

IAASB CAG PAPER



International Federation of Accountants

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Agenda Item

C.1

Committee: IAASB Consultative Advisory Group

Meeting Location: Toronto

Meeting Date: September 4-5, 2008

**Draft Minutes of the Public Session of the Meeting of the
INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD
CONSULTATIVE ADVISORY GROUP (CAG)**

Held on March 3-4, 2008

Basel, Switzerland

PRESENT

Members

David Damant	Chair
Xinhua Ju	Asian Financial Executives Institutes
Gerald Edwards	Basel Committee on Banking Supervision (parts of the meeting)
Marc Pickeur	Basel Committee on Banking Supervision
Kristian Koktvedgaard	BUSINESSEUROPE
Rebecca Todd McEnally	CFA Institute
Elena Lobanova	Dean of the Graduate School of Financial Management, Russia
Jan Robberecht	European Commission
Federico Diomeda	European Federation of Accountants and Auditors for SMEs
George Couvois	European Financial Executives Institutes (March 3)
Hilde Blomme	Fédération des Experts Comptables Européens
Philip Johnson	Fédération des Experts Comptables Européens
Robert Roussey	Information Systems Audit and Control Association (March 3)
Bengt Hallqvist	Instituto Brasileiro de Governanca Corporativa
Sam Gutterman	International Actuarial Association
Henning Goebel	International Association of Insurance Supervisors
George White	International Bar Association
Christianna Wood	International Corporate Governance Network
Susan Koski-Grafer	International Organization of Securities Commissions
Pat Sucher	International Organization of Securities Commissions
Filip Cassel	International Organization of Supreme Audit Institutions
Rifaat Karim	Islamic Financial Services Board
Lori Cox	Institute of Internal Auditors
Hayanari Uchino	Japan Securities Dealers Association
David Morris	North American Financial Executives' Institute
Ajith Ratnayake	Sri Lanka Accounting and Auditing Standards Monitoring Board
Yoseph Asmelash	United Nations Conference on Trade and Development
John Hegarty	World Bank (March 3)
Thomas Krantz	World Federation of Exchanges

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

Observers

Tom Ray U.S. Public Company Accounting Oversight Board

By Invitation

Ben Scicluna IFAC Small and Medium Practices Committee
Richard Fleck Chairman of the Auditing Practices Board in the United Kingdom and
Chairman of the Ethics Consultative Advisory Group (March 4)

IAASB

John Kellas Chairman
Diana Hillier Member

Public Interest Oversight Board

Sir Bryan Nicholson Member

IFAC Staff

Jim Sylph Executive Director, Professional Standards
Kathleen Kerrigan IAASB Manager
Alta Prinsloo IAASB Deputy Director

APOLOGIES

Members

Conchita Manabat Asian Financial Executives Institutes
Nelson Carvalho Chairman of the Standards Advisory Council of the International
Accounting Standards Board
Vickson Ncube Eastern Central and Southern African Federation of Accountants
David Schraa Institute of International Finance
Mohini Singh Institute of International Finance
Wayne Upton International Accounting Standards Board
John Carchrae International Organization of Securities Commissions
Tomokazu Sekiguchi International Organization of Securities Commissions

Observers

Norio Igarashi Japanese Financial Services Agency

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

MARCH 3, 2008¹

Introduction (Agenda Item A)

Welcome by Chair and Others

Mr. Damant opened the meeting and welcomed those present. In particular, he welcomed Messrs. Goebel and Robberecht to their first meeting. Mr. Goebel was attending on behalf of the International Association of Insurance Supervisors and Mr. Robberecht on behalf of the European Commission. Mr. Damant noted that:

- Sir Bryan Nicholson was observing the meeting on behalf of the Public Interest Oversight Board;
- Mr. Scicluna was observing the meeting on behalf of the IFAC Small and Medium Practices Committee; and
- Mr. Fleck, a lawyer and chairman of the UK Auditing Practices Board and of the Ethics Consultative Advisory Group, would be attending part of the meeting and make a presentation on “The Challenges Facing Auditing” in the afternoon of the second day of the meeting.

Mr. Edwards, Senior Advisor on Accounting and Auditing Policy – Financial Stability Forum, welcomed the participants on behalf of the Bank for International Settlements (BIS). He indicated that Mr. Andresen, Secretary-General of the Financial Stability Forum (FSF), and Mr. Walter, Secretary-General of the Basel Committee on Banking Supervision, would be making presentations on their respective organizations during the lunches on the two days of the meeting.

Previous Minutes

The minutes were approved subject to inserting the following paragraph under Accounting Estimates, Additional Application Material:

“Mr. Uchino questioned whether the linkages between asset valuation and capital and risk were adequately covered in the ISA, and suggested that the ISA include the concept of risk management.”

It was noted that the comment was included in the *Report Back—Accounting Estimates* (Agenda Item B.1); however it was attributed to Mr. Sekiguchi. The comment was raised by Mr. Uchino.

Quality of Meeting Material

During the meeting Messrs. Damant, Krantz and Johnson and Ms. Koski-Grafer commented on the comprehensiveness and high quality of the meeting material provided to support the IAASB CAG discussions. Ms. Koski-Grafer also noted that for this meeting the volume of material was very considerable and had been difficult to run off due to the late stage at which some material was received and the fact that for some agenda items the reference papers underlying the meeting material were provided as attachments in the relevant emails, while for other agenda items only the text of the meeting material contained links to the reference papers. This inconsistency led to

¹ The minutes present the discussions in the order that they were taken. This may not be the same as that indicated on the agenda.

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

a situation where material run off by an assistant, based on the emails received, did not include important reference papers. Mr. Damant noted that the links to the reference papers in the meeting material were not presented as obvious links, and that this would be clarified for the future.

Report Back on IAASB Projects (Agenda Item B)

To NOTE how the respective IAASB Task Forces and the IAASB have considered the Representatives' comments.

Accounting Estimates (ISA 540 (Revised and Redrafted)²) – final ISA approved by the IAASB in December 2007

The Representatives had no additional comments on the report back on accounting estimates.

Written Representations (ISA 580 (Revised and Redrafted)³) – final ISA approved by the IAASB in December 2007

The Representatives had no additional comments on the report back on written representations.

Related Parties (ISA 550 (Revised and Redrafted)⁴) – final ISA to be approved by the IAASB in March 2008

The following was noted with regard to the report back on related parties:

- Mr. Damant thanked the Task Force and IAASB staff for a comprehensive report back, which clearly indicates how the Task Force and IAASB considered the comments of the Representatives at the September CAG meeting. Ms. Koski-Grafer commended the Task Force for its responses to the comments of public interest oriented respondents to the exposure draft. She hoped that the changes proposed by the Task Force will be accepted by the IAASB.
- Mr. Cassel indicated that the IAASB CAG Working Group is satisfied with how the Task Force responded to the comments of the Representatives. He noted that the working group is of the view that the proposed ISA does not have to be re-exposed.
- Ms. Koski-Grafer was of the view that the Requirements section of the final ISA should at least mention the existence of special purpose entities. Ms. Hillier indicated that special purpose entities are specifically referred to in the application material to the definition of related parties. As part of that definition, special purpose entities will be in the mind of the auditors when they comply with the requirements of the ISA. In addition, ISA 315 (Redrafted)⁵ deals with special purpose entities in the application material to the requirement for the auditor to obtain an understanding of the entity. Ms. Koski-Grafer pointed out,

² ISA 540 (Revised and Redrafted), “Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures.”

³ ISA 580 (Revised and Redrafted), “Written Representations.”

⁴ ISA 550 (Revised and Redrafted), “Related Parties.”

⁵ ISA 315 (Redrafted), “Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment.”

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

however, that special-purpose entities and structured finance vehicles have represented a special risk condition for more than 10 years and, for that reason, were worthy of being mentioned in the requirements directly. Messrs. Goebel and Roussey and Ms. Todd McEnally shared Ms. Koski-Grafer's view. Mr. Koktvedgaard, although not opposing this view, emphasized the fact that ISAs should remain principles based.

- Mr. Scicluna asked how the proposed ISA deals with entities that are under the control of a single family; a question shared by Mr. Hegarty. Ms. Hillier responded that the IAASB was of the view that the Task Force's proposal to limit the definition of "common control" to fellow subsidiaries narrowed it unnecessarily. As a result, the revised definition includes family relationships. In the context of that definition, the auditor will focus on circumstances where there is evidence of influence as result of those relationships.

Communicating Deficiencies in Internal Control (ISA 265⁶) – exposure draft of proposed ISA approved by the IAASB in December 2007

The following was noted with regard to the report back on communicating deficiencies in internal control:

- Mr. Kellas explained that the extant ISAs used the term "material weakness" for purposes of reporting internal control deficiencies to those charged with governance to provide them with information relevant to fulfilling their responsibilities. In the case of the standards of the US Public Company Accounting Oversight Board (PCAOB), the term "material weakness" is used for purposes of reporting to the public, which results in quite a high threshold. For purposes of the ISAs, a definition in line with that of the PCAOB would constrain the communication with those charged with governance (i.e., it would be at an incorrect level) while introducing a different definition for the same term may give rise to confusion. As a result, the IAASB decided not to define the term for purposes of the ISAs.
- Mr. Kellas also expanded on the response to Mr. Roussey's comment noted in the Report Back. He explained that the ISAs do not use the term "material weakness" in an operational context. As a result, the proposed deletion of the term does not give rise to unintended consequences.
- Mr. Roussey suggested that the Task Force consider developing an additional paragraph that deals with reporting of material weaknesses to the public. This could include a definition of "material weakness" that is acceptable to the European Commission and others. Further, does the existence of a material misstatement imply that there is a material weakness? Mr. Cassel emphasized the importance of the ISA in the public sector, where different frameworks for reporting deficiencies in internal control exist. He suggested that the Task Force consider providing guidance on matters the auditors may take into account when required to report publicly on material weaknesses in internal control. Mr. White suggested that the ISA provide for the auditors to communicate with management and those charge with governance the need to consider the public disclosure requirements applicable to the entity. He was of the view that the ISA is designed to address communication with management and those charged with governance; it is not designed to address reporting by the entity to the public. The issue of

⁶ ISA 265, "Communicating Deficiencies in Internal Control."

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

what the auditors can disclose publicly is not clear in ISAs, and may be difficult to address given the different reporting regimes of the entities subject to audit.

- Mr. Johnson was concerned that the lack of a definition of “material weakness” may give rise to the different European Union Member States developing different definitions, as the Statutory Audit Directive requires reporting of key matters, including material weaknesses in internal control. He was also concerned that more than one official definition, i.e., one by the IAASB and another by the PCAOB, may give rise to confusion.
- Mr. Morris noted that preparers of financial statements want consistency in financial reporting, including auditing. Matters reported to management, those charged with governance, and the public should be similar irrespective of the jurisdiction of the reporting entity. Mr. Koltvedgaard noted that the user community would also prefer consistency. Mr. Johnson, however, was of the view that inconsistency is unavoidable as the scope of an audit in accordance with ISAs is different from the scope of an audit in accordance with the standards of the PCAOB.
- Mr. Ray was of the view that a common definition of “material weakness” will be helpful. He explained that, in the US the auditor of a public company is required to conclude whether the system of internal control is effective. In conducting the audit, the auditor evaluates the severity of each deficiency in internal control to determine whether a material weakness exists. He asked how often the auditor will make such determination in the case of an audit conducted in accordance with ISAs. Mr. Johnson responded that the auditor will determine whether a deficiency in internal control is so material that it could impact the financial statements. If the case, the auditor will consider the effect on the audit and the audit opinion.
- Mr. Goebel was of the view that, in the case of regulated entities, the auditor should be required to report material weaknesses in internal control to the relevant regulators. He did not think that such reporting should depend on national law or regulation.
- Ms. Todd McEnally was concerned that users of financial statements often become aware of a material weakness in internal control only when the financial statements are materially misstated. She was of the view that deficiencies in internal control should be identified and reported before they result in material misstatement of the financial statements. Mr. Johnson was of the view that the requirement to report deficiencies in internal control to those charged with governance will make them aware of deficiencies that in time may become more serious.
- Mr. Uchino explained the difficulties experienced in implementing the Japanese equivalent of the Sarbanes-Oxley Act. He noted that there is a shortage of management and internal auditors who have sufficient knowledge of systems of internal control and, in the case of larger companies, the auditors are not permitted to assist them in this regard while there are insufficient other professionals to consult.
- Mr. Diomeda was of the view that the ISA is focused on larger entities with structured systems of internal control. He was concerned about the definition of “internal control” and the application of the requirements (in particular those relating to communication in writing) in the context of an audit of a smaller entity, which may not have a structured system of internal control and where management and those charged with governance may be the same. He suggested that further consideration be given to audits of smaller entities; in particular the costs versus the benefits.

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

- Mr. Scicluna noted that it is not clear whether communication in writing means a letter from the auditor to those charged with governance. He asked whether a copy of the minutes of a meeting between the auditor and those charged with governance, circulated to those charged with governance, would be regarded as communicating in writing. Ms. Koski-Grafer was of the view that it would.

Service Organizations (ISA 402 (Revised and Redrafted)⁷ and ISAE 3402⁸) – exposure drafts of proposed ISA and ISAE approved by the IAASB in December 2007

The following was noted with regard to the report back on service organizations, in particular proposed ISA 402 (Revised and Redrafted):

- Mr. Roussey, speaking as the IAASB CAG representative for the Working Group, believed the comments in the report back were handled well. He still questions whether the IAASB should take on a separate project about the extended enterprise – it is an important governance matter. Such a project would include consideration of the relationship between the entity and its suppliers, and how this is addressed, as well as the process and procedures that an entity follows in assessing its service organizations.
- Mr. Diomeda requested that more application and other explanatory material be added to address the needs of SMEs. He was of the view that Type A and Type B reports may not often be used in SME audits, and it would be helpful for the proposed ISA to provide examples of what the user auditor would do if a Type A or Type B is not available.
- Mr. Morris, with the support of Mr. Couvois, was of the view that the requirements of the ISA should be enhanced to provide more emphasis on the auditor's understanding of why the entity is using service organizations (for example, for tax planning or to enhance operating efficiency) prior to obtaining a Type A or Type B report.
- Ms. Blomme noted that FEE was still considering its response to the exposure draft, in particular its views on how (if at all) the ISA could be applied to the audit of shared service centers in more complex situations.
- Mr. Pickeur noted his preliminary views that the ISA could emphasize more what needs to be done when the auditor does not use a service auditor's report. He also questioned whether a firm providing pricing services would meet the definition of a service organization or whether it would be considered an expert used by management and, therefore, covered by requirements and guidance in a different ISA?. Thus, he questioned what the auditor is expected to do when the service organization could also be seen to be an expert. Mr. Gutterman raised a similar concern.
- Mr. Pickeur also noted that the Appendix contains typical common law terms that may be difficult to translate.

⁷ ISA 402 (Revised and Redrafted), "Audit Considerations Relating to an Entity Using a Third Party Service Organization."

⁸ ISAE 3402, "Assurance Reports on Controls at a Third Party Service Organization."

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

Assurance Engagements on Carbon Emissions Information – project proposal approved by the IAASB in December 2007

The following was noted with regard to the report back on assurance engagements on carbon emissions information:

- Mr. Sylph noted that the IAASB had approved the proposal at its December 2007 meeting. At that time, the IAASB recognized that the work to be undertaken in 2008 regarding the Clarity project should take priority; however, the IAASB did agree to begin working on this project and has named two co-chairs for the project – Roger Simnett, a former IAASB member and academic, and Caithlin McCabe, an IAASB member. Mr. Sylph also noted that the IAASB has heard from a number of interested parties volunteering to assist the IAASB with this project, indicating that the IAASB had struck a chord with broader based users of this information, as well as those currently preparing such assurance reports.
- It is anticipated that, in 2008, the IAASB will hold one or more public forums to test some of the issues in this area with interested parties. Information gained during these forums will be incorporated into an issues paper that would be considered by the IAASB.
- Mr. Damant agreed with the IAASB's decision to start with the area of carbon emissions information. In a very broad subject, such as sustainability, it was appropriate to focus on specific areas. He noted that there was general support for this project within the IAASB CAG.

Clarity Project (Agenda Item C)

Report Back and Update (Agenda Item C.1 and C.2)

To NOTE how the IAASB has considered the CAG Representatives' comments and to RECEIVE an update on the Clarity project.

Mr. Kellas reported on how the relevant Task Forces had responded to the comments on ISA 260 (Revised and Redrafted)⁹ and ISA 720 (Redrafted)¹⁰ raised by the Representatives at the previous meeting. The final ISAs were approved by the IAASB at its December 2007 meeting. The PIOB has confirmed that due process was followed in the development of these ISAs. The Representatives did not raise further comments.

Mr. Kellas noted that the IAASB is on track to complete the Clarity project by the end of 2008. The last exposure drafts of proposed redrafted ISAs were approved in December 2007 and it is envisaged that the final redrafted ISAs will be approved during 2008. The IAASB has made provisional plans to hold an additional meeting in November for purposes of work on the Clarity project, should it be necessary.

Mr. Johnson commented on the high volume of papers and short period that was allowed for their review. He asked whether it would be possible to submit comments after this IAASB CAG

⁹ ISA 260 (Revised and Redrafted), "Communication with Those Charged with Governance."

¹⁰ ISA 720 (Redrafted), "The Auditor's Responsibility in Relation to Other Information in Documents Containing Audited Financial Statements."

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

meeting on the ISAs to be approved at the June IAASB meeting. Mr. Kellas responded that it would be possible.

Mr. Johnson also noted that the IAASB CAG Working Group – Clarity was of the view that the role of the IAASB CAG should not be limited to a review of the individual redrafted ISAs, but that it should also include a review of the project as a whole. As a result, the working group suggested that the IAASB CAG review the effectiveness of the project and whether it has met its objectives during the 2009 meetings.

Final ISAs to be Approved by IAASB in March 2008 (Agenda Item C.3)

To DISCUSS matters highlighted by the Redrafting Task Forces or brought forward by CAG Representatives.

Mr. Kellas explained that the responses to the exposure drafts of the proposed redrafted ISAs included comments that go beyond the application of the clarity conventions. In the case of the standards that have been revised and redrafted, most of the comments were considered as part of their revision and, accordingly, no further action is intended to be taken. In the case of standards redrafted, but not revised, the comments will be taken into account in determining whether an ISA should be revised during the 2009-2011 strategic period (See Agenda Item I).

ISA 250 (REDRAFTED), “CONSIDERATION OF LAWS AND REGULATIONS IN AN AUDIT OF FINANCIAL STATEMENTS”

Mr. Kellas noted that the IAASB Steering Committee and IAASB previously had considered whether to revise extant ISA 250 and concluded that it was not necessary.

Mr. Kellas noted that certain comments referred to the fact that the ISA follows a procedural as opposed to a risk-based approach, and the effect that this has on the objectives. He explained that a procedural approach is necessary to avoid creating unreasonable expectations. That is, to what extent could the auditor be expected to look for instances of noncompliance?

However, based on the comments on the exposure draft, the Task Force was proposing to the IAASB that the objectives be revised to be more outcomes oriented.

The Representatives commented as follows:

- Mr. White and Ms. Sucher agreed with the revised objectives. Ms. Sucher was of the view that part (c) of the objective creates a reasonable expectation. (Part (c) states that the objective of the auditor is to respond appropriately to identified or suspected noncompliance with laws and regulations that has come to the auditor’s attention during the course of the audit.) Mr. Ray, however, was concerned that the phrase “that has come to the auditor’s attention during the course of the audit” implies a passive responsibility that is not be consistent with parts (a) and (b) of the objectives. Mr. Kellas explained that it is not reasonable to expect the auditor to search for noncompliance with every law and regulation. Ms. Koski-Grafer noted that the members of the IOSCO Standing Committee 1 (the auditing subcommittee) did not have an open-ended search in mind, but that they were hoping for something more than the passive responsibility implied by part (c). That is, as part of obtaining an understanding of the entity and assessing the risks of material misstatement of the financial statements, the auditor will

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

look harder in the case of laws and regulations particularly relevant to the business of the entity.

- Mr. Roussey suggested that the ISA refer to laws and regulations relevant to the industry in which the entity operates. He also suggested that the ISA provide for the auditor to enquire about the existence of claims as a result of noncompliance with laws or regulations.
- Mr. White noted that the phrases “identified or possible noncompliance” and “identified or suspected noncompliance” are used interchangeably. He suggested that the phrase “identified or suspected noncompliance” be used.
- Ms. Sucher suggested that the Task Force reconsider the use of the double negative in paragraph 11, which reads as follows: “The auditor shall obtain sufficient appropriate audit evidence that the financial statements are not materially misstated due to noncompliance with laws and regulations ...”
- Mr. White noted that an entity may not be permitted to share with the auditor correspondence with relevant licensing or regulatory authorities, as is envisaged in paragraph 12(b) of the proposed ISA.
- Mr. White was of the view that, if his comments could be addressed as part of the application of the clarity conventions, the ISA would not be an obvious candidate for revision. Ms. Sucher, however, noted that IOSCO was of the view that the ISA should be revised because of developments in financial reporting and related laws and regulations, and the growth in compliance functions.

ISA 320 (REVISED AND REDRAFTED), “MATERIALITY IN PLANNING AND PERFORMING AN AUDIT” AND ISA 450 (REVISED AND REDRAFTED), “EVALUATION OF MISSTATEMENTS IDENTIFIED DURING THE AUDIT”

Ms. Hillier briefly explained the significant comments on the exposure draft of proposed ISA 320 (Revised and Redrafted) and proposed ISA 450 (Revised and Redrafted) highlighted for consideration by the IAASB CAG. The Representatives did not raise further comments.

ISA 510 (REDRAFTED), “INITIAL AUDIT ENGAGEMENTS – OPENING BALANCES”

Ms. Hillier briefly explained the significant comments on the exposure draft of proposed ISA 510 (Redrafted). The Representatives commented as follows:

- Ms. Koski-Grafer noted that the members of the IOSCO Standing Committee 1 debated whether the changes to the extant ISA go beyond the application of the clarity conventions. She noted that the redrafted ISA defines “predecessor auditor” as “the auditor from a different audit firm, who audited the financial statements of an entity in the prior period and who has been replaced by the current auditor.” This definition is different from that in the Glossary of Terms. In addition, the Glossary of Terms explains that the term “auditor” is used to describe either the engagement partner or the audit firm. Ms. Hillier explained that the proposed change is necessary to clarify the scope of the ISA. ISA 510 (Redrafted) applies when the audit firm is new to the engagement. ISA 220 (Redrafted) applies in the case of rotation of the partner.

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

- Ms. Koski-Grafer also noted that they debated whether the terms “split opinion” and “piecemeal opinion” have different meanings. They did not understand the term “piecemeal opinion,” and were concerned that it would be difficult to translate.
- Ms. Koski-Grafer noted that the requirement in paragraph 5(a) of the ISA for the auditor to determine whether the prior period’s closing balances have been correctly brought forward to the current period or, when appropriate, have been restated is not limited to an initial audit engagement, i.e., it applies to all audits.

ISA 570 (REDRAFTED), “GOING CONCERN”

Ms. Hillier briefly explained the significant comments on the exposure draft of proposed ISA 570 (Redrafted). The Representatives commented as follows:

- Mr. Damant asked whether it was sufficient only to redraft the ISA. Ms. Hillier explained that the comments that go beyond the application of the clarity conventions relate to matters that were debated extensively during the development of the extant ISA. There were not many respondents that were of the view that those debates should be reopened.
- Mr. Diomeda noted that a small entity is often dependent on the continued support of the owner-manager. He asked whether, in the case of an audit of a small entity, the auditor assumes that this condition exists as one that may cast significant doubt on the entity’s ability to continue as a going concern. Ms. Hillier explained that it was not the intention to have an Emphasis of Matter(s) paragraph in all cases where a small entity is managed by its owner. She referred to the flow of the standard – if during the risk assessment the auditor identifies events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern, including dependence on the continued support of the owner-manager, the auditor explores the condition or event and determines whether the entity’s response is adequate or whether a significant uncertainty exist.

ISA 610 (REDRAFTED), “USING THE WORK OF INTERNAL AUDITORS”

Mr. Kellas briefly explained the significant comments on the exposure draft of proposed ISA 610 (Redrafted). The Representatives commented as follows:

- Mr. Hallqvist was of the view that the external auditors should not be permitted to use internal auditors to do work on their behalf. They may however use the reports of the internal auditors. Mr. Kellas noted that respondents to the exposure draft had diverse views on this point. Some respondents held views that were in line with that of Mr. Hallqvist, while others thought that the external auditors should consider how they could use internal auditors to reduce audit fees. However, this is a matter to be considered when the ISA is revised.
- Ms. Blomme welcomed the definition of “internal audit,” but was concerned that it is written at a level that may not assist in practice – particularly in the case of smaller entities, where it may be difficult to establish whether there is an internal audit function. She was of the view that the definition could include some of the matters described in paragraphs A2-A5 of the ISA. Mr. Kellas explained that the extant ISA does not contain a definition. In developing the definition, care was taken not to change the scope of the ISA by excluding activities that may be regarded as internal auditing. The Task Force did consider the definition developed by the

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

Institute of Internal Auditors (IIA), but found that it was developed for a different purpose and includes aspirational aspects that may not be relevant.

- Ms. Cox indicated that the IIA would like to be involved in the future revision of the ISA.

Review of Significant Comments on Clarity EDs (Agenda Item C.3)

To DISCUSS matters highlighted by the Redrafting Task Forces or brought forward by CAG Representatives.

ISA 200 (REVISED AND REDRAFTED), “OVERALL OBJECTIVE OF THE INDEPENDENT AUDITOR, AND THE CONDUCT OF AN AUDIT IN ACCORDANCE WITH INTERNATIONAL STANDARDS ON AUDITING”

Mr. Kellas introduced the topic, noting that the exposure draft of proposed ISA 200 (Revised and Redrafted) was issued in May 2007. The responses to the exposure draft will be discussed at the March 2008 IAASB meeting. The aim is to approve the proposed final ISA at the June 2008 IAASB meeting.

Overall Objectives of the Auditor

Mr. Kellas noted that the original exposure draft contained two objectives – the objective of the audit and the objective of the auditor. There was a strong view that this was confusing and that the application and other explanatory material included to reconcile the two objectives was difficult to follow. The Task Force has consequently decided to revise the description of the audit to indicate its purpose and provide an objective only for the auditor. The revised ISA therefore discusses the nature of an audit upfront, with expansion as necessary in the application and other explanatory material. Mr. Kellas said that the Task Force believes this presentation is more coherent, as it sets the context of the objective.

The Representatives commented as follows:

- Mr. Roussey expressed concern about the following statement in the revised ISA: “The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements.” He was of the view that an audit has a direct purpose (to enhance the credibility of the financial statements) and an indirect purpose (to provide the ability to users of the financial statements to determine how much credibility they want to place on the audited financial statements). The statement appears to address the latter (i.e., indirect purpose). He preferred a statement along the following lines: “An audit is designed to enhance the credibility of the financial statements and, indirectly, to allow users of the financial statements to determine the degree of confidence that they can place on the audited financial statements.” Mr. Ray supported this view. Mr. Scicluna was concerned that such a focus may give rise to questions as to whom the auditor is responsible. Ms. Koski-Grafer suggested that a more appropriate focus in an ISA would seem to be on what it is that auditors do that lends credibility to the financial statements. Mr. White supported the revised ISA as drafted. He was of the view that it avoids liability traps. Ms. Wood, however, was of the view that the main objective of the auditor is to lend credibility to the financial statements.
- Mr. Ray found it interesting that the objective of the auditor is to obtain reasonable assurance as opposed to rendering an opinion. He thought the objective should focus on forming an

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

opinion on the financial statements, and the requirements should establish the obligation to obtain reasonable assurance in order to have an appropriate basis on which to form that opinion. Mr. Kellas responded that the objective includes reference to reasonable assurance as the basis for the auditor's opinion (the forming of which is also included in the objective). Ms. Blomme was of the view that the standard could elaborate more on the meaning of reasonable assurance.

- Mr. Koktvedgaard asked why the objective of the auditor is phrased in terms of “financial statements prepared, in all material respects, ...” as opposed to “financial statements that give a true and fair view ...” Mr. Kellas responded that the ISAs address both fair presentation and compliance frameworks. The Introduction section of the revised ISA contains references that give greater prominence to a fair presentation framework. Mr. Damant was of the view that the link between the objective of the auditor and the financial reporting framework is clear and logical.
- Mr. Roussey was of the view that paragraph 5 of the revised ISA should address the risk that the auditor expresses a qualified opinion when the financial statements are not materially misstated, as well as the risk that the auditor fails to modify the opinion when the financial statements are misstated. Mr. Kellas noted that the matter is addressed later in the draft.
- Ms. Koski-Grafer noted that, in her view, the purpose of the audit is to lend credibility to the financial statements, which in turn promotes confidence in the integrity of financial reporting and supports the effective functioning of the capital markets. She was pleased to see that some changes had been made in response to IOSCO comments on the exposure draft, in particular the changes to this section, and said that she hoped that the changes made by the Task Force would be accepted by the IAASB. She also noted that she would discuss the revised ISA with the IOSCO Standing Committee 1 at its next meeting to confirm her reactions, and would advise the IAASB and IAASB CAG Chair, since there had not been time to do this before the IAASB CAG meeting.

The Auditor's Obligation in Respect of Objectives Stated in ISAs

Mr. Kellas noted that paragraph 24¹¹ in the exposure draft was intended to give effect to the authority of the objectives stated in the ISAs. In general, respondents accepted the thinking of the IAASB. One objection, however, was the use of the phrase “having complied with the requirements.” Some respondents felt that the objectives stated in the ISAs should be considered when planning the audit as well as being used as a check at the end of the audit to determine whether the auditor has achieved what he or she intended to achieve. Some respondents also seemed to think that the auditor should evaluate whether sufficient appropriate audit evidence had

¹¹ ED-ISA 200 paragraph 24 states: “To achieve the overall objective of the auditor, the auditor shall use the objectives stated in relevant ISAs to judge whether, having regard to the interrelationships amongst the ISAs and having complied with the requirements of the ISAs: (a) Sufficient appropriate audit evidence has been obtained in the context of the overall objective of the auditor; and (b) Other audit procedures need to be performed in pursuance of the objectives. The assessment of whether sufficient appropriate audit evidence has been obtained and the other audit procedures, if any, that may be necessary in the circumstances are matters of professional judgment. The proper application of the requirements of the ISAs will ordinarily provide a sufficient basis for the auditor's achievement of the objectives. However, the ISAs cannot anticipate all circumstances that may arise.”

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

been obtained and, if not, use the objectives to determine other procedures required. This ignored the planning use of objectives, and their interpretation in those ISAs that did not require evidence gathering.

Mr. Kellas noted that respondents supported the IAASB's view that there should be a requirement for the auditor to document that failure to achieve an objective as opposed to a requirement to document that each objective has been achieved. This is in line with the call to avoid unnecessary audit documentation that is often heard from SMPs and others. Ms. Koski-Grafer noted that working papers themselves serve as audit documentation. Mr. Kellas responded that this concept is embedded in ISA 230 (Redrafted).¹²

Inherent Limitations of an Audit

Mr. Kellas noted that some stakeholders, including the European Commission, were of the view that the discussion of inherent limitations should be consolidated in one place, rather than within individual ISAs. He noted that this has been done in proposed ISA 200 (Revised and Redrafted), with minimal discussion in other ISAs. Where the subject does come up elsewhere, such as in the ISAs on fraud and related parties, no new principles are involved.

Mr. Kellas noted that respondents commented on the tone of the discussion of inherent limitations. Some believed that the IAASB overplayed the role of inherent limitations and underplayed the responsibility of the auditor to obtain sufficient appropriate audit evidence. The revised drafting was intended to meet that objection.

The Representatives commented as follows:

- Mr. Damant supported a discussion of inherent limitations within the revised ISA, in particular because the public may be unaware that such limitations exist. There was clearly an expectations gap. Mr. Hallqvist did not support the discussion of inherent limitation in the ISAs. He was of the view that such limitations should not exist, because the audit committee, as agent for the owners, could devote the extra resources needed so that sufficient audit work can be performed to overcome them. Ms. Wood was of a similar view, noting that audit committees should be permitted to spend more money to ensure that the audit is designed to detect all material errors and fraud. Mr. Damant noted that it is a financial statement audit is not a full forensic audit and the challenge is how to judge in advance how much additional work would be necessary in any particular circumstance. Mr. Sylph noted that many audits are conducted in entities that do not have audit committees. In order to apply to all audits, the ISAs need to address inherent limitations. Mr. Krantz suggested that the revised ISA distinguish between public and private companies.
- Mr. Johnson believed that the content of the revised ISA is appropriate to bridge the expectations gap. He noted that FEE had done a study in the area of inherent limitations. The study inter alia found that investors expect financial statements to be audited in a reasonable period of time. Mr. Scicluna supported this view, noting that the fundamental aim of the audit was to obtain reasonable assurance.

¹² ISA 230 (Redrafted), "Audit Documentation."

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

- Although agreeing with Mr. Johnson that there are inherent limitations in the audit process and that it is appropriate to recognize them in auditing standards, Mr. Ray was concerned that there was still too much emphasis on inherent limitations in the revised ISA. He identified a few areas in the draft in which he thought the balance wasn't quite right (e.g., paragraphs A41 and A43 which deal with the legal and practical limitations on the auditor's ability to obtain audit evidence and the expectations regarding the completion of the audit in a reasonable period of time and at a reasonable cost). Mr. Pickeur and Ms. Sucher had similar concerns. Ms. Sucher noted that the term "expectations gap" may be more suitable than "inherent limitations" and expressed a preference for focusing on what an audit is and what it is not rather than describing inherent limitations. Ms. Todd McEnally acknowledged that inherent limitations exist and should be recognized, but was of the view that the language in the revised ISA continues to be defensive. She also noted that a global survey conducted by the CFA Institute indicates that users of financial statements demand more information in the auditor's report about major judgments made and concerns noted by the auditors during the audit. Mr. Pickeur noted that the discussion of inherent limitations is a significant proportion of the overall ISA and expressed concern that there is a risk that this may inadvertently diminish the perceived value of an audit.
- Mr. Kellas was of the view that the revised ISA should be able to point out the truths about inherent limitations. He noted that, although some may view the discussion of inherent limitations in the revised ISA as lengthy, it relates to all ISAs, the vast majority of whose content concerned the responsibilities of the auditor. Furthermore, the discussion also highlights what the auditor does in light of the inherent limitations. He did not believe that anyone was questioning whether inherent limitations exist, but rather how much emphasis they should receive.
- Ms. Koski-Grafer noted that IOSCO had encouraged the IAASB to have a full and clear discussion of what the audit does and does not do in ISA 200 (Revised and Redrafted), including inherent limitations, and that she was supportive of such a discussion so long as it was balanced and not too negative.

Mr. Damant concluded by saying that the IAASB should take particular note of the comments of the Representatives; not on the fact that there were inherent limitations, which was agreed, but that the text, as drafted, appeared defensive because of its length and some of the wording.

Mr. Damant asked whether the IAASB could defer the approval of the proposed final ISA to provide the IAASB CAG Member Organizations an opportunity to discuss it.

Professional Judgment

Mr. Kellas noted that respondents believed that the exercise of professional judgment should be reasonably consistent amongst auditors and the result of proper training. Some respondents were concerned, however, that the proposed description in the Exposure Draft could be interpreted to set a low threshold. He noted that the Task Force has removed the objectionable discussion in the ISA, but has retained the language that is intended to promote rigor of professional judgment. The revised ISA requires the auditor to apply professional judgment throughout the audit. This may help to limit references to professional judgment throughout the ISAs. Mr. Damant and Ms. Sucher supported the changes. Mr. Damant noted that professional judgment is a very important concept in moving towards principles rather than rules.

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

Application and Other Explanatory Material

Mr. Kellas explained that the IAASB believes that the auditor should read and understand the entire text of the ISAs. The IAASB's view is that, while it is possible for an experienced auditor to read a particular requirement and know exactly what to do, the application and other explanatory material is necessary as it explains what is meant by the requirement. The Task Force believes that the changes should dispel the notion that the application and other explanatory material is entirely optional.

The Representatives commented as follows:

- Mr. Damant was of the view that it would be dangerous for jurisdictions to adopt only the objectives and the requirements. Mr. Kellas confirmed that that was the view of the IAASB; however, the requirements and application and other explanatory material do not necessarily have to be presented in the same place. The proposed requirement specifically sets out the responsibilities of the auditor in relation to other material as a safeguard against their separation.
- Ms. Koski-Grafer supported the changes, though she suggested that paragraph A57¹³ of the revised ISA be moved to the Requirements section as she believed that this information was essential to having a proper understanding of the requirements.

ISA 500 (REDRAFTED), "CONSIDERING THE RELEVANCE AND RELIABILITY OF AUDIT EVIDENCE"

Mr. Kellas noted that extant ISA 500¹⁴ contains an overarching requirement for the auditor to obtain sufficient appropriate audit evidence. In redrafting the ISA, the IAASB was of the view that the principle of obtaining sufficient appropriate audit evidence is interrelated with the concept of reasonable assurance. As a result, this requirement was moved to proposed ISA 200 (Revised and Redrafted). Proposed ISA 500 (Redrafted) was refocused on the auditor's responsibility to design and perform audit procedures to obtain relevant and reliable audit evidence.

Respondents to the exposure draft did not support the effect of this proposal on ISA 500. They were of the view that ISA 500 (Redrafted) should cover both sufficiency and appropriateness of audit evidence, despite the repetition that may arise with proposed ISA 200 (Revised and Redrafted). As a result, the Task Force has amended the title and scope of the ISA and the objective of the auditor, and introduced a new requirement that includes consideration of the sufficiency of audit evidence. Ms. Sucher supported this view, noting that it had seemed artificial to separate the discussion of sufficiency and appropriateness in different ISAs.

¹³ Paragraph A57 of the ISA states: "In addition to objectives and requirements (expressed in the ISAs using "shall"), an ISA contains related guidance in the form of application and other explanatory material. It may also contain introductory material that provides context essential to a proper understanding of the ISA, and definitions. Accordingly, to understand the objective and to apply the requirements of an ISA properly, it is necessary for the auditor to read and understand all parts of the text of an ISA."

¹⁴ ISA 500, "Audit Evidence."

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

ISA 530 (REDRAFTED), “AUDIT SAMPLING”

Mr. Kellas explained that some respondents were of the view that the proposed ISA shows a bias towards statistical sampling, and that changes that had been made to extant ISA 530 may have inadvertently ruled out certain types of sampling. The Task Force therefore is proposing a number of changes to align the redrafted ISA with the extant ISA, while retaining clarity of the auditor’s responsibilities.

Mr. Kellas also noted that a method of sampling is often associated with the methodology of an individual audit firm, making it difficult to provide significant detail in the ISA without bias appearing to constrain the firms to particular approaches. The IAASB, however, does not believe there are issues with the use of sampling by auditors that would warrant a fundamental revision of the ISA.

The Representatives had no comments.

ISA 700 (REDRAFTED), “THE INDEPENDENT AUDITOR’S REPORT ON GENERAL PURPOSE FINANCIAL STATEMENTS”

Ms. Hillier briefly explained the significant comments on the exposure draft of proposed ISA 700 (Redrafted). The Representatives commented as follows:

Financial Reporting Frameworks Described by Reference to International Financial Reporting Standards (IFRS)

- Ms. Sucher noted that her understanding is that the responses to the proposed amendment to IAS 1¹⁵ are not positive. She also noted that the ISAs should be framework neutral, but that the relevant guidance in proposed ISA 700 (Redrafted) is based on the proposed amendment to IAS 1.
- Mr. Johnson was concerned about the implications for the auditors – he was not sure how the auditors will apply the requirement and guidance in proposed ISA 700 (Redrafted) if the reporting entity is not required to quantify the difference between the modified IFRS framework and IFRS. He also questioned how comparison amongst jurisdictions is possible without quantification of the difference. Mr. Damant also supported quantification of the difference where this might be possible, but he appreciated that such a quantitative reconciliation would frequently not be possible since it would imply a full reconciliation to the original IFRS. Nevertheless, the IASB text did not make it clear how the difference could be reported qualitatively, apart from the separate requirement that the non-application of certain IFRS would be noted.
- Ms. Todd McEnally did not think that it is necessary to quantify the difference. She cautioned against the auditor assuming the responsibility to address financial reporting deficiencies in an audit client, or being put in the position of the regulator. She believed that it is necessary for the reporting entity to provide the disclosures necessary to neutralize financial reporting deficiencies, and was hoping that others would step forward to solve the problem.

¹⁵ International Accounting Standard (IAS) 1, “Presentation of Financial Statements.”

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

- Sir Bryan noted that the IASC Foundation is concerned about jurisdictions eroding IFRS by way of carve out, and that the proposal of the International Accounting Standards Board (IASB) is an important aspect in avoiding this. The real issue, however, is whether the investor community is being misled. He agreed that this is a difficult call for the IAASB and encouraged it to give appropriate weight to the views of the various constituencies.

Consistency in the Auditor's Report

- Ms. Sucher, presenting her view rather than that of IOSCO, noted that there is more merit in having a meaningful auditor's report than having consistency in auditors' reports.
- Mr. Scicluna, however, preferred consistency in auditor's reports. He was concerned that readers may not be able to understand auditors' reports if they were inconsistent.
- Ms. Todd McEnally was of the view that certain parts of the auditor's report could be consistent, but that it would be helpful to have some flexibility to address critical concerns that the auditor may have about a particular audit.

[Discussion of the remainder of this agenda item, Agenda Item D – Project Proposal on Assurance Reports on Prospectus Information, and Agenda Item E – IAASB-National Standard Setters Meeting was postponed until the following day.]

MARCH 4, 2008

ISA 705 (REVISED AND REDRAFTED), "MODIFICATIONS TO THE OPINION IN THE INDEPENDENT AUDITOR'S REPORT"

Ms. Hillier noted that some respondents to the exposure draft were of the view that the definition of "pervasive" should include reference to matters that are fundamental to users' understanding.

The Representatives commented as follows:

- Ms. Sucher noted that IOSCO was also of the view that the definition of "pervasive" is confusing. She supported the proposed reference to "fundamental to users' understanding," which would be more outcome orientated.
- Mr. Scicluna was concerned that the requirement for auditors to include disclosures that were omitted by management in the auditor's report may be problematic in practice.

ISA 706 (REVISED AND REDRAFTED), "EMPHASIS OF MATTER PARAGRAPHS AND OTHER MATTER(S) PARAGRAPHS IN THE INDEPENDENT AUDITOR'S REPORT"

Ms. Hillier explained that proposed ISA 706 (Revised and Redrafted) allows the auditor to apply professional judgment in determining whether to include an Emphasis of Matter paragraph in the auditor's report. She noted that respondents to the exposure draft were of the view that this ISA should acknowledge the requirements for Emphasis of Matter paragraphs in other ISAs.

Ms. Koski-Grafer noted that there was some confusion among the IOSCO representatives as to how an Other Matter(s) paragraph would be used, and whether the use of such a paragraph is rare.

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

ISA 800 (REVISED AND REDRAFTED), “SPECIAL CONSIDERATIONS – AUDITS OF SPECIAL PURPOSE FINANCIAL STATEMENTS AND SPECIFIC ELEMENTS, ACCOUNTS OR ITEMS OF A FINANCIAL STATEMENT”

Ms. Hillier briefly explained the significant comments on the exposure draft of proposed ISA 800 (Revised and Redrafted). She noted that in the responses to this reporting ISA, in particular, respondents raised matters other than those related to the application of the clarity conventions.

Mr. Damant asked whether a true and fair / present fairly opinion can be expressed on a specific element, account or item of a financial statement. Ms. Hillier responded that the principle underlying ISA 800 is that it is possible if the element, account or item is prepared and presented in accordance with a fair presentation framework. She noted, however, that some respondents had questioned whether fair presentation frameworks, such as IFRS, contemplate “fair presentation” other than in the context of a complete set of financial statements, and whether a specific element, account or item prepared in accordance with the relevant requirements of such framework can achieve fair presentation.

ISA 805 (REVISED AND REDRAFTED), “ENGAGEMENTS TO REPORT ON SUMMARY FINANCIAL STATEMENTS”

Ms. Hillier briefly explained the significant comments on the exposure draft of proposed ISA 805 (Revised and Redrafted).

Ms. Blomme was concerned about the form of opinion to be expressed on summary financial statements. She was of the view that the required work effort does not support the form of opinion. Mr. Damant also questioned referring to “fair,” while Mr. Ratnayake supported the reference to “fair summary.” Ms. Blomme was of the view that the fact that the ISA provides for flexibility with regard to prescribed auditors’ reports could be made clearer.

GENERAL

Referring to the ISAs that deal with auditors’ reports, Mr. Karim was concerned that it may not be possible to reflect the finer nuances in translations of the standards. Mr. Kellas responded that the IAASB takes great care to achieve the right nuance in the English version of the standards. He did not understand why this was not also possible in the translated versions. He noted that the exposure drafts of proposed standards include a question about translation of the text of the proposed ISA. Mr. Damant was of the view that the work of the “plain language expert”¹⁶ also helps in this regard.

Assurance Reports on Prospectus Information (Agenda Item D)

To DISCUSS a project proposal on assurance reports on prospectus information.

Mr. Kellas noted that there is a demand for the IAASB to undertake this project as a result of the European Prospectus Directive, but that it would also benefit other jurisdictions that do not have

¹⁶ This expert is contracted by the IAASB to review proposed standards to ensure that they are written in plain language, i.e., the text is complete and consistent, brief and concise, and clear.

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

relevant standards. He noted that prospectuses are portable among the EU Member States and that uniformity in practice is in the public interest. He noted that a consultation document to obtain feedback may be helpful in the development process. He asked the Representatives whether the project will be useful; in particular, in a non-European environment.

The Representatives commented as follows:

- Mr. Damant noted that this project is in the interest of investors. He asked about the next steps. Mr. Kellas explained that a task force will be established if the IAASB approves the project proposal at its March 2008 meeting.
- Ms. Blomme expressed FEE's support for the project and, in particular, the proposal to prioritize work on assurance reports on pro forma financial information. She also hoped that further work could be done on assurance reports on prospective financial information. She referred to the discussion papers that FEE has issued in this area.
- Mr. Ray referred to the guidance on comfort letters that exists in the United States. Mr. Kellas indicated that it is proposed that the project does not focus on comfort letters to avoid jurisdictional issues. The focus is on the reporting by the auditor on information provided to the public, rather than communication between the auditor and an underwriter. Mr. Morris noted that, in practice, there is diversity in what is done for public and private offerings with regard to communication with underwriters.

Mr. Damant asked the Representatives to inform him or Ms. Prinsloo should they be interested in being a member of the IAASB CAG Working Group.

[Discussion of Agenda Item E – IAASB-National Standard Setters Meeting was postponed until after Mr. Fleck's presentation.]

IAASB Strategy and Work Program for 2009-2011 (Agenda Item I)

To REVIEW a summary of significant comments on the Consultation Paper, a proposed strategy and work program, and related matters.

Mr. Kellas noted that the IAASB CAG has been very helpful in developing the strategy. He introduced the matters highlighted for consideration by the Representatives.

The Representatives commented as follows:

Revision of ISAs (Redrafted, But Not Revised as Part of Clarity Project)

- Ms. Koski-Grafer noted that these ISAs should be revised over a period of time to ensure that at some point in time the IAASB has a complete set of up-to-date standards. She suggested that, in addition to ISA 720 (Redrafted), the IAASB consider revising ISA 210 (Redrafted),¹⁷ ISA 250 (Redrafted)¹⁸ and ISA 510 (Redrafted)¹⁹.

¹⁷ ISA 210 (Redrafted), "Agreeing the Terms of Audit Engagements."

¹⁸ ISA 250 (Redrafted), "Consideration of Laws and Regulations in an Audit of Financial Statements."

¹⁹ ISA 510 (Redrafted), "Initial Audit Engagements—Opening Balances."

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

- Mr. Edwards asked whether a reasonable timetable for revising these ISAs could be developed, taking account of the IAASB's other planned projects and the need to be able to respond to important emerging matters. Mr. Kellas referred him to the planned work program for 2009-2011, which includes the timetables for the revisions of ISA 610 (Redrafted)²⁰ and ISA 720 (Redrafted).

Process for Assessing the Effectiveness of New Standards

- Mr. Damant noted that the process could also be used to identify areas where translation of ISAs has led to ambiguity. Ms. Koski-Grafer supported this point.
- Ms. Koski-Grafer was of the view that there should be greater mention of working with audit oversight bodies to identify areas for improvement within the ISAs. Ms. Blomme suggested that national standard setters be involved. Mr. Kellas responded that national standard setters may assist in identifying barriers to adoption of ISAs. Ms. Koski-Grafer noted that national standard setters may be able to assist the IAASB to understand ISA "pluses."
- Mr. Koltvedgaard agreed that regulators should be involved, but stressed the need for them to promote the use judgment in the interpretation of standards, and not to look for standards that were checklists.
- Mr. Asmelash suggested that the IAASB also obtain feedback from relevant stakeholders in developing nations.

Implementation Guidance, Including Fair Value Audit Guidance

- Mr. Damant was of the view that it might be practical to chose certain areas within the whole topic of fair value audit guidance rather than to embrace the whole subject in one document. He also noted that there is a view that the IAASB should develop such guidance only if a need arise as a result of the implementation of ISA 540 (Revised and Redrafted). He did not agree with this view for two reasons. First, the matter was in itself of very considerable complexity and importance, and required special study, even though it might have been appropriate for ISA 540 (Revised and Redrafted) not to go into more detail than it did as it was a worldwide standard applicable in so many jurisdictions. A second reason for pursuing the project on fair value audit guidance was provided by recent events in the capital markets as a result of the sub-prime crisis.
- Mr. Goebel was of the view that any guidance should be developed independently from ISA 540 (Revised and Redrafted), as preparers and auditors are concerned that guidance developed prematurely may undermine the standard.
- Referring to the recent market turmoil, Mr. Edwards suggested that auditing firms take stock of their "best practice" audit procedures. These best practices should be drawn upon to enrich the IAASB's fair value audit guidance, for example, on the audit of model-based estimates. He also noted that this approach would reflect well on the accountancy profession and the related standard setters. He underlined that the suggestion was made in a positive sprit and not to suggest "deficiencies" in audits or auditing standards as these have not come to light at

²⁰ ISA 610 (Redrafted), "Using the Work of Internal Auditors."

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

this time. Mr. Gutterman supported this suggestion. Mr. Goebel also supported gathering information from auditors before concluding that guidance should be developed. Mr. Krantz suggested that the information gathered from auditors and others be published on the IAASB's website, highlighting the challenges experienced and how they have dealt with them. Mr. Johnson questioned whether this would be possible.

- Mr. Scicluna was of the view that the development of guidance for preparers may address the challenges faced by auditors. He suggested that the IAASB liaise with the IASB in this regard. Mr. Johnson, who believed that the development of guidance is not appropriate at this time, was of a similar view. He noted that additional financial reporting disclosures will assist substantially in this regard. Mr. Johnson and Ms. Sucher supported the proposal that the next step should be to gather information from auditors to determine whether guidance is in fact necessary.
- Ms. Todd McEnally cautioned against complacency. She noted that recent issues in the marketplace pertained to interest rate swaps, which are common instruments that are marked-to-market. As such, she believed that the need for guidance existed before the current environment. Mr. Damant agreed.
- Mr. Robberecht noted that the EC has drafted a communication to the European Parliament and Council that calls for cooperation between the IASB, IAASB, FSF and IOSCO.
- Mr. Uchino noted that in many cases management may not understand the type of risk that they assume in dealing with complex financial instruments. In particular, smaller institutions – such as regional banks – may not have risk management or compliance departments.
- Mr. Kellas responded that the next step is to bring the auditors together in order for the IAASB to understand the challenges they are facing. If necessary, the IAASB may consider producing, for example, an alert that does not replicate accounting guidance. He noted that audit evidence may be an area to be explored. He was of the view that the IAASB CAG discussion confirmed the approach of consultation to determine whether guidance is necessary.

Alternative Assurance Service for SMEs

- Mr. Diomeda noted that a number of jurisdictions are either raising or introducing thresholds for statutory audit exemptions. He wondered whether the IAASB's view that "an audit is an audit" may be a limitation to maintaining good quality in financial reporting by encouraging alternatives to audit or no audit at all. He suggested that the IAASB obtain feedback on how this view affects legislators in setting thresholds.
- Mr. Scicluna noted that the IFAC Small and Medium Practices Committee supports the IAASB's proposal first to revise ISRE 2400²¹ and ISRS 4410,²² and then to determine whether there is a broader need to be addressed.

²¹ International Standard on Review Engagements 2400, "Engagements to Review Financial Statements."

²² International Standard on Related Services 4410, "Engagements to Compile Financial Statements."

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

- Mr. Damant noted that, while there had been strong support for something to be done in this area at previous IAASB CAG meetings, he supported the IAASB's proposal to be aware of developments in this area while revising ISRE 2400 and ISRS 4410.

Conceptual Framework

- Mr. Johnson noted that FEE has raised this issue and that there seemed to be a demand from the oversight bodies in Europe to develop a conceptual framework. The project is on the agenda of FEE. He asked the IAASB to continue to consider embarking on a similar project. Mr. Asmelash was of the view that a conceptual framework may assist in understanding how the ISAs fit together.
- Mr. Diomeda suggested that the IAASB establish a small group to consider matters relating to a conceptual framework until such time as the IAASB has resources to develop such framework. Mr. Gutterman did not believe that the development of a conceptual framework should be a high priority. He suggested that the IAASB commission research to minimize the use of IAASB resources. Ms. Asmelash suggested that IFAC member bodies sponsor academic research in this area. Ms. Sucher expressed support for how it is positioned in the proposed strategic plan.
- Mr. Damant was of the view that work in this regard should not be undertaken until it is clear what is meant by a conceptual framework for auditing. There were several matters relevant to such a framework already covered in the IAASB pronouncements. Mr. Karim suggested that time be devoted at a future IAASB CAG meeting to understanding the logic for an auditing conceptual framework as a basis for considering IAASB CAG's view of its relative priority.
- Mr. Kellas noted that the respondents who had expressed interest were not regulators or practicing auditors. He questioned why the IAASB is being called upon to develop further conceptual thinking when it seems that the academic community is not particularly interested. He noted that any project on a conceptual framework would probably need to be outsourced and funded.
- Mr. Damant remarked that, based on the comments noted and the general reaction of the CAG, there seemed to be no noticeable demand for the immediate development of a conceptual framework and supported the IAASB's conclusions in its Strategy and Work Program.

Other

- Mr. Edwards suggested that the IAASB CAG in future discuss efforts towards global convergence based on updates from the IAASB, PCAOB and others. Mr. Kellas referred to the recognition of ISAs, or the process for developing ISAs, by the FSF, International Monetary Fund, World Bank and World Federation of Exchanges.
- Mr. Kellas noted that it would be extremely helpful to receive an official endorsement of ISAs by IOSCO. He observed that the adoption of IFRS has increased since the IOSCO endorsement in 2002. It could serve as an incentive to countries who are considering adopting ISAs by providing a reason why they should do so. Ms Koski-Grafer was of the view that it is important for the IAASB to recognize countries that have their own standards while exploring convergence, for example the United States.

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

- Mr. Krantz encouraged the IAASB CAG Member Organizations to work towards formal endorsement of ISAs or the process for developing ISAs.

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

The Challenges Facing Auditing (Agenda Item J)

Mr. Fleck presented on the challenges facing auditing. In this regard, he referred to two initiatives that had been undertaken in the United Kingdom, i.e., the development of *The Audit Quality Framework* by the UK Financial Reporting Council in February 2008, and the issue of the *Discussion Paper: The Auditor's Report: A Time for Change?* by the UK Auditing Practices Board (APB) in December 2007.

Mr. Fleck noted that the phrase “audit quality” is being used in many ways, and sometimes inappropriately. Also, the concept of audit quality is difficult to understand and assess. As a result, readers of the auditor's report have little feel for what audit quality they are getting. He was of the view that *The Audit Quality Framework*, which identifies the drivers of audit quality, should assist in this regard: (1) the culture within an audit firm; (2) the skills and personal qualities of audit partners and staff; (3) the effectiveness of the audit process; (4) the reliability and usefulness of audit reporting; and (5) factors outside the control of auditors affecting audit quality.

Mr. Fleck emphasized the importance of further debate about the auditor's report. Many, in addition to the investor community, are relying on the auditor's report. The first question is whether the auditor's opinion is what the users want; or whether there are other practical ways in which users can be provided with the information that they require. Users need information that is of value to them. The current descriptions of the responsibilities of management and the auditor in the auditor's report are seen as protecting the auditor, while users fear that they are not made aware of the key issues discussed by the auditor and the audit committee. The purpose of the Consultation Paper is to focus respondents on identified issues and encourage debate on the way forward.

Mr. Kellas noted that the future debate about the auditor's report will include discussion of who is responsible for providing what information, and the use of the auditor's report to overcome financial reporting deficiencies. Mr. Fleck was of the view that, if the auditors are aware that the directors are misleading the users of the financial statements, they have to respond; however, it is not the auditors' responsibility to provide information that investors may find useful but that the directors ought to provide.

Mr. Kellas explained that there are two reasons for including the auditor's report on the work program for 2009-2011, i.e., to consider the matters reported in the auditor's report and whether it should include other matters, and the fact that extant ISA 700 has not been adopted by some jurisdictions. Mr. Fleck noted that Europe is keen on a standard European wide report. Mr. Kellas noted that every jurisdiction, however, has its own laws and regulations. This was the reason for the two-part ISA report.

Mr. Sylph noted that the American Institute of Certified Public Accountants (AICPA) and the IAASB have commissioned research with regard to the wording of the auditor's report. The research is conducted by one researcher from New Zealand, one from the United Kingdom and two from the United States. The results of the research, the responses to the UK APB's paper and the findings of the global survey being conducted by CFA Institute will inform the debate about the auditor's report.

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

IAASB-National Standard Setters Meeting (Agenda Item E)

To REVIEW a brief report on the agenda for the annual IAASB-NSS meeting scheduled for March 27-28, 2008.

Mr. Sylph summarized the matters to be discussed with the National Standard Setters (NSS) during the annual IAASB-NSS meeting scheduled for March 27-28, 2008. The Representatives commented as follows:

- Ms. Koski-Grafer suggested that the agenda include an open question about barriers to the adoption of ISAs, including the translation of ISAs.
- Mr. Scicluna noted that the reference to Implementation Guidance is very wide and that there were differences of opinion as to whether it was a standard setter's role to be involved in its promulgation. To focus discussions it will be necessary to clarify which part of implementation is being referred to. He was of the view that possible candidate material for issue as formal implementation guidance could be identified based on the experience encountered in the actual implementation of a standard subsequent to its coming into force by posing the question whether any issues so arising in practice would have been included in the original text of the standard as application and other explanatory material had the issue been brought to light at that early drafting stage. If the matter arising from live experience in the implementation of the standard would have been so included in such standard as application or other explanatory material at the time of original drafting had it been considered at that stage, then such guidance should be deemed appropriate for its promulgation as implementation guidance at a later stage of the standard's life.
- Mr. Asmelash referred to the list of NSS. He asked whether other NSS have been invited to attend the meeting. Mr. Sylph explained that the group is limited to those NSS that can share resources with the IAASB. Over the past seven years, the group has expanded from eight to 12 members. So far, members of the group have decided to keep it fairly small. Ms. Koski-Grafer noted that, although the IAASB CAG is a larger group, its participants manage to contribute actively to the debates. It should therefore be possible to expand the group of NSS.
- Ms. Koski-Grafer also noted that IOSCO members had commented from time to time on the fact that the IAASB-NSS meetings are not open to the public and said she was glad to see that this issue was on the agenda for the IAASB-National Standard Setters meeting.

Closing

Mr. Damant noted that the next meeting is scheduled for September 4-5, 2008 in Toronto. The Spring 2009 meeting will be held in Dubai.

Mr. Damant thanked BIS, the Basel Committee on Banking Supervision and the FSF for hosting the meeting and for the presentations by their representatives. He also thanked Mr. Kellas and Ms. Hillier for their contribution to the meeting, and Mr. Sylph and his staff for their support.

Sir Bryan shared the views of others about the quality of the meeting material. He noted that it helped focus the discussion. He was impressed by the participation of the Representatives and thought that the discussions were content rich. He commented on the fact that the Representatives

IAASB CAG PAPER

IAASB CAG Agenda (September 2008)

Agenda Item C.1

Minutes – March 3-4, 2008

and other participants listened to each other's views and encouraged the group to keep up the good work.

Mr. Damant closed the meeting.