Agenda Item 1

Complexity, Understandability, Scalability and Proportionality (CUSP) Drafting Principles and Guidelines

> **Overview and Objective of the Discussion**
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> The objective of this Agenda Item is to obtain the Board's consent for staff to finalize and use the CUSP Drafting Principles and Guidelines (CUSP DPGs).
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> The discussion of the CUSP DPGs will focus on the comments received from the targeted outreach and the resulting changes to the CUSP DPGs, particularly regarding the sections on scalability and proportionality. The CUSP Working Group does not intend to seek detailed comments on the CUSP DPGs but welcomes input on matters of fatal flaws.
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> The Agenda material accompanying this paper includes a marked version of the DPGs (**Agenda Item 1-A**) and a clean version (**Agenda Item 1-B**). The marked version will be used in the board discussion.

A. Background to the CUSP Initiative

1. At the December 2019 IAASB meeting, feedback from respondents to the Discussion Paper (DP), *Audits of Less Complex Entities (LCEs): Exploring Possible Options to Address the Challenges in Applying the ISAs* and related outreach, was presented. Although the DP focused on audits of LCEs, there was a strong message in the responses to the DP that many of the issues within the ISAs have a significance for all audits and are not unique to just audits of LCEs. *Agenda Item 6* of that meeting noted that a combination of actions would likely be needed to address the challenges identified by respondents. Accordingly, at the April 2020 IAASB meeting, the Board was broadly supportive of progressing the work to address respondents' comments to the DP as two workstreams: one to address challenges that have been identified in applying ISAs related to CUSP relevant to audits of all types of entities (lead by the CUSP Working Group); and another on addressing the challenges in applying the ISAs in an audit of an LCE (lead by the LCE Task Force).

2. The CUSP workstream centered on developing a set of drafting principles and guidelines to address the concerns noted by respondents to the DP related to the drafting of the ISAs more broadly. In particular, these concerns highlighted that recently revised standards were being perceived as longer, more prescriptive, and more complex than those issued previously. In addition, substantial concerns were noted about the scalability and proportionality of the full suite of ISAs.

3. The CUSP workstream resulted in the Board's consideration of the draft CUSP DPGs at its April 2021 meeting (see *Agenda Item 1*).

Approach Taken in the Draft CUSP DPGs

4. As a reminder, the following key principles underpins the approach taken in the draft CUSP DPGs:

    (a) The **intended primary users** of the draft CUSP DPGs are the IAASB's Staff, operating under the direction of the Board (and Task Force, if applicable). The CUSP DPGs will also be helpful to the Board in reviewing and commenting on revisions to standards and may also be useful to Task Forces and Working Groups, National Standard-Setters, translators, and other users of the ISAs.

(b)   The CUSP DPGs are **directed at the drafting of ISAs**, not other IAASB International Standards. Some principles and guidelines may be useful to the development of other IAASB International Standards.[1]

(c)   The proposed CUSP DPGs are **non-authoritative**.[2] Staff are expected to follow the principles and need to discuss deviations with senior staff. Judgment will need to be exercised on when to raise deviations from the principles with the Board through the normal agenda item process for each project.

(d)   The IAASB has determined that the CUSP DPGs **should not be applied retrospectively** (i.e., to the current IAASB Handbook). Instead, ISAs should be updated to align with the CUSP DPGs as each ISA is revised in due course.

B.   Feedback From Outreach

Targeted Outreach

5.   As discussed with the IAASB in April 2021, feedback was sought on the CUSP DPGs in a targeted fashion. The CUSP initiative is not subject to the IAASB's formal due process, but the CUSP Working Group believed that targeted feedback would provide relevant viewpoints from those with experience in drafting standards and rules. Feedback was received from the IAASB CAG at its September 2021 meeting, at a series of multilateral and bilateral events in Q3, 2021, and via a survey posted on the IAASB website.

IAASB CAG

6.   In summary, the feedback was strongly supportive of the objectives of the CUSP work. Specific comments included:

(a)   Content: The scalability and proportionality sections could be clarified and enhanced (see expanded description below).

(b)   Process:

(i)   The IAASB needs strong leadership and mechanisms to push back on poor drafting.

(ii)   Outreach and consultation, particularly with translators, is important.

(iii)   Questions about whether the CUSP principles would be applied to the existing ISAs.

Other Feedback

7.   In addition to the CAG, feedback was obtained from national standard-setters, regulators, firms, and global standard-setters – many with translation responsibilities. Overall, there was strong support for the initiative from the groups represented. Major feedback included:

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[1]   These include: International Standards on Quality Management (ISQM), International Standards on Review Engagements (ISREs), International Standards on Assurance Engagements (ISAEs), and International Standards on Related Services (ISRSs).

[2]   'Non-authoritative' material is not part of the IAASB International Standards and is not subject to the IAASB's due process (i.e., not subject to the formal approval process as for authoritative documents).

    (a)   Content:

        (i)   Comments about the importance of the project given the length of some recent standards and the length of sentences and complexity of language.

        (ii)   The scalability and proportionality sections are key and should be enhanced (see expanded description below).

        (iii)   There should be more emphasis on developing principles-based standards and limitation of the volume of application material.

        (iv)   The appendices setting out the terms used to describe "likelihood of occurrence" and "work effort" are critical, and the IAASB should look to further reduce the number of terms used.

        (v)   The IAASB should look at how other global standard-setters (IASB and IESBA in particular) use terms and structure their standards. This would provide an opportunity to engage on aligning drafting approaches at a suitably high level (e.g., consistent use of terms such as "extremely rare").

    (b)   Process:

        (i)   The IAASB needs to have mechanisms to consistently apply the CUSP DPGs to all ISA projects.

        (ii)   The IAASB should take the lessons learned from the ISA for LCEs project and incorporate them into the DPGs in due course.

        (iii)   Questions about how the approach of updating the current ISAs for CUSP DPGs when each standard is revised will work when doing narrow-scope projects.

Focus on Scalability and Proportionality

8.   Feedback from the outreach included that the CUSP DPGs correctly reflected the IAASB's current approach, but that more should be done in the DPGs to try to improve drafting of matters related to scalability and proportionality. It was recognized that developing a separate standard for audits of financial statements of LCEs is also part of the package of responses, and that this project may address some of the concerns about the lack of explicit approaches in the ISAs to scalability and proportionality given the typical nature and circumstances of an audit of an LCE.

9.   Notwithstanding the project to develop a separate standard for audits of LCEs, it was also noted that the IAASB would need to remain alert for opportunitites to demonstrate scalability and proportionality in the ISAs themselves to address the concerns that had been raised more broadly and recognizing that the ISAs will continue to be designed to be applied to a wide range of entities with a wide range of circumstances, including varying complexities. There was still some desire for a "building blocks" or bottom-up approach where the standards start with the minimum requirements and then conditional requirements deal with more complex matters. Other possible solutions mentioned were to address proportionality in the project proposal so that the necessary thinking is included in the project design, and an explicit commitment to provide more detailed examples of scalability in practice.
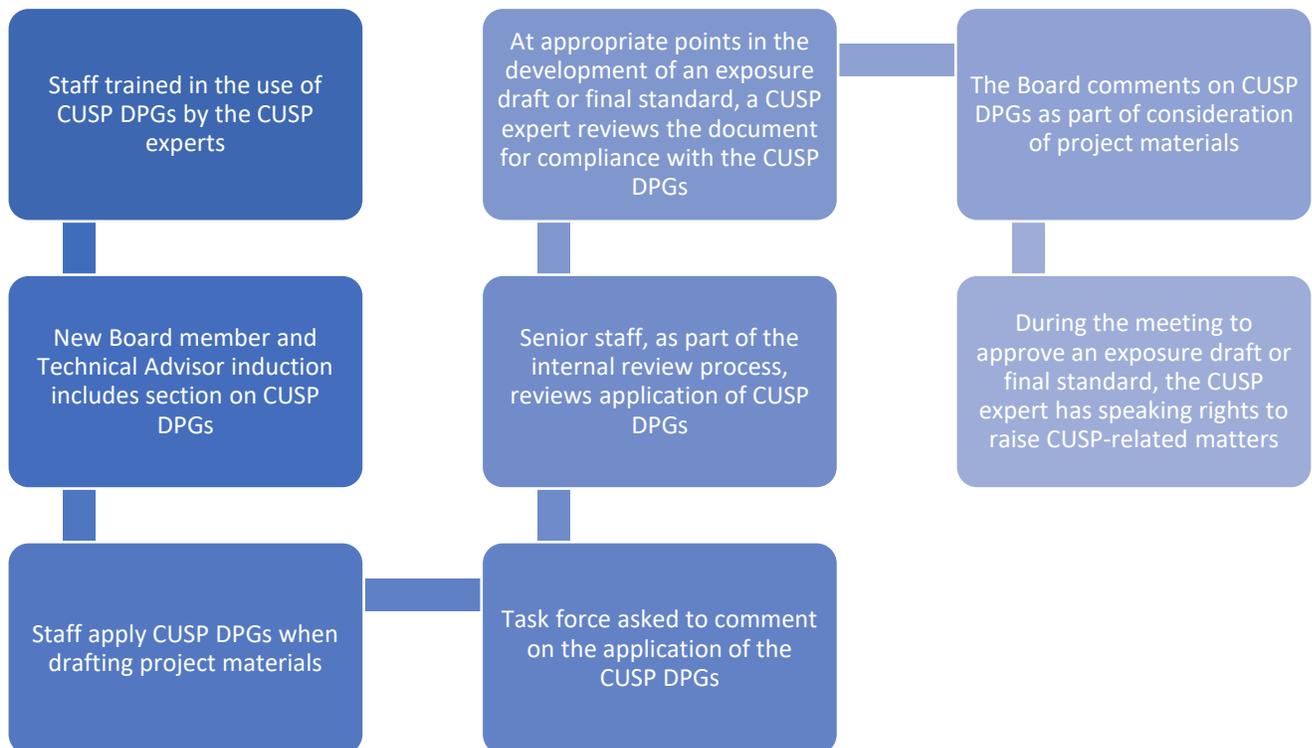
C.   Responses to Feedback

10.   Much of the feedback related to the use of the CUSP DPGs. This is discussed further in Section D below.

11.   In relation to the feedback on content, and in recognition of the need for a stable platform for the staff to use, the CUSP Working Group and Staff determined that the best way forward with the CUSP DPGs is to treat the draft as a first step in an ongoing process. Put another way, **Agenda Item 1-A** is version 1.0 and there will be a version 1.1 in the future. As such, the changes to the CUSP DPGs shown in Agenda item 1-A are limited, with the exception of the section on scalability and proportionality. Future maintenance of the CUSP DPGs is discussed in Section D below.

12.   In relation to feedback on scalability and proportionality, in deciding on the approach to develop drafting principles and guidelines as part of a "package" to address scalability and proportionality in the ISAs more broadly, the IAASB expressed strong views (which had been noted by a number of respondents to the DP) that there was no desire to revise all of the ISAs using a different approach (such as a "building-blocks" approach) (i.e., a "clarity 2" project). Instead, it was agreed that a separate standard be developed for "audits of LCEs" that would address aspects of proportionality (and scalability) aimed at less complex entities. It was agreed that, in developing this separate standard, any learnings that would be relevant to how the ISAs are drafted as it relates to scalability and proportionality could be considered for the broader ISAs at a later time.

13.   Therefore, it is intended that, once the ISA for LCE standard is complete and has been implemented, further consideration be given to whether more is needed regarding proportionality and scalability, and if so, how this can be done. The CUSP Working Group has further considered the comments that are related to specific drafting principles and guidelines on scalability and proportionality considerations, and made relevant changes as described further below.

14.   In brief, the changes shown in Agenda Item 1-A comprise:

(a)   Scalability and Proportionality:

(i)   Clarification of the principle for drafting the ISAs in a manner that is scalable and proportionate, including distinguishing between the aim to be achieved for each.

(ii)   Focusing the drafting guidelines on supporting the drafting of requirements and application and other explanatory material that reflect both scalability and proportionality, together."

(b)   Editorial and other limited changes in response to the points raised in the feedback from outreach.

Matter for IAASB Consideration

1.   Does the IAASB agree to Staff's implementation of the CUSP DPGs (as shown in **Agenda Item 1-A**) as part of its internal procedures?

D.   The Future of CUSP

15.   As noted in Section B above, how the IAASB will implement the CUSP DPGs, including how they will be kept up to date with the latest thinking was a key focus for respondents.

16.   IAASB Staff undertake the substantial drafting of new and revised standards. As such, it will be key that all Staff who have drafting responsibilities are very familiar with the CUSP DPGs so that the initial drafting of new and revised requirements and application material is done in accordance with CUSP DPGs. In addition, IAASB Staff will appoint CUSP DPGs "experts" or "champions" who have sufficient experience and seniority to undertake a full "CUSP" review at an appropriate time in the development of a new or revised standard (i.e., towards the latter part of the development of an exposure draft or final standard, but with sufficient time that changes can still be made).

17.   In addition to the Staff process, various other mechanisms can also be instituted to help Board Members and Technical Advisors (or others involved in the drafting process) with maintaining the stricter drafting requirements related to new and revised standards, including:

(a)   Broadly explaining the importance of the CUSP DPGs in the annual New Board Member Induction session;

(b)   Involving a specific member of each Task Force to specifically focus on maintaining the integrity of the drafting (i.e., ongoing monitoring of CUSP DPGs as drafts are developed); and

(c)   Focusing the Board discussion on the CUSP DPGs by addressing considerations in this regard in the issues paper(s), as appropriate, and including a question to the Board whether there are any further matters related to the application of the CUSP DPGs to be addressed by the Task Force.

Staff trained in the use of CUSP DPGs by the CUSP experts

At appropriate points in the development of an exposure draft or final standard, a CUSP expert reviews the document for compliance with the CUSP DPGs

The Board comments on CUSP DPGs as part of consideration of project materials

New Board member and Technical Advisor induction includes section on CUSP DPGs

Senior staff, as part of the internal review process, reviews application of CUSP DPGs

During the meeting to approve an exposure draft or final standard, the CUSP expert has speaking rights to raise CUSP-related matters

Staff apply CUSP DPGs when drafting project materials

Task force asked to comment on the application of the CUSP DPGs

18. With regard to the ongoing maintenance of the CUSP DPGs, as previously noted, this is intended to be a 'living' document and updated as necessary (for example, where new guidelines and principles are established). It is proposed that the CUSP DPGs be reviewed at least annually to determine the need for any updates. In consultation with the Planning Committee and taking into account feedback from the Board, as appropriate, the Program and Technical Director with concurrence by the IAASB Chair or Deputy Chair would authorize Staff to undertake an update.

Matters for IAASB Consideration

2. Board members are asked for their views on:

    (a) The processes described in paragraphs 16 and 17 above to ensure compliance with the CUSP DPGs. Is there anything else that should be done to help ensure that the CUSP DPGs are followed?

    (b) Maintaining the CUSP DPGs as described in paragraph 18 above.