

# IAASB CAG PAPER



**International Federation of Accountants**

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## Agenda Item

# A.1

**Committee:** IAASB Consultative Advisory Group

**Meeting Location:** Prague

**Meeting Date:** September 12-13, 2011

**Minutes of the Joint Public Session of the Meeting of the  
INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD AND  
INTERNATIONAL ETHICAL STANDARDS BOARD FOR ACCOUNTANTS  
CONSULTATIVE ADVISORY GROUPS (CAGs)**

**Held on March 8, 2011**

**New York, USA**

**APPROVED**

### **PRESENT**

#### **Members**

Linda de Beer  
Vânia Borgerth

Marc Pickeur  
Kristian Koktvedgaard  
Matthew Waldron  
Jan Robberecht  
Federico Diomeda  
Marie Lang  
Jean-Luc Peyret  
Hilde Blomme  
Philip Johnson  
Dr. Obaid Saif Hamad Ali Al Zaabi  
Paul Koster  
Robert Roussey  
Margie Bastolla  
Wayne Upton  
Sam Gutterman  
Peter Windsor  
George White  
Bengt Hallqvist  
Koichiro Kuramochi  
Nigel James  
Filip Cassel  
Rifaat Ahmed Abdel Karim

Chairman  
Associação Brasileira de Instituições Financeiras de  
Desenvolvimento  
Basel Committee on Banking Supervision  
BUSINESSEUROPE  
CFA Institute  
European Commission  
European Federation of Accountants and Auditors for SMEs  
European Federation of Accountants and Auditors for SMEs  
European Financial Executives' Institutes  
Fédération des Experts Comptables Européens  
Fédération des Experts Comptables Européens  
Gulf States Regulatory Authorities  
Gulf States Regulatory Authorities  
Information Systems Audit and Control Association  
Institute of Internal Auditors  
International Accounting Standards Board  
International Actuarial Association  
International Association of Insurance Supervisors  
International Bar Association  
International Corporate Governance Network  
International Organization of Securities Commissions  
International Organization of Securities Commissions  
International Organization of Supreme Audit Institutions  
Islamic Financial Services Board

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## IAASB CAG Agenda (September 2011)

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Hayanari Uchino  
Gaylen Hansen  
David Morris  
Dominique Pannier  
Ajith Ratnayake  
Simon Bradbury  
Thomas Krantz

Japan Securities Dealers Association  
National Association of State Boards of Accountancy  
North American Financial Executives Institutes  
Organization for Economic Cooperation and Development  
Sri Lanka Accounting and Auditing Standards Monitoring Board  
World Bank  
World Federation of Exchanges

#### Observers

Martin Baumann\*  
Brian Bluhm

U.S. Public Company Accounting Oversight Board  
IFAC SMP Committee

#### IAASB

Prof. Arnold Schilder  
Diana Hillier  
James Gunn  
Kathleen Healy  
Brett James  
Joanne Moores  
Ken Siong  
Jessie Wong

Chairman  
Deputy Chair  
IAASB Technical Director  
IAASB Senior Technical Manager  
IAASB Technical Manager  
IAASB Senior Technical Manager  
IAASB Deputy Director  
IAASB Technical Manager

#### IESBA

Ken Dakdduk

Chair

Richard Fleck  
Jan Munro

IESBA CAG Chair  
IESBA Deputy Director

#### Public Interest Oversight Board

Michael Hafeman

#### IFAC Staff

Gary Pflugrath

Senior Technical Manager, Regulation and Public Policy

#### APOLOGIES

##### Members

Han Fang  
Conchita Manabat  
Gerald Edwards  
Elena Lobanova  
Patricia Sucher  
Frank Bollman

Asian Financial Executives' Institutes  
Asian Financial Executives' Institutes  
Financial Stability Board  
Graduate School of Financial Management  
International Organization of Securities Commissions  
International Valuation Standards Council

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\* Views expressed by PCAOB representatives represent their views and do not necessarily reflect the view of the PCAOB Board or other Board members or staff.

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Norio Igarashi  
Yoseph Asmelash

Japanese Financial Services Agency  
United Nations Conference on Trade and Development

### **Staff**

Jim Sylph

Executive Director, Professional Standards

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MARCH 8, 2011<sup>1</sup>

### Definition of Professional Accountant (Item B)

*To DISCUSS a proposed revised definition of professional accountant developed by an IFAC Task Force.*

Mr. Pflugrath introduced the paper, explaining that its objective is to stimulate debate on how the term ‘professional accountant’ might be redefined to provide a foundation for the standard setting boards and IFAC committees when identifying to whom standards are directed, to improve the applicability of the definition on a national level, and to enhance public understanding of professional accountants. He highlighted issues with the existing definition of professional accountant and summarized key elements of the proposed definition.

Ms. Hillier noted that the IAASB has been able avoid many of the concerns with the existing definition by defining in each of its standard to whom they are directed, for example by defining the term ‘auditor’ in the ISAs. Mr. Gunn noted that informal feedback to date from some IAASB members highlighted some concerns about losing the direct link to IFAC’s member body compliance program and Statements of Membership Obligations (SMOs).

Ms. Munro noted that the topic is likely of greater import for the IESBA as every requirement applies to professional accountants. Accordingly, the IESBA had formed a working group to further examine the issues. She also noted that the proposed definition broadens the scope of the term but weakens the link with SMOs, and that there are differing views amongst IESBA members on the way forward. Mr. Dakdduk was of the view that the definition should be easy, simple, understandable and operational. He noted that some IESBA members do not believe the proposed definition is an improvement due to its complexity.

Mr. Hafeman noted that the current definition has exposed some areas where the lack of a clear definition has caused problems. He noted, for example, that the current definition is not useful in deciding what types of organizations would be eligible to apply for IFAC membership. He also noted that member bodies already include a wide range of accountants: some are just auditors; some include auditors and accountants in business; some include accounting technicians. Some standards, such as education, might not be equally applicable to all “members of IFAC member bodies”. Finally, he noted that, in some countries, standards are set or the profession is overseen in ways other than by IFAC member bodies. Some standards are also relevant to parties such as accounting educators. If the standards are to be promoted for wide use, they need to be written appropriately, not just referring to IFAC member bodies.

The Representatives commented as follows:

- Messrs. Morris and Roussey questioned the objective of the proposed changes to the definition, noting that it was not clear whether the proposed definition is intended to scope in professional accountants outside public practice, such as Chief Financial Officers, as well as

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

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professionals who majored in finance and perform some accounting but do not see themselves as professional accountants. Mr. Roussey noted that there is also the question about whether preparers should be qualified in accounting, but acknowledged that this is a broader issue.

- Mr. Upton questioned whether the proposal to change the definition is to address an expectations gap concern. If this is not the case, he could not see what problem the proposal was intended to solve.
- Mr. Kuramochi suggested that reference to being a member of an IFAC member body could be incorporated into the new definition to avoid losing the benefit that that reference brings.
- Mr. Hansen supported the proposed definition, noting that broadening the definition to scope in the licensed accountants from U.S. state boards of accountancy is an improvement. He also suggested that the proposed definition should refer to “qualified through formal education” rather than “achieved through formal education.” Mr. Kocktvedgaard supported this point, noting that an examination or similar test should be included in the definition to set an appropriate hurdle.
- Mr. Uchino noted that the quality control should be further emphasized, as at the moment it only appears to come in at Level 3 of the definition.
- Mr. Fleck noted that the greater maturity of the standard-setting boards means that the IAASB and the IESBA have a wider role in the community, and that regulators can use the definition where needed to impose obligations on the people they regulate. Mr. Hegarty agreed with Mr. Fleck noting that the change in the definition shows that the boards are maturing, and that this would assist the boards in demonstrating their legitimacy when setting standards that apply to non-accountants.
- Mr. Gutterman expressed the view that the explanatory guidance on Level 1 is too complex and still appears to be circular. He noted that the words “or other regulatory mechanism” should have some further explanation to assist users in understanding the context of these words. He also noted that the term “competence” in the definition was not, in his view, the right words, and that further explanation was needed for this important point.

#### Update on European Commission Green Paper (Item C)

*To RECEIVE an update on developments in the European Union based on the October 2010 Green Paper.*

Mr. Robberecht introduced the topic, noting that the European Commission (EC) had released a Green Paper in October 2010, and had more recently released a summary of the comments received. Mr. Robberecht noted that the EC had sought to generate a debate, and that the volume of comments received from stakeholders who did not usually respond to audit consultations indicated that the desired result had been achieved. Mr. Robberecht stressed that the views he expressed were his own and not the ones of DG MARKT or the European Commission. Ms. Nathalie de Basaldúa of the EC was invited to attend also, but was an apology.

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Mr. Robberecht gave an overview of the different comments received in the areas of auditor's conflicts of interest, rotation of firms, restricting or banning of non-audit services, ownership rules for firms and limitations on the share of fees. He explained that in his view the governance and independence of auditors are crucial issues as the audit service was not only required by law, but was also relied upon by banks, counterparties and others. He also noted that network firms are global, and operate across Europe, so one of the in his view important questions related to whether there should be international or European supervision of audit firms, similar to the model used to supervise credit rating agencies.

Mr. Robberecht noted that Commissioner noted in his speech at the Conference on Auditing in Brussels in February 2011 that he was concerned about the concentration in the market for audit services, with 90% of audits of listed companies being audited by the biggest firms. He noted that, in some states the concentration may be higher than this, and there were concerns about the effect on concentration when one of the Big 4 may not offer audits in some sectors. He noted that it was of crucial importance to see how these issues affected SMEs and any administrative burdens on these entities.

Mr. Robberecht informed the CAG that the summary of the comments received showed that there was broad support for the adoption of the ISAs. However, there were differences of opinion in whether this should be a binding measure on member states - professional bodies supported binding adoption and firms, investors and public authorities supported adoption but not always via binding measures. He noted that academics supported binding standards, but warned of the risk of the US not accepting ISAs. He also noted that companies were less supportive, and that they pointed to the need to reinforce the IAASB's governance and due process.

Mr. Robberecht also updated the Representatives on other matters contained in the Green Paper, including the appointment and rotation of auditors. He stressed that the EC continued to reflect on the comments received and that no decisions had been taken yet. The next stage is a proposal which is planned for November 2011.

The Representatives comments as follows:

- Mr. Fleck noted that one of the challenges is that, across the member states, a number of these issues have already been addressed in some form; for example, audit committees are already required or permitted in some countries to be involved in the appointment of auditors. Therefore, there is a question about whether the EC is more interested in the final outcome or the process or achieving the outcome. Mr. Robberecht responded that in his view both could be considered. Regarding Mr. Fleck's example, Mr. Robberecht said that looking at the comments received on the GP, it could be for example that on the one hand the Commission would look at process by making sure that the audit committee would be independent, but could also focus on output by strengthening their role in appointing the auditor.
- Mr. Hansen noted that it was currently common for US practitioners to travel to the EC to service their clients, and asked if there was any intention to restrict this. Mr. Robberecht noted that Europe has always allowed other standards and that the EC has developed an interim process to determine if countries have equivalent auditor oversight and regulatory

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systems to the EC. Having an equivalent system means that the EC expects that the oversight of auditors in that country is of the appropriate level of quality. The equivalence process has resulted on 19 January 2011 in recognising ten countries as being equivalent, among which the US. In addition, a number of countries moving towards independent oversight were granted a transitional period. Mr. Robberecht noted that, in his view, this matter needs to be raised with the Group of 20 and Financial Stability Board to achieve global cooperation on auditor oversight.

- Mr. Hallqvist noted that the questions posed in the Green Paper were quite broad, and that it may be difficult for the EC to determine a direction given the broad range of views. Mr. Robberecht responded by noting that the EC wished to get a balanced overall response from a broad range of stakeholders, including non-auditors, and that 40% of the responses to the Green Paper came from non-auditors. He noted that, despite the broad range of stakeholders, there were nevertheless common themes in the responses.
- Mr. Baumann asked if there was a view that audit fees should from a single client be limited to a specific percentage of the total fee income of the audit firm, and if there were circumstances where this had been an issue. Mr. Robberecht noted that was only consulting whether there was a need to have such a limit but that there were suggestions from commentators of 10-30.
- Mr. Baumann noted that there appeared to be broad support from academics for a ban on the provision of non-audit services by audit firms. Mr. Robberecht agreed, but noted that there were differing views on whether this should apply to all clients or only the firm's audit clients. Mr. Baumann commented that restricting audit firms from performing other services was a significant issue.
- Mr. Ratnayake noted that auditing is carried out by professionals and that the integrity of the profession and the auditor needs to have a more significant role than profits. He commented that, if a listed company carries out an audit, profits are likely to come first. Mr. Robberecht replied that other fields such as independence deal with integrity. The issue of ownership in his view focused on growth for mid-tier firms and raising capital for big 4 in case of liability issues. Concentration of audit market should not result in a too big to fail firm and consequently in moral hazard which would also endanger audit quality.
- Mr. Koktvedgaard noted that the impact of the Eighth Directive has not undergone a full evaluation yet. Mr. Robberecht noted that legislation and its implementation would not be completed for a few years. Therefore waiting with proposals to reinforce auditing would put audit policy behind the other aspects of financial supervision that are being considered. Mr. Koktvedgaard also noted that the Green Paper made little reference to the global work of the CAGs, IFAC, IAASB and IESBA. He asked if there was an intention to understand global perspectives. Mr. Robberecht noted that the EC's membership of the CAG and status as an observer at the IAASB enabled the EC to obtain a global perspective.
- Mr. Waldron supported a ban on non-audit services. He asked how the comments will be weighted, and noted the need to educate and reach out to investors. Mr. Robberecht responded, noting that the EC do not look solely at the numbers, but also consider

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stakeholder groups to ensure that the all stakeholders are heard. Mr. Robberecht added that the EC had previously had difficulties obtaining responses from investors, companies, etc. and welcomed the response by these investors to this consultation.

- Mr. Krantz noted that Hong Kong Exchanges and Clearing is the operator of the regulated marketplace as well as a public listed company. He explained that, by Hong Kong Law and its own corporate statutes, whenever there is a problem in the marketplace it must give priority to meeting the public good requirements of its position, even at cost to its commercial side. He noted that the public interest of the exchange is its primary obligation, and that has been met time and again.
- Ms. Borgerth noted that in Brazil auditor rotation is mandatory and non-audit services are banned. She noted that this had not been easy but had been good for the Brazilian audit market, although mandatory rotation was currently suspended to facilitate IFRS adoption, but that rotation would commence again in 2011.
- Mr. Uchiro commented that a key question was the value of an audit. He noted that the summary of responses to the Green Paper mentioned that investors supported a non-binding approach, and that there was the expectations gap between investors and auditors.
- Mr. Fleck noted that, as many people understand the importance of the proposals that the EC plan to release in November, in his view, the member organizations may like to continue to follow the developments.

Prof. Schilder agreed with Mr. Robberecht's summary of the support for ISA adoption, noting that, based on his reading of most of the comment letters, he had found only ten or so comment letters that were against ISA adoption. Prof. Schilder also noted that the message that ISAs are scalable to the size and complexity of the entity has been received. He said that many practitioners from France and Germany had acknowledged this and wanted the EC to take this into account in the adoption process. He also noted that, while many know that the IAASB is not dominated by the accounting profession, this message still needed to be reinforced.

Mr. Robberecht thanked the Representatives for their comments.