

# IAASB CAG PAPER



**International Federation of Accountants**

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## Agenda Item **B-2**

**Committee:** IAASB Consultative Advisory Group

**Meeting Location:** Toronto

**Meeting Date:** September 11-12, 2006

### **Report Back—Materiality and Misstatements**

#### **Objectives of Agenda Item**

To provide a brief report back on the May 11-12, 2006 proposals of Representatives on the proposed “close off” versions of ISA 320 (Revised), “Materiality in Planning and Performing and Audit” and proposed ISA 450, “Evaluation of Misstatements Identified during the Audit.”

The IAASB approved the “close off” versions of the ISAs in May 2006. The IAASB concluded that re-exposure of the requirements and guidance was not necessary. Mr. Sylph confirmed that the IAASB had followed due process with regard to the project.

The IAASB considered a first draft of the proposed “clarity” versions of the ISAs in July 2006. Approval for public exposure is scheduled for October 2006.

#### **May 11-12, 2006 CAG Proposals**

Below is an extract from the minutes of the May 11-12, 2006 CAG meeting<sup>1</sup> and an indication of how the IAASB Task Force or the IAASB responded to the Representatives’ comments.

Representatives’ comments	IAASB task force/IAASB response
<b>Proposed ISA 320 (Revised)</b>	
With regard to the implicit references to management materiality in ISA 315, “Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement,” Mr. Damant was of the view that the ISAs are widely used and not everybody may be able to identify such implicit references. It therefore may be necessary to make an explicit reference somewhere in the ISAs.	After careful consideration of the related requirements and guidance in existing ISAs, the IAASB concluded that further clarification by way of conforming amendment is not necessary.
Mr. Hallqvist was of the view that the auditor should define what is material in the audit engagement letter and state that his or her audit procedures will be	Ms. Esdon responded, at the meeting, that some of the matters raised by Mr. Hallqvist are dealt with in proposed ISA 260 (Revised), “Communication with

<sup>1</sup> The minutes will be approved at the September 11-12, 2006 IAASB CAG meeting.

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### IAASB CAG Agenda (September 2006)

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Representatives' comments	IAASB task force/IAASB response
sufficient to confirm that there is no material fraud or error in the financial statements. He was also concerned about the auditor adjusting materiality when the final financial results are different from those on which materiality was originally based.	Those Charged with Governance.” Proposed ISA 320 (Revised) emphasizes that it is helpful to discuss expectations of those charged with governance and that materiality needs to be considered as the audit progresses.
<b>Proposed ISA 450</b>	
Ms. Blomme asked the Task Force to ensure that the reference to fair presentation frameworks in the definition of misstatements is aligned with the direction taken by the Special Reports Project.	<p>Paragraph 3 of the “close off” version of ISA 450 reads as follows: “When the auditor expresses an opinion on whether the financial statements give a true and fair view or are presented fairly, in all material respects, misstatements also include those adjustments of amounts, classifications, presentation, or disclosures that, in the auditor’s judgment, are necessary for the financial statements to give a true and fair view or present fairly, in all material respects.”</p> <p>The exposure draft of the proposed “clarity” version of ISA 450 will be issued before completion of the Special Reports Project. Conforming amendments will be processed to ISA 450 (Redrafted), if necessary.</p>
With regard to the suggested fourth category of misstatement (i.e., misstatements as a result of the improper application of an accounting policy that may become material in the future), Mr. Popham was of the view that this is a common problem and should at least be included as an example in the application material.	The examples of qualitative aspects that may affect the evaluation of misstatements were expanded to include the incorrect selection or application of an accounting policy that has an immaterial effect on the current period’s financial statements but is likely to have a material effect on future periods’ financial statements.

**The close off versions of ISAs 320 and 450 are available from <http://www.ifac.org/IAASB/Meeting-FileDL.php?FID=2310> and <http://www.ifac.org/IAASB/Meeting-FileDL.php?FID=2311> respectively.**