine whether any IAPS is relevant to the circumstances of the audit and, if so, obtain an understanding of its content. Depending on the nature of the topic(s) covered, an IAPS may assist the auditor in:

- (a) Obtaining an understanding of the circumstances of the entity, and in making judgments about the identification and assessment of risks of material misstatement;
- (b) Making judgments about how to respond to assessed risks, including judgments about procedures that may be appropriate in the circumstances; or
- (c) Addressing reporting considerations, including forming an opinion on the financial statements and communicating with those charged with governance.

Practice Statements Relating to Other International Standards

24. Although none has been issued to date, the IAASB may also issue International Review Engagement Practice Statements (IREPSs), International Assurance Engagement Practice Statements (IAEPSs), and International Related Services Practice Statements (IRSPSs)—~~are issued to~~ serve the same purpose for ~~implementation of ISREs, ISAEs, and ISRSs respectively.~~

Other Papers Published by the International Auditing and Assurance Standards Board

21. ~~Other papers, for example Discussion Papers, are published³ to promote discussion or debate on auditing, review, other assurance and related services and quality control issues affecting the accounting profession, present findings, or describe matters of interest relating to auditing, review, other assurance, related services and quality control issues affecting the accounting profession. They do not establish any basic principles or essential procedures to be followed in audit, review, other assurance or related services engagements.~~

Language

2522. The sole authoritative text of an exposure draft, International Standard, Practice Statement or other paper is that published by the IAASB in the English language.

³ ~~The IAASB Chair will appoint a review group of four IAASB members to consider whether a draft paper has sufficient merit to be added to the IAASB's literature. The draft paper may come from any source and the IAASB need not have specifically commissioned it. If the review group believes that the paper has sufficient merit, it recommends to the IAASB that the paper be published and added to its literature.~~