



International Federation of Accountants

545 Fifth Avenue, 14th Floor, New York, NY 10017 USA
Tel +1 (212) 286-9344 Fax +1 (212) 286-9570 www.ifac.org

Agenda Item

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Committee: IAASB Consultative Advisory Group

Meeting Location: Washington

Meeting Date: September 9-11, 2009

ISA Implementation Monitoring

Objectives of Agenda Item

To review developments to date in relation to the ISA Implementation Monitoring Project.

The IAASB will receive an update on the progress made with the Implementation Monitoring part of this project ("Phase 1") at its meeting in December 2009.

IAASB Task Force

The IAASB Task Force members are:

- Jon Grant (Task Force Chair), IAASB member
- Phil Cowperthwaite, IAASB member
- Dan Montgomery, IAASB member
- Tomokazu Sekiguchi, IAASB member
- Abudullah Yusuf, IAASB member.

Background

1. Developments to Date

1.1 In its 2009-2011 Strategy and Work Program the IAASB committed to undertake the development and implementation of a process for assessing the effectiveness of the implementation of the Clarity ISAs. The purpose of such a process is to assist the IAASB in determining whether there is any need for further refinement in those Standards in order to achieve their intended objectives.

1.2 Any such post-implementation review should be distinguished from:

| Activity | Responsibility |
|-------------------------------------------------------------------------------------------------------------------|---------------------------------|
| Monitoring national compliance for IFAC purposes | IFAC Compliance Committee |
| Evaluating the appropriateness of how audit firms integrate the ISAs into their methodology and train their staff | National audit monitoring units |
| Evaluating the appropriateness of the application of the ISAs to individual audits | National audit monitoring units |

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- 1.3 The Task Force presented an Issues Paper to the IAASB at its June 2009 meeting in Lisbon. Preliminary discussions were held with the IAASB National Auditing Standard Setters (NSS) Group in April 2009.
- 1.4 The IAASB has agreed that during 2009 and 2010 it should:
 - Actively monitor the implementation process of the Clarity ISAs, and
 - Discuss with stakeholders their views on the need for a post-implementation review and, if so, how and when such a review might be conducted.

2. PHASE ONE - Monitoring The Implementation Process (July 2009 – June 2011)

- 2.1 Audit firms in many countries will be planning to implement the Clarity ISAs in their methodologies in 2009 and 2010. This activity is likely to provide important information regarding matters such as:
 - The way that the ISAs are implemented (including the use made of the objectives and the application material),
 - Aspects of the ISAs that might be difficult to understand, and
 - Areas in which the audit firms decide to provide additional guidance material to achieve consistent application.
- 2.2 At the same time there will also be activity at a national level to embed the Clarity ISAs in national standards and translate them. This activity is likely to provide interesting information regarding matters such as:
 - The way that the ISAs are implemented (including the use made of the objectives and the application material),
 - The need for additional requirements (“pluses”) or deletions (“carve-outs”), and
 - Aspects of the ISAs that may be difficult to translate for various practical reasons, for example because the meaning of the ISA may be unclear.
- 2.3 It will be valuable to collect information while it is still fresh in peoples’ minds although it is important to do this in a way that does not give rise to expectations that the ISAs will be changed in the near future as a result. While changes to the Clarity ISAs are not expected this activity might result in:
 - Further implementation support initiatives including possible Staff Alerts (to assist later adopters benefit from the experience of early adopters),
 - A “reservoir” of information to assist future revisions to the ISAs
- 2.4 It is planned that most of the data to support monitoring the implementation process will be obtained from the completion of questionnaires. This will be supplemented as far as is practicable with direct dialogue with participants to understand the responses included in the questionnaires. A number of “focus group” meetings are planned.
- 2.5 It is planned that data will be requested from:
 - the larger firms,
 - INTOSAI

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- countries that are known to be implementing the Clarity ISAs - using their NSS and national institutes (where necessary to obtain an SMP perspective)
- In addition information will be included on the IFAC website and other entities will be invited to contribute views if they so wish.

Details of participating entities are set out in Appendix 1.

2.6 The timing of data collection will reflect when the underlying activity takes place. While responses from the larger audit firms and some countries can probably be expected by early 2010 other responses are likely to be later. Aiming to report to IAASB preliminary findings by June 2010 with a final report by June 2011 is likely to be realistic. Care will however be needed in how the findings of this work are communicated externally as the findings may be seen by some stakeholders as being overly focused on the views of the audit profession.

2.7 IAASB will be alert, throughout the information gathering process, for indications of whether urgent action may be needed. While such action is not likely to involve changes to the Clarity ISAs themselves, there may be a need for interpretation / supplementary guidance to be provided where:

- A number of different firms / countries identify the same topic as one which causes significant difficulty in the implementation process, and
- That topic is considered by the IAASB to have a significant impact on the consistent application of the Clarity ISAs.

3. PHASE TWO - Considering The Need For a Post-Implementation Review

3.1 In parallel with monitoring the implementation process it is proposed that discussions be held with stakeholders to obtain their views on the need for a post-implementation review of the Clarity ISAs and, if so, how and when such a review might be conducted.

3.2 While stakeholders are likely to be supportive of a post-implementation review being undertaken, care will need to be taken not to raise expectations regarding the extent and immanency of possible changes that would:

- Give the impression that IAASB does not believe that its existing ISAs are high quality and fit for purpose, and
- Act as a deterrent for countries and audit firms not implementing the Clarity ISAs as soon as is practicable.

Objective

3.3 Being clear as to the objective of such a post-implementation review is fundamental as this will influence the participants, process for data collection, and the timetable. It will also have a significant impact on the likely extent of IAASB's work in responding to the comments received.

3.4 There is a difference between evaluating whether the Clarity ISAs are being implemented in the way that IAASB had hoped (consistency review) and revisiting whether the Clarity ISAs need to be further enhanced to achieve audit quality (an effectiveness review).

3.5 A *consistency* review is likely to involve consideration of matters such as:

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- Consistency in the way that the ISAs are understood;
 - Consistency of the application of the ISAs in practice; and
 - Identifying difficulties in application of the ISAs.
- 3.6 Responses to comments received are likely to impact on changes to the wording of the ISAs (to achieve further clarity) and perhaps additional guidance being drafted but probably not significant changes to the requirements.
- 3.7 A distinction can be made between the consistency of the *understanding* of the ISAs or the consistency of their *application*. There are challenges in both regards. Consistency of the understanding may be closely linked to training / translation issues (which are outside of IAASB's remit) and will be difficult to measure. Consistency of application will also be difficult to measure given that the standards are principles based and allow for judgment. In practice it will be difficult to disentangle the two and it is likely that the focus will be on the consistency of application as this embraces the consistency of understanding.
- 3.8 An *effectiveness review* would involve consideration of matters such as whether:
- There are additional matters that need to be addressed in the overall ISAs package to improve audit quality;
 - The requirements of individual ISAs are sufficiently robust to achieve audit quality; and
 - The scalability of the application of the ISAs to audits of different size and complexity.
- 3.9 Responding to comments received from an effectiveness review is likely to have a much bigger impact on the requirements in the ISAs. There is a danger that encouraging such an exercise in the near future could reduce the effectiveness of the current implementation exercise.
- 3.10 While the focus of any post-implementation review is likely to be on the consistency of application, in practice comments are likely to be obtained on aspects of improvement and, in the public interest, IAASB will also need to be prepared to respond to these as well.
- 3.11 The objective of the review could be stated as:
- “To obtain information on the way that the Clarity ISAs are being applied internationally and determine whether action needs to be taken to increase the consistency of their application. If, in the course of the review, issues come to the IAASB's attention which would help to improve the standards, the IAASB will analyze them and determine whether changes to the ISAs would be appropriate in promoting audit quality in the public interest.”
- 3.12 To avoid any unreasonable expectations developing about the nature of the IAASB's review it will be necessary to emphasize that IAASB will not be reviewing individual audits to determine whether the ISAs have been properly applied as that is the role of national audit oversight functions.

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Potential participants in the review

3.13 Who the IAASB encourages to participate in the review will depend on the objective of the review. If the focus is primarily on the consistency aspect, the review should focus on obtaining information about issues arising from the direct experience of those who have experienced the ISAs first hand. These “main user groups” are likely to be:

- Audit inspection groups
- Larger firms
- Smaller firms
- Public sector auditors.

3.14 If the objective is broadened to the effectiveness of the ISAs, the views of “main user groups” will still be very important but others are also likely to have an interest including perhaps NSSs, securities regulators, preparers¹ and investors². There has never been a shortage of opinion on how standards should be changed to improve the quality of audits. Indeed views on this have already been obtained in response to the Clarity exposure drafts and, to the extent that the ISAs have been revised, embodied in the final Clarity ISAs. However not all of the ISAs have been recently revised in substance.

3.15 The “best of both worlds” might be achieved by focusing IAASB’s resources on working with the “main user groups” in a relatively structured manner and allowing others to contribute as they wish in accordance with a published IAASB timetable. To explore the extent to which the process of data collection can be structured and coordinated discussions will be held with:

- IFIAR – Independent audit inspection/oversight groups
- IFAC – Inspection/quality assurance activities of IFAC member bodies
- The Forum of Firms – Larger firms and networks of firms
- IFAC’s SMP Committee - Smaller firms
- INTOSAI - Public sector auditors
- The IAASB Consultative Advisory Group.

3.16 The extent to which it will be possible to obtain a single coordinated response from these groups will need to be discussed with them. Even if it will not be possible to get a single response, working with these groups is likely to be helpful to assist with communicating IAASB’s objective and plans and in obtaining input from their constituencies.

Responding to the results of the review

3.17 Responding to the information obtained from the review is likely to be a far greater challenge for IAASB than gathering the information.

- Information gathered will need to be analyzed,

¹ For example, preparers may have a particular interest in ISA 580 and audit committees on ISA 260 and 265.

² For example, investors may have a particular interest in ISAs 700, 705 and 706

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- Decisions will need to be taken as to whether changes to the ISAs are needed and what they are to be, and
- Changes will need to be exposed for comment.

All this will take time. In order to avoid unrealistic expectations about how quickly ISAs might be changed IAASB will need to communicate externally its strategy for further revisions to the ISAs at the same time as its plans for a post-implementation review.

- 3.18 One of the key aspects of IAASB's future strategy for further revisions to the ISAs will be whether future changes to ISAs will be made on a "rolling basis" or as another "big bang." One of the lessons of the Clarity Project has been to demonstrate the interrelationships that exist between individual ISAs. There was also significant support for releasing revised standards as a package (the "big bang" approach).
- 3.19 While a "big bang" approach for future revisions remains appealing, disadvantages include:
- Other stakeholders may take the view that it could result in unacceptable delay to changes to the standards in important areas. For example, it would seem wrong to delay changes to an important standard identified at an early stage in the process until, say 2016, by which time the whole set of ISAs had been reviewed.
 - It would delay the ISAs being updated for relatively easy issues; the International Accounting Standards Board, for example, has an annual improvement project for updating accounting standards for relatively minor issues.
- 3.20 In parallel with developing plans for any post-implementation review it is likely that IAASB will need to also establish a strategy for responding to the information collected. Any such strategy is likely to need to deal with:
- Urgent changes to the requirements;
 - Less urgent but nevertheless significant changes to the requirements (including structural changes to the ISAs); and
 - Relatively minor changes (e.g., a request to clarify an ISA in a relatively narrow area).

Timing

- 3.21 The Clarity ISAs come into effect for accounting periods commencing on or after 15 December 2009. If the IAASB were to focus the review on the second year of implementation (ie calendar 2011 audits) the earliest it could commence would be mid 2012, and data collection would not have been completed much before 31 December 2012. This allows for:
- The first two calendar years audits, being 2010 and 2011.
 - Audit inspection units will not be reviewing the audits of 2011 calendar year end audits much before June 2012.
 - It will take at least 6 months to allow participants to collect data and summarise it in a helpful manner (more time will probably be needed if the main user groups aim to prepare a single coordinated response).

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- 3.22 However, undertaking the review in 2012 may be too early to involve some important groups if, as is likely, the European Commission (EC) and other important jurisdictions such as China, Japan and the AICPA which will not have adopted the Clarity ISAs for 2010 audits. A case can be made for starting in 2013. However 2012 fits well with IAASB's strategic planning timetable (see Appendix 2).
- 3.23 An important issue to consider in relation to timing is whether any review would focus on individual ISAs or on the whole package of Clarity ISAs. This decision will impact the process to be applied and, more importantly perhaps on the timing of the overall project.

Review of individual ISAs or the package of Clarity ISAs at one time

- 3.24 One approach might be to focus on a relatively small number of standards in any one year. For example, IAASB could plan to review about 7 standards each year and therefore cover the whole population of ISAs within a 5 year period.
- 3.25 Advantages of such an approach include:
- It will be possible to spread the work (an advantage to both the “main user groups” and IAASB).
 - It would allow the IAASB to establish priorities (e.g., perhaps to focus on those Clarity ISAs that were not revised as part of the Clarity Project in the early years).
 - It would allow the review to focus on an ISA at a reasonable level of detail (this could also be a disadvantage if we are trying to avoid a proliferation of relatively minor changes).
 - It might work well with a “rolling approach” to future changes to the ISAs.
- 3.26 Disadvantages of such an approach include:
- Focusing on individual ISAs might mean that the review becomes overly detailed.
 - Focusing on individual ISAs might miss “macro” issues such as whether there are additional matters that need to be addressed in the overall ISAs package that might improve audit quality.
 - If a “big bang” approach is favoured for updating the ISAs, spreading the review process over 5 years and allowing, say, a further 3 years for IAASB to update the ISAs and follow due process for issuing them is likely to mean that 10 years would have passed since the Clarity ISAs were first issued – this may seem rather too long.
- 3.27 Public expectations are likely to be that IAASB should have completed its review and revised the ISAs within, say, 6 years of introducing new standards. If the review starts 2 ½ years after the effective dates, takes 6 months to collect data, and will require at least 2 years (and probably more time) to decide what changes to make and consult on them, there is no option but to review the whole package of Clarity ISAs.

4. Communications

- 4.1 IAASB's plans to review the Clarity ISAs are likely to be of considerable interest to stakeholders/constituencies. It will be important to obtain the views of these groups at as early a stage as possible but also in a logical sequence.

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4.2 Key stakeholders and communication plans are as follows:

| | |
|---------------------------------|------------------------------------------------------------------------------------------------------------------------------|
| IAASB National Standard Setters | Discussed the strategy - April 2009 in Vancouver Discuss results of national questionnaires in Vienna on 29/30 April 2010 |
| IAASB CAG | Discuss the strategy - 10 September 2009 in Washington |
| IFIAR | Discuss the strategy - 16 September 2009 in Singapore |
| Forum of Firms | Discuss the strategy - 8 October 2009 in New York Discuss preliminary findings – 14 April in London |
| IFAC SMP Committee | Discuss the strategy – 29/30 October 2009 in Beijing |
| World Bank | To be arranged |
| INTOSAI | To be arranged |

4.3 In order to put into effect Phase 1 the Task Force Chair has written to participating countries and firms. It is hoped that the IAASB's interest in obtaining the information requested will be self-evident.

4.4 Views on the need for and likely design of Phase 2 are likely to evolve in 2009 / 2010. Rather than formally consulting on these separately it may be beneficial to integrate these in a wider consultation of IAASB's 2012 / 14 Strategy and Work Program. Appendix 2 sets out an outline plan which demonstrates that IAASB could:

- Consult on its plans for a post implementation review alongside its consultation of its 2012-2014 strategy (mid 2010?), and
- Benefit from the findings of any post implementation review when setting its priorities for its 2015-2018 strategy (mid 2013?).

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Appendix 1

Entities Participating In The Implementation Monitoring Phase

Countries

| | Information gathering in 2009 | Information gathering in 2010 |
|--------------|-------------------------------|-------------------------------|
| Australia | X | |
| Brazil | X | |
| Canada | X | |
| China | | X |
| India | | X |
| Japan | | X |
| Netherlands | X | |
| New Zealand | X | |
| South Africa | X | |
| UK | X | |
| US (AICPA) | | X |

Firms

Information will be requested from the following firms with global methodologies by 31 December 2009:

- BDO
- Deloitte Touch Tohmatsu
- Ernst & Young
- Grant Thornton
- KPMG
- PwC

Input from other audit firms will be discussed Forum of Firms. Discussions will also be held with INTOSAI.

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Appendix 2

Review timetable in context of IAASB's 3 year planning cycle

