



## AUASB International Update

This Update summarises the significant news of the IAASB, other national auditing standards-setting bodies and professional organisations for the period 4 September 2012 to 21 November 2012.

### International Auditing and Assurance Standards Board (IAASB)

#### 1. Auditor Reporting

The IAASB received a report back on discussions held at its North American and European Auditor Reporting Roundtables and during other outreach activities to date. Broadly speaking, strong support has been expressed for the IAASB's efforts. Nevertheless, there is diversity of views in terms of both the value and impediments of suggested improvements to the auditor's report and how they could be operationalized in practice.

The IAASB also discussed on a preliminary basis the scope and potential structure of the ISAs to be revised as part of its Auditor Reporting project.

The IAASB will consider responses received on its June 2012 Invitation to Comment, as well as feedback from its Asia Pacific Roundtable and other outreach activities, at its December 2012 meeting.

#### 2. Assurance needs of smaller entities – revised standard on Review Engagements

In support of its commitment to explore standards for services that meet the unique needs of small- and medium-sized entities (SMEs), the IAASB released International Standard on Review Engagements (ISRE) 2400 (Revised), *Engagements to Review Historical Financial Statements*. ISRE 2400 (Revised) follows the release earlier in 2012 of International Standard on Related Services (ISRS) 4410 (Revised), *Compilation Engagements*, a standard also addressing services of particular relevance to SMEs.

Review engagements are of particular relevance for entities that are not required, or do not elect, to have an audit, but wish to enhance the credibility of, and confidence in, their unaudited financial statements among their users through practitioner involvement. The practitioner's report when a review engagement has been conducted in accordance with ISRE 2400 (Revised) describes whether anything has come to the practitioner's attention that causes the practitioner to believe the financial statements are not prepared, in all material respects, in accordance with the applicable financial reporting framework. A review is a limited assurance engagement, however, and the procedures performed are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing. Accordingly, the practitioner's review engagement report does not express an audit opinion on the financial statements.

The revised standard is effective for reviews of financial statements for periods ending on or after December 31, 2013.

#### 3. IAASB proposes standard enhancing auditor responsibilities for disclosures beyond the financial statements

The IAASB released for public comment proposed International Standard on Auditing (ISA) 720 (Revised), *The Auditor's Responsibilities Relating to Other Information in Documents Containing or Accompanying Audited Financial Statements and the Auditor's Report Thereon*.

The proposed standard clarifies and enhances the scope and focus of auditor efforts on “other information”—that is, information included in documents containing or accompanying the entity’s audited financial statements. The proposals recognise that significant changes in financial reporting have occurred over the last two decades regarding the information issued in connection with an entity’s financial statements and the manner in which it is shared with users.

Under the proposed standard, the auditor is required to read and consider the other information in light of the understanding of the entity and its environment the auditor has acquired during the course of the audit, and to respond appropriately when the auditor identifies a potential material inconsistency in the other information or a material misstatement in the audited financial statements. The proposed ISA 720 expands the documents considered as “other information,” and clarifies and enhances the nature of the auditor’s responsibilities with respect to reading and considering other information. In addition, it includes guidance to assist auditors in determining the nature and extent of their work in considering the other information.

Proposed ISA 720 (Revised) also introduces reporting obligations to explain in the auditor’s report the nature of the auditor’s responsibilities relating to the other information and the findings from the auditor’s work, to enhance transparency. The proposals do not extend the scope of the auditor’s opinion on the financial statements to cover the other information.

## **CANADA**

### **The Canadian Institute Of Chartered Accountants (CICA)**

#### **1. Mandatory comprehensive audit firm review – a sound alternative to mandatory audit firm rotation?**

There are different alternatives being considered to address perceptions that auditors are overly familiar with their clients – mandatory comprehensive audit firm review (MCAR) seems to be gaining some attention. The appointment of the auditor is nominally made by shareholders of a company, but is usually proposed by the audit committee and, in practice, is highly influenced by the recommendations of management. This creates an inherent conflict in the independent and objective role of the auditor – auditors are expected to critically examine financial statements prepared by the very people who are involved in their appointment (often referred to as a familiarity threat).

To address this conflict, Canada adopted the international model which is a principles-based approach. An auditor must identify and evaluate threats to independence and apply safeguards to reduce threats to an acceptable level, or refuse to accept the audit engagement. In the aftermath of the 2008 economic crisis, several international bodies are challenging this approach and proposing changes to revise auditor independence requirements.

In its response to the Public Company Accounting Oversight Board (PCAOB) Concept Release on auditor independence and audit firm rotation, the Canadian Public Accountability Board (CPAB) suggested the PCAOB explore MCAR as an alternative to mandatory audit firm rotation. MCAR puts an onus on the audit committee to evaluate the effectiveness of the auditor on a periodic basis, and to report the results of this evaluation to the shareholders. In this report, the audit committee would, among other things, justify why the existing auditor has been reappointed or why a new auditor has been appointed.

## 2. Concerns about emerging market issuers examined through an audit quality lens

In a recent post *Audit Quality: In the Eye of the Beholder?*, reference was made to efforts by the International Auditing and Assurance Standards Board (IAASB) to develop an international audit quality framework. A recent regulatory review of EMIs by the Ontario Securities Commission (OSC), Staff Notice 51-719: Emerging Markets Issuer Review, can be used to demonstrate the merits of such a framework.

The purpose of the OSC's review was to assess the quality and adequacy of selected EMI disclosure and corporate governance practices, as well as the adequacy of the roles played by auditors, underwriters and the exchanges, to identify any broad policy issues and entity-specific concerns. The OSC defined an EMI as one where mind and management, and principal operations, of an entity are largely outside of Canada, in regions such as Asia, Africa, South America and Eastern Europe.

In performing its review, the OSC examined the performance of senior management, the board of directors, audit committees, auditors and others in providing credible public disclosures about an EMI. It resulted in recommendations for performance improvements by all concerned.

Many of the EMI recommendations made by the OSC can be re-formulated in the context of the IAASB's three aspects of audit quality. For example, the OSC recommended improvements to audit performance (inputs) and governance processes (contextual factors). The OSC did not make specific recommendations for improving auditor communications (outputs), however it is quite possible that one of the results of the OSC review will be that management, the audit committee and the auditor enhance their communications about emerging market issues. The IAASB framework could therefore be a useful tool in identifying how audit quality could be enhanced for EMI audits. Using such a tool has the benefit of ensuring the analysis is complete and in understanding how different recommendations interrelate to enhance audit quality.

### FRANCE

#### **Compagnie Nationale Des Commissaires Aux Comptes (CNCC)**

There have been no new recent developments.

### GERMANY

#### **Institut der Wirtschaftsprüfer (IDW)**

The IDW commented on the following:

1. IAASB's Concept Paper "*Improving the Auditor's Report*"
2. IESBA's Exposure Draft "*Proposed Change to the Definition of 'Those Charged with Governance'*"

### NEW ZEALAND

#### **1. Professional and ethical standards**

The NZAuASB considered the responses received on ED 2012-6 Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Providers* and Withdrawal of Professional and Ethical Standard 2 *Independence in Assurance Engagements* and ED 2012-7 & 8 *Structural*

*Change to PES 3 Quality Control Proposed.* Nine submissions were received, consisting of submissions from auditing firms, NZICA, CPA Australia and the Office of the Auditor-General. The NZAuASB appreciates and thanks all respondents for the high quality feedback and for the submissions received.

The NZAuASB noted that respondents were generally supportive of the approach proposed in the exposure drafts. The NZAuASB intends to publish a Basis of Conclusions when finalising the revised professional and ethical standards that will set out the rationale for the NZAuASB's conclusions on all the comments received. The NZAuASB is on track to finalise the revised professional and ethical standards in December 2012.

## **2. Assurance on a Greenhouse Gas Statement**

The NZAuASB approved for release a new assurance standard, International Standard on Assurance Engagements (New Zealand) Assurance Engagements on Greenhouse Gas Statements (ISAE (NZ) 3410).

The standard conforms to the equivalent international standard, and is therefore consistent with the NZAuASB's strategy of maintaining convergence with the body of equivalent international auditing and assurance standards issued by the IAASB. The NZAuASB did not identify any compelling reason to modify the requirements in the equivalent international standard for application in New Zealand.

ISAE (NZ) 3410 will be effective for assurance reports covering periods ending on or after 30 September, 2013.

## **3. Project to adopt ISRE 2400 (Revised): Engagements to Review Historical Financial Statements**

At its August meeting, the NZAuASB approved a project plan to adopt the international review standard ISRE 2400 (Revised). The NZAuASB notes that the scope of ISRE 2400 only covers reviews to be performed by an assurance practitioner who is not the auditor of an entity and therefore there is a need in New Zealand to also prepare or adopt an additional standard to effectively cover the situation where review engagements are undertaken by the auditor of a client.

The NZAuASB considered two options in this regard, that is, whether to adopt the international standard ISRE 2410: *Review of Interim Financial Information Performed by the Independent Auditor of the Entity* or the equivalent Australian standard ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity*.

The NZAuASB noted that ISRE 2410 is an older IAASB standard that is inconsistent with the current clarity format for international standards. In contrast, the NZAuASB noted that ASRE 2410 is more recent and up to date, is in the clarity format but certain requirements differ from those contained in the equivalent international standard. After careful consideration, the NZAuASB proposes to adopt, but adapt for application in New Zealand, ASRE 2410. The NZAuASB proposes to apply its policy and strategy on convergence with international standards and harmonisation with the Australian standards in the development of an equivalent standard for application in New Zealand.

## **4. Convergence and Trans-Tasman Harmonisation of Standards**

The NZAuASB further considered the project on convergence with international standards and harmonisation with the Australian standards. In particular, the Board discussed the impact of changes made to the terms "management" and "those charged with governance" from the equivalent ISAs for application in New Zealand.

The most pervasive changes to the ISAs (NZ) has been to include a requirement to consider “those charged with governance” in addition to “management” or to replace “management” with “those charged with governance”, where applicable. These amendments were made in order to clearly reflect the respective statutory responsibilities in New Zealand of “those charged with governance” and “management”.

The NZAuASB reached agreement on proposed changes to more closely align the ISAs (NZ) with the equivalent international and Australian standards and to enhance the clarity of expectations in respect of the current statutory responsibilities of “those charged with governance”. An exposure draft on the proposed changes will be issued in due course.

## **5. Project on Auditor Reporting**

The IAASB issued an Invitation to Comment, *Improving the Auditor’s Report* in June 2012, for comment by 8 October 2012.

Members of the NZAuASB and XRB staff met with key stakeholders and interest groups during March and April 2012 and again during September to consider the IAASB proposals. The NZAuASB has consulted widely with key stakeholders, including CEOs, Directors, Chairs of Audit Committees, Accounting and Auditing firms and financial analysts. These discussions have provided the NZAuASB with a broad range of views and opinions and were persuasive in the development of the NZAuASB’s final submission to the IAASB.

The NZAuASB also had the opportunity to discuss the IAASB’s proposals with Professor Arnold Schilder, Chair of the IAASB, and James Gunn, IAASB Technical Director during their visit to New Zealand on 5 October 2012.

The IAASB is intending to issue the exposure draft(s) on proposed changes to the Auditor’s Report for public comment in 2013, and final standard(s) late 2014.

## **SOUTH AFRICA**

### **Independent Regulatory Board for Auditors (IRBA)**

#### **1. Assurance Engagements on Broad-Based Black Economic Empowerment (B-BBEE) Verification**

The IRBA released the South African Standard on Assurance Engagements (SASAE) 3502 Assurance Engagements on Broad-Based Black Economic Empowerment (B-BBEE) Verification (SASAE 3502), approved by the IRBA Board for issue on 1 November 2012, as the authoritative standard to be applied by all B-BBEE approved registered auditors when providing limited assurance on B-BBEE Verification Certificates in accordance with the Broad-Based Black Economic Empowerment (B-BBEE) Codes of Good Practice (the "Codes of Good Practice") issued by the Department of Trade and Industry ("DTI"). SASAE 3502 is also to be applied by all registered auditors when providing Certificates to Exempt Micro Enterprises (EMEs).

SASAE 3502 is a subject specific assurance standard based on the principles in the International Framework for Assurance Engagements (the Framework) and those in the International Standard on Assurance Engagements (ISAE) 3000 Assurance Engagements other than Audits or Reviews of Historical Financial Information (ISAE 3000), the overarching standard for subject-specific assurance engagements, where no separate ISAE exists. The Framework and ISAE 3000 are part of the International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements issued by the International Audit and Assurance Standards Board (the IAASB),

that are prescribed for use by registered auditors in the conduct of audit, review and other assurance engagements.

## **UNITED KINGDOM**

### **Financial Reporting Council (FRC)**

#### **1. FRC and ICAS commission review of auditor's competencies**

The FRC and The Institute of Chartered Accountants of Scotland (ICAS) are to commission jointly a major project that will investigate the competencies and professional skills of auditors. It will consider what they are responsible for today and how this might change in the future. The project is being commissioned as a contribution towards restoring market confidence through improving audit quality and re-building trust in the audit profession.

The project will also explore the mix of attributes, competencies, professional skills and qualities that need to be combined in an audit team in order for it to perform a high quality public interest audit in a modern and complex global business environment. It will consider questions such as whether or not there is a need to reconsider the staffing model for the audit of complex businesses to incorporate, for example, individuals with relevant business or technical experience within the audit team, and associated training implications.

The year-long study will be running concurrently with the implementation of measures that have been taken and that are being considered by, amongst others, the FRC, the Government, the European Commission and the International Auditing and Assurance Standards Board to address the value of audit and to reform the audit market. The study will have regard to the implications of these measures and proposals for the skills and competencies of the auditor that will in future be necessary to deliver high quality statutory audits and to help restore confidence in audited financial statements, in particular those of banks, insurers and large listed companies. The report will consider whether a fundamental reassessment of the auditor's skills and competencies is required to create an audit team that can repair confidence and meet the challenges of a changing landscape.

#### **2. FRC consults on updated guidance for the audit of financial instruments**

The FRC has recently issued a consultation on the proposed update of the guidance to auditors on the audit of financial instruments; an update to Practice Note 23 (Revised).

The proposed update reflects both the clarified International Standards on Auditing (ISAs) (UK and Ireland) and updated guidance issued by the International Auditing and Assurance Standards Board (IAASB) in its International Auditing Practice Note (IAPN) 1000, *Special Considerations in Auditing Financial Instruments*.

The FRC has supplemented IAPN 1000 with guidance that is currently set out in Practice Note 23 (Revised) that is still believed relevant and with a small amount of new guidance in relation to matters not covered in either IAPN 1000 or Practice Note 23 (Revised).

The consultation period closes on 4 January 2013.

#### **3. FRC issues revised auditing standards to enhance communications to audit committees and auditor reporting**

The FRC has, following consultation, recently issued revised International Standards on Auditing (ISAs) (UK and Ireland):

260 Communication with those charged with governance

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*This document contains preliminary views and/or staff recommendations to be considered at a meeting of the AUASB, and does not necessarily reflect the final decisions of the AUASB. No responsibility is taken for the results of actions or omissions to act on the basis of reliance on any information contained in this document (including any attachments), or for any errors or omissions in it.*

700 The auditor's report on financial statements (Revised)

705 Modifications to the opinion in the independent auditor's report

706 Emphasis of matter paragraphs and other matter paragraphs in the independent auditor's report

720A The auditor's responsibilities relating to other information in documents containing audited financial statements

The revised standards are effective for audits of financial statements for periods commencing on or after 1 October 2012.

The revisions primarily give effect to proposals in *Effective Company Stewardship: Next Steps* published by the FRC in September 2011 and support changes to the UK Corporate Governance Code and Guidance for Audit Committees that have also been issued by the FRC today. The changes in the standards are mainly directed at:

- Enhancing auditor communications by requiring the auditor to communicate to the audit committee information that the auditor believes the audit committee will need to understand the significant professional judgments made in the audit;
- Extending auditor reporting by requiring the auditor to report, by exception, if the board's statement that the annual report is fair, balanced and understandable is inconsistent with the knowledge acquired by the auditor in the course of performing the audit, or if the matters disclosed in the report from the audit committee do not appropriately address matters communicated by the auditor to the committee.

Revisions to the auditor reporting standards have also been made to enable those standards to be used by auditors in the Republic of Ireland; and also more fully align the requirements of ISAs (UK and Ireland) 705 and 706 with those of ISA (UK and Ireland) 700.

## **UNITED STATES**

### **American Institute of Certified Public Accountants (AICPA)**

There have been no new recent developments.

### **Public Company Accounting Oversight Board (PCAOB)**

#### **1. Public meeting on auditor independence and audit firm rotation in Houston**

The PCAOB hosted its third public meeting on ways to enhance auditor independence, objectivity, and professional scepticism, including through mandatory rotation, or term limits, for audit firms. The meeting was held on 18 October 2012. The Board issued a concept release on 16 August 2012 that invited commenters to discuss measures that might meaningfully enhance auditor independence, objectivity and professional scepticism. The release included a number of questions related to mandatory audit firm term limits, such as whether the PCAOB should consider a firm rotation requirement for audit tenures of more than 10 years, or for the largest issuer audits only.

For a copy of the concept release, refer to:

<http://pcaobus.org/Rules/Rulemaking/Pages/Docket037.aspx>