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Mr. Russell Guthrie
Executive Director
Quality and Member Relations
International Federation of Accountants
545 Fifth Avenue – 14th Floor
New York, NY 10017
U.S.A.

Dear Mr. Guthrie,

Re: Proposed Statements of Membership Obligations 1-7 (Revised)

I am pleased to provide comments of the Standards Group at the Canadian Institute of Chartered Accountants (CICA) regarding the proposed Statements of Membership Obligations. Our review of IFAC's proposals was made in light of the circumstances in Canada where the CICA, a member of IFAC, entirely finances and provides professional and administrative staff support to all of the activities of three Canadian standard setting boards: (a) the Auditing and Assurance Standards Board (AASB); (b) the Public Sector Accounting Board (PSAB) and (c) the Accounting Standards Board. However, the boards act autonomously from the CICA under public oversight bodies.

General Comment

Overall, we strongly support the Applicability Framework under which a member body has either (i) direct responsibility; (ii) shared responsibility or (iii) no responsibility for an SMO area. With respect to standard setting, the CICA falls into the "no responsibility" category. Given the legal, regulatory and governance structure in Canada for setting auditing and accounting standards, and rules of professional conduct, it is not practicable for CICA (or other Canadian member bodies) to implement all of the requirements in the SMOs. We feel that the "best endeavours" concept in the Framework has worked well to date and will continue to do so. For example, the Canadian Auditing and Assurance Standards Board has been successful in adopting the International Standards on Auditing (ISAs) as Canadian Auditing Standards with only minimal changes. These changes relate, for example, to the fact that rules of professional conduct in Canada are the responsibility of provincial accounting bodies who have not yet fully adopted the IFAC Code.

We also support most aspects of description of what is expected of a member body under each category of responsibility. However, we feel that the IFAC Board should consider clarifying certain aspects of the draft SMOs, as set out below.

Request for Specific Comments

Our responses to the matters on which you specifically requested comments are set out below.

1. *Considering differing national regulatory environments around the world, does the applicability framework included in each SMO provide sufficient clarity on what is expected of member bodies, when they have varying degrees of responsibility for an SMO area?*

In most respects, we feel the description in the SMOs of the varying degrees of member responsibility is clear except for paragraphs describing direct responsibility that refer to “exceptional circumstances” and the possible need for departures that are “in the public interest”.

We suggest the following wording change (indicated by underlining):

In exceptional circumstances, an IFAC member body may depart from a requirement of this SMO, if so doing so is determined by the member body to be in the public interest in the particular environment in which that body operates.”

In our view, without this additional wording, there may be an implication that one or more of the international standard setting bodies has developed standards or guidance that are not in the public interest in the broad international context. It seems inappropriate for the SMOs to imply that this might be the case.

We also feel it would be useful to provide examples of what might be considered “exceptional circumstances” that justify a departure from an SMO requirement. In our view, a useful example would be a case where an international standard setting body is embarking on setting standards in an area which represents a new service for many countries. However, in the country of a particular member body, that assurance or related service may be mature, having been performed for many years using robust national standards and supporting guidance. The newly developed international standards might well need to evolve over time before they are appropriate for application in the environment of that particular jurisdiction. In such a case, it would not likely be in the public interest, for the member body in the particular jurisdiction, to adopt the newly developed international standards. As another example, an international body may develop a standard relating to a matter that is relevant in a number of jurisdictions, but not all. One recent example is the international standard for assurance engagements dealing with pro forma financial information. It would not seem appropriate to require a member body to adopt a standard for a service not performed in its jurisdiction.

2. *The SMOs refer to adoption and implementation of international standards and provide descriptions of both concepts to ensure that both terms are understood in their broader meaning. Are these descriptions sufficient to ensure clear understanding that adoption and implementation encompasses a broad range of actions including national convergence, harmonization, incorporation, transposition, and integration of international standards into national frameworks?*

In our view, for reasons noted below, some changes are needed to the SMOs to help ensure that they will provide a basis for a clear understanding of the meaning of adoption.

Inconsistencies with other guidance re adopting international standards

Paragraph 20 states “Adoption typically includes ...a convergence process to eliminate or minimize the differences between international and national standards.” In our view, this is not entirely consistent with, for example, the IAASB’s Policy Position Paper “*A Guide for National Standard Setters that Adopt IAASB’s International Standards but Find It Necessary to Make Limited Modifications.*” That document provides guidance on the conditions that need to exist before a national standard setter may assert that its national standards conform to the international standards sent by the IAASB. In particular, it sets out guidelines for the limited additions to, or deletions from, the international standard that would be allowed if a national standard setter wants to make the conformity assurance.

In our view, the phrase in the SMOs “eliminate or minimize differences” seems somewhat vague. For clarity to be achieved, we suggest that the description of “adoption” in the SMOs more closely mirror what is set out in the IAASB Guide or similar guides.

Compliance with the IFAC Code

There are various references to the IFAC Code in the SMOs. For example, paragraph 20 of SMO 1 on quality control states “Firms shall be required (a) to adhere to a code of ethics (such as the IESBA Code of Ethics...” The use of “such as” implies a wide degree of latitude in whether the IFAC Code would be applied by firms within the jurisdiction of an IFAC member. On the other hand, paragraph 60 of SMO 1 implies there is no latitude. It states “The objectivity and confidentiality principles of the IESBA *Code of Ethics* in relation to the quality assurance review team’s conduct of a review shall be complied with.” Also, these and other references do not seem to be consistent with SMO 4, which contains the same guidance on the Applicability Framework as other SMOs including the degrees of responsibility and recognition of exceptional circumstances.

In addition, it is not clear that various references to the IFAC Code in the SMOs are consistent with guidance in international standards. For example, ISA 200, *Overall objectives of the independent auditor and the conduct of an audit in accordance with International Standards On Auditing*, paragraph 14 states “Relevant ethical requirements ordinarily comprise Parts A and B of the International Ethics Standards Board for Accountants’ Code of Ethics for Professional Accountants (IESBA Code) related to an audit of financial statements together with national requirements that are more restrictive.” Use of the word “ordinarily,” indicates that there is not unlimited latitude in apply the IFAC code of ethics. The wording also clearly establishes the IFAC code as the basis for assessing whether other codes have the required rigour.

In our view, to avoid confusion and achieve greater clarity, further work is needed to ensure that references to the IFAC Code in various SMOs reflect what is stated in SMO 4 and also be consistent with what is stated in relevant international standards.

Other Comments

In our view, there are other areas where changes would help improve the clarity of the draft SMOs.

Diagram 1

Each SMO describes the three levels of responsibility of an IFAC member in the following order: (a) direct responsibility; (b) no responsibility; and (c) shared responsibility. This ordering makes sense since the third level (shared) is a combination of the first two.

Diagram 1 does not reflect this order and it is therefore not consistent with the content of the SMOs. From left to right, it shows the degrees as direct, shared and no responsibility. In our view Diagram 1 would be clearer, and appropriately mirror the text in the SMOs, if the “no responsibility” box were to be moved to the center position and the “shared responsibility” box to the furthest right hand position.

SMO 1 – Quality Assurance Review System

Paragraph 2 – clarity of scope

Paragraph 2 states that SMO 1 deals with an IFAC member’s quality assurance review system covering engagements for various types of “engagements of financial statements.”

This SMO is meant to apply to a broad range of engagements, not just those related to financial statements. For example, paragraph 4 correctly refers to ISQC 1, a standard which covers all assurance and related services engagements. The reference to “financial statements” in paragraph 2 should therefore be deleted.

Paragraphs 3, 7, 80, 81 and 86 – consistency of concepts, terms and definitions

Paragraph 3 is meant to describe three levels of quality assurance. It refers to the “engagement level”, the “firm level” and “the body responsible for quality assurance.” This latter description of what is presumably is a third level is, in our view, far from clear. In addition, paragraph 7 refers to a “quality assurance systems for firms” operated by an external authority, when the reference should be to “quality assurance review system.” Further, paragraphs 80 and 81 appear to describe a fourth level of quality assurance in which the implementation and effectiveness of the third level of quality assurance is assessed.

In our view, it is vital that SMO 1 clearly and consistently describe, and distinguish between, the levels of quality assurance throughout the SMO. In our view, changes in terminology, and clear definitions, are needed to achieve this objective. For example, we suggest that the levels of quality assurance might be more clearly described as follows:

1. Performance of quality control procedures for particular engagements (quality assurance - engagement level)
2. Establishment and implementation by a public accounting firm of a quality control system, setting out policies and procedures to be performed, including those at the individual engagement level (quality assurance - firm level)
3. Establishment and implementation, by a body or bodies independent of firms, of a system for assessing firm level quality assurance (quality assurance - practice inspection level)

4. Establishment and implementation, by an appropriate body, of a system for assessing quality assurance at the practice inspection level (quality assurance - overall monitoring level)

We feel that changes made to achieve clarity should include using terminology that clearly distinguishes the levels of quality assurance, defining all key terms for inclusion in definitions paragraph 86, and avoiding inconsistent use of terminology.

Paragraph 6 – group audits

Paragraph 6 states that an IFAC member has a responsibility for quality assurance review systems in respect to its members but “only to the extent they are performing engagements in the country or countries of the IFAC member body’s domicile.” This gives rise to a significant inconsistency with ISA 600, *Special Considerations - Audits of Group Financial Statements (including the Work of Component Auditors)* under which the group auditor is responsible for the entire audit, including the work done by component auditors in foreign jurisdictions. Further, in many jurisdictions (including Canada) practice inspections of group audits encompass work done by component auditors in other jurisdictions.

In our view, paragraph 6 needs to be revised to deal with group audits in a manner consistent with relevant standards and the international scope of practice inspections common in many countries.

Paragraph 7 – overlap of quality assurance systems

Paragraph 7 focuses on a need to “ensure there is no undue overlap” between quality assurance systems. It is not clear why this point should be a requirement in the SMO since it relates primarily to the efficiency with which practice inspections are undertaken. We feel that, at a minimum, efficiency of practice inspection systems should be positioned as a clearly secondary matter, with the primary consideration being actions to help ensure that the quality assurance systems by firms have been implemented and are operating effectively (which in turn would mean that quality assurance at the engagement level is being appropriately addressed.)

Paragraph 27 -level of detail

In our view, it is not clear why paragraph 27 goes on at considerable length to describe differences in the objectives of the system when the subject of practice inspection is a firm vs. when the subject is an individual partner. The differences between the two scenarios seem quite subtle and as noted in paragraph 28, in every case both the actions of the firm and individual partners need to be taken into account.

In our view, there is no need to go into this level of detail regarding these scenarios: at most it may warrant a brief note that the approaches to practice inspection may vary, but as noted in paragraph 28, a practice inspection has to cover matters both at both the firm level and individual engagement level.

Paragraph 33 (d) and SMOs 5 and 7 - references to accounting standards

Paragraph 33 (d) requires an assessment of compliance with IFRSs or IPSASs. This is not consistent with the ISAs which deal with audits of financial statements prepared in accordance with any acceptable financial reporting framework. Further, it is not clear why paragraph 33(d) is not positioned as part of the quality assurance review team procedures in paragraphs 44 to 51.



In our view, action needs to be taken to avoid what appear to be inappropriate inconsistencies between the SMOs and relevant standards (in particular the ISAs) with respect to the acceptability of financial reporting frameworks. The position in the ISAs is that an acceptable financial reporting framework need not necessarily be, for example, IFRS or IPSASs. This has implications not only for paragraph 33(d) but also SMOs 5 and 7. In our view, it would be helpful to clarify in the SMOs how the positions taken regarding the adoption of IFRSs and IPSASs relate to the position taken in the ISAs, which IFAC members are also expected to adopt, that there is flexibility regarding what constitutes an acceptable financial reporting framework.

Paragraphs 44-51 -level detail and reason for inclusion in the SMO

In our view, it is not clear why SMO 1 should provide a list of procedures on quality assurance review team procedures at the level of detail contained in paragraphs 55 to 51. In our view, the IFAC Board should consider significantly reducing the amount of detail in these paragraphs. If this level of detailed is to be maintained, then at a minimum we feel that the rational for providing this level of detail should be set out in the SMO.

Also, paragraph 47 provides a long list of procedures that the team “may consider” performing. For clarity, it may be useful to set out in the Preface the intended purpose of non-requirement paragraphs For example, it might be noted that they are meant to serve as explanatory or application material to support the requirements. However, it is not clear that all these non-requirement paragraphs serve that purpose. Alternative courses of action conclude therefore include eliminating certain “may consider” paragraphs from the SMOs or perhaps making these paragraphs into “shall consider” paragraphs.

Paragraph 79 – encouraging relationships

Paragraph 79 encourages members to establish relationships with oversight bodies. Similar to the point noted immediately above, this is a non-requirement paragraph. Encouraging the establishment of relationships with oversight bodies is desirable. It might be useful to making this into a requirement, at a minimum a “shall consider” requirement.

We hope that these comments will be useful in finalizing proposed SMOs.

Yours very truly,

Ron Salole
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