

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

Matters for Discussion

1. There are four highly-interrelated issues central to the way forward for IAPs:
 - (i) What if anything should be done with respect to the extant IAPs?
 - (ii) How should the authority and purpose of new IAPs 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?
 - (iii) Following from (ii), how should such a statement be positioned, to achieve the aim of expected use of IAPs while not creating unnecessary complications relative to the body of ISAs?
 - (iv) How should the IAASB best proceed to ensure that any new IAP is carefully considered and unhelpful proliferation is avoided?

Issue (i)—Extant IAPs

2. The IAASB has agreed in principle that it is likely necessary to withdraw the six extant IAPs, 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 They are out of date and potentially misleading.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 IAP in relation to the issue of status and authority, and also allows the IAASB to determine what new IAPs, if any, should be developed for the future (see further discussion on criteria below).

Issue (ii)—Clarifying the Status and Authority of the IAPs

3. The current Preface states:

International Auditing Practice Statements (IAPs) 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.

4. The IAASB has expressed divergent views on the intent of current Preface and agreed 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 IAPs, 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.

5. 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. 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 (as illustrated by IAPS 1012). Giving IAPSs the same status as application material in the ISAs seems to extend the ISAs which is not desirable. In contrast, retaining the “comply or explain” model introduces a level of discretion that is less than helpful.
6. The following wording seeks to clarify the status and authority, incorporating the suggestions from the March 2010 meeting and the subsequent discussion by the Working Group:

International Auditing Practice Statements are issued to provide practical assistance to auditors on particular topics that may be addressed by a number of ISAs and to promote good practice. The auditor shall determine whether any IAPS is relevant to the circumstances of the audit. If the auditor determines an IAPS is relevant, the auditor shall obtain an understanding of the IAPS and consider whether the examples of procedures in the IAPS may be appropriate in the circumstances. However, an IAPS does not impose requirements for auditors to perform the procedures that may be contained in the IAPS. IAPSs are not intended to provide further explanation of the requirements, nor explain more precisely what a requirement means or is intended to cover, as this is the role of the application and other explanatory material within the ISAs.

7. One implication of the above wording is that an IAPS will need to be quite clear on its relevance. This is being taken into account in revising IAPS 1012. Equally important is where it will be placed; but the IAASB is first asked to consider the above.
8. Subject to feedback received from the IAASB and NSSs, the Working Group intends to finalize the wording for inclusion in the anticipated July consultation on IAPS 1012 to solicit views on how such wording would be interpreted, and whether it is appropriate in light of the content of IAPS 1012 (or indeed, whether the content of IAPS 1012 is appropriate in light of its authority).

Matter for IAASB Consideration

Q1. The IAASB is asked for its views on the proposed revised wording. In particular:

- Is it a clearer statement when compared to the extant statement?
- Does it effectively communicate the need for the auditor to read the IAPS, while at the same time making clear that it is neither part of the ISAs nor equivalent to application material?

Issue (iii)—Placement of the Wording Describing the Auditor’s Obligation

9. Should the IAASB continue to support the need to clarify the existing wording describing the authority attaching to IAPSs, the question then is where such wording should be placed. It is necessary to clarify the expectation and promote the use of IAPSs, but equally important that doing so be considered from a practical implementation point of view.
10. There is 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) 3¹ and the IAASB Policy Position about Modifications to International Standards by National Standard Setters to highlight IAPSs and how they should be considered by IFAC member bodies and used by NSSs.
 - 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 200.²
11. These proposals were presented in Agenda Item 6-A of the March 2010 agenda material but were not discussed during the meeting. The Working Group has agreed that the four proposals remain relevant in light of the March 2010 IAASB discussions on the proposed wording to describe the status and authority, and proposes that the various options and any preference thereon be put forth as part of the consultation on IAPS 1012 related to the question of its authority. This will allow for feedback on how each option might be viewed by different jurisdictions. The above options are discussed below.

Continuing to Use the Preface to Describe the Authority of IAPSs

12. This option essentially retains the status quo. It is effectively assuming that auditors have been following the Preface in relation to the IAPSs that currently exist today. However, as part of the Clarity project, the intent was for auditor’s obligations when conducting an audit in accordance with ISAs to now be wholly contained in ISA 200. In addition, some jurisdictions that adopt the ISAs into law or regulation do not reproduce or adopt the Preface. Auditors in those jurisdictions therefore may not look to the Preface to identify additional guidance that may be relevant to their audits.

Relying on SMO 3 and the IAASB Policy Position about Modifications to International Standards by National Standard Setters

13. IFAC SMO 3 (Amended November 2006³) states that “Member bodies should use their best endeavors ...to assist with the implementation of International Standards [ISs] or

¹ SMO 3, *International Standards, Related Practice Statements and Other Papers Issued by the IAASB*

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

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.”

14. While SMO 3 places an obligation on member bodies to build awareness of IAPSs, it also allows for the development and use of national implementation guidance in lieu of adopting the IAPSs. If the status of IAPSs is to be addressed in SMO 3, the current obligation in SMO 3 to “promote the use of Practice Statements” would need to be strengthened. However, relying solely on the SMOs to convey the status, authority and other key matters relating to adopting the IAPSs may not be effective, since not all NSSs who have adopted, or intend to adopt the ISAs, are obligated by the SMOs.
15. Related, 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*,⁴ sets out the IAASB’s views on when a NSS that adopts the IAASB’s ISs as their NSs with little or no amendment can assert that their NSs conform to ISs. Preliminary discussions with the IAASB have indicated that this Policy Position may need to be revised to explicitly cover all IAASB pronouncements, including IAPSs. Also, in light of the proposed obligation, the Policy Position could be updated to describe the process by which NSSs may be permitted to make changes to IAPSs or conclude that equivalent guidance developed by NSSs carries the same intent and authority as the IAPSs. This would further strengthen the use of new IAPSs.

Incorporating the Auditor’s Obligations into ISA 200

16. The intent in commencing a project to revise IAPS 1012 was to provide guidance on how the requirements of the ISAs could be applied in a particular circumstance. IAASB discussions have indicated the need for a vehicle to do so, 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.
17. Incorporating the obligation with respect to IAPS 1012 described in paragraph 6 into ISA 200 as a discrete requirement 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. There are implications from this approach however, as discussed below, and therefore the IAASB’s views on this are particularly important.
18. Making changes to ISA 200 may affect those that have or are in process of adopting the ISAs, and in particular those adopting or planning to adopt the ISAs in law or regulation such as the European Commission (EC). It was explained at the December 2009 meeting that while the European Union (EU)’s 8th Company Law Directive does contemplate that IAPSs

³ SMO 3 was amended in part to update it for the IAASB’s discussion on IAPSs at its May 2006 meeting.

⁴ The Modifications Policy can be accessed at: web.ifac.org/publications/international-auditing-and-assurance-standards-board/policy-positions-and-papers.

could be adopted into law on a case-by-case basis the current IAPSs are not being considered for adoption concurrently with the clarified ISAs.

19. The Working Group nevertheless feels that future IAPSs (which would presumably be developed under clear criteria and kept up to date) are a necessary form of authoritative guidance and therefore should be adopted by those that are adopting the ISAs. It therefore believes that a party could not decide on a case-by-case basis whether to adopt an IAPS if the IAPS is relevant to the audit. This would not be inconsistent with the current obligation on auditors under ISA 200 to address new or revised ISAs to comply with the ISAs.⁵
20. For reference, the International Accounting Standards Board (IASB) includes their International Financial Reporting Interpretations Committee (IFRIC) Interpretations as International Financial Reporting Standards (IFRSs) mandatory pronouncements. Interpretations of IFRSs are prepared by the IFRIC to give authoritative guidance on issues that are likely to receive divergent or unacceptable treatment, in the absence of such guidance. Financial reporting statements must not be described as complying with IFRSs unless they comply with all the requirements of IFRSs (including IFRICs). IAS 8⁶ notes that when a Standard or an Interpretation specifically applies to a transaction, other event or condition, the accounting policy or policies applied to that item must be determined by applying the Standard or Interpretation and considering any relevant Implementation Guidance issued by the IASB for the Standard or Interpretation. This appears to give IFRSs developed by the IASB and Interpretations developed by IFRIC equal authority.

Hierarchy of Standards and Guidance, Including IAPSs

21. To clarify the status of IAASB's authoritative pronouncements (ISAs and IAPSs), as well as the distinction between such pronouncements and non-authoritative pronouncements (e.g., Staff Publications), there is the option of establishing a formal hierarchy of pronouncements and guidance. Such a hierarchy could be placed in either in the Preface, an IAASB Policy Position, or both, as means to build sufficient awareness. The Appendix includes a possible proposal for a hierarchy.

Matter for IAASB Consideration

- Q2. Using IAPS 1012 for context, what in the IAASB's view is the most appropriate placement for the language proposed in paragraph 6? In addressing this question, the IAASB is asked to comment on what it considers to be the main benefits and drawback of each option.

Issue (iv)—Criteria Used to Determine the Appropriateness of Developing a New IAPS

22. An important consideration in resolving the above, and in particular if the route to be taken is to have a strong obligation and placement in ISA 200, is the need to ensure that new IAPSs are developed only in appropriate circumstances. The IAASB therefore

⁵ Paragraph 18 of ISA 200 states: "The auditor shall comply with all ISAs relevant to the audit. An ISA is relevant to the audit when the ISA is in effect and the circumstances addressed in the ISA exist."

⁶ International Accounting Standard (IAS) 8, *Accounting Policies, Changes in Accounting, Estimates and Errors*

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 NSSs, 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 Q&A).
23. Like other IAASB projects, the decision to develop an IAPS begins with a project proposal discussed by the IAASB. In explaining why guidance on a particular topic is necessary and considering whether an IAPS is the appropriate vehicle to issue such guidance, the project proposal could highlight whether:
- There is divergent practice internationally, and therefore promulgating an IAPS would promote high-quality and consistent auditing practice, contributing to improved financial reporting;
 - Such guidance was needed to help achieve the consistent application of the requirements in the ISAs in particular circumstances or industries, and it would be applicable without significant modification for national circumstances;
 - The issue extends across a number of ISAs but does not necessitate the development of new requirements, and therefore promulgating an IAPS may be more effective than revising application material in particular ISAs;
 - The benefit of an IAPS would exceed the associated cost; and
 - The need for an IAPS is widely acknowledged by stakeholders.

Matter for IAASB Consideration

- Q3. Does the IAASB agree it would be useful to develop criteria for when an IAPS should be developed? If so, are the elements above helpful and are there other considerations that should feature in the criteria?

Appendix

Proposed Hierarchy of Standards and Guidance

IAASB Authoritative Pronouncements

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*.

The obligations associated with, and further description of, International Standards and Practice Statements issued by the IAASB are provided below.

[The proposed wording in paragraph 6 would also be incorporated in the Policy Position, along with relevant information from ISA 200 describing the auditor's obligations in relation to the ISAs.]

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