

IFAC  
Mr. John Kellas  
Chairman of IAASB  
545 Fifth Avenue  
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New York N.Y. 10017

January 20, 2005

Dear Mr. Kellas,

We appreciate this opportunity to comment on the Exposure Draft (ED) “*Proposed Policy Statement, ‘Clarifying Professional Requirements in International Standards issued by the IAASB’*” and on the Consultation Paper (CP) “*Improving the Clarity and Structure of IAASB Standards and Related Considerations for Practice Statements*”.

We are strongly supportive of IAASB’s overall objective to serve the public interest by setting high quality international auditing standards, and continually improving those standards over time, and believe the proposed Policy Statement and Consultation Paper, taken together, are a significant contribution towards establishing the means of achieving that objective.

We especially see them as an important factor in ensuring that the standards are understandable by those who perform audits, are clear and are capable of consistent application.

As noted in the Consultation Paper, the challenge for IAASB is to issue high quality auditing standards that, among other things, meet the three following objectives:

- They are recognized by the various regulators around the world;
- They are accepted by the profession at the international and national levels;
- They are applicable to and are applied in practice by all auditors for all audits, regardless of the size and structure of their firm or of the entity audited.

Successfully balancing these objectives is a significant challenge. To better understand this challenge we identified three major issues with respect to the clarity of auditing standards:

- Definition of the terms to describe requirements and guidance

- Principles by which the board determines requirements including the level of their specificity
- The organization of requirements and guidance

We agree with the Board's proposal to define requirements and presumptive requirements and discontinue the use of the present tense. Because the Board did not address the issue of how to determine the requirements, we do not believe that the ED and CP provide a basis for resolving the continuing issues about the number and specificity of requirements. We provide some thoughts on the matter below. Some of our member firms believe that restructuring is essential. Others do not believe it is necessary or urgent. Nevertheless, we support option B provided that the requirements are sufficiently specific to meet the principles we propose below.

The Board must address the three issues mentioned above substantively and timely to retain credibility as a standard setter. Accordingly, the Board needs to demonstrate action rather than entirely relegate the issues to lengthy study. Actions to address clarity issues must also engage the user community constructively to agree on the level of specificity of requirements. To accomplish this we propose the following actions:

1. Agree on the definition of terms as described in the ED by December 2005. In so doing, the Board will be taking decisive and substantive action on a timely basis to promote convergence and to clarify what is required in the existing literature. The question of whether the requirements are sufficient or overly detailed in the existing literature is a different question that should be addressed prospectively.
2. Seek a dialog with regulators, investors and appropriate parties concerning the level of detail of the requirements and the principles on which the board decides what the requirements are and their level of specificity. The obvious forums for discussions are the Consultative Advisory Group (CAG) and the national standard setter's forum. If the various parties are willing to make a good faith effort to achieve a satisfactory compromise, the resulting prize of a single set of internationally recognized, high quality auditing standards, realistically capable of being implemented by audit practitioners around the globe, would be well worth that effort. We will be pleased to contribute in this debate.
3. Agree on principles by which the Board will determine what requirements are, their level of detail and whether they are absolute or presumptive by December 2005. Our thoughts are:

Requirements should:

- Describe an audit in sufficient detail to provide a framework for understanding the objectives of the audit and appropriate responses by the auditor to those objectives,

- Be necessary to performing an effective audit,
- Promote a reasonable degree of consistency in performance, and
- Be capable of reasonable measurement of performance.

Absolute requirements generally should be applied to higher level descriptions of principle. Presumptive requirements are better suited to more detailed descriptions of procedures or considerations because all circumstances cannot be foreseen.

Implementation of changes all at once is not possible because of the length of time it would take to revamp all the existing standards. Accordingly we recommend

- Apply the definitions of requirements to existing standards as of January 1, 2006
- Apply the principles for determination of the requirements and the new structure of standards to exposure drafts issued beginning January 1, 2006
- Update all the existing standards as of January 1, 2006 over a 5 year cycle.

This approach combines immediate action to promote understanding of the requirements with an orderly approach to resolving the use of the present tense in the existing standards.

\* \* \*

We have structured our response in two parts. Firstly, to address the Exposure Draft questions in Appendix 1, secondly, to express our views on the necessity to improve the clarity and structure of ISAs in Appendix 2.

We appreciate the opportunity to comment, and would be pleased to discuss these issues with you further. If you have any questions or would like to discuss these issues further, please contact P. Nicholas Fraser at (212) 492-4118.

Very truly yours,

/s/ Deloitte Touche Tohmatsu

## Appendix 1 - Response to the Exposure Draft

### **Equal Authority**

#### **1. Do respondents agree with the view of the IAASB, or would a statement of ‘equal authority’ assist in clarifying the responsibilities of the professional accountant?**

We support the view of the IAASB that the use of the term “equal authority” would not further enhance the effect of the intended changes and moreover that the meaning of the term is subject to interpretation, with the risk of having the opposite effect.

### **Categories of Professional Requirements**

#### **2. Do respondents agree with the proposed categories of professional requirements and the related obligations they would impose on professional accountants?**

Provided that the “fundamental principles underlying an ISA audit” are clearly distinguished from individual standards, and that the “shall” requirements are only used when relating to such principles universally applicable whatever the circumstances, we think that the proposed categories of professional requirements and the related obligations are acceptable.

#### **3. Do respondents believe that the proposals will improve the quality and consistency of audits?**

As modified by our recommendations we believe the quality and consistency of audits will be facilitated by the new definitions of requirements. We believe the resolution of the present tense should take place as part of a plan to revise standards over a 5 year period using principles for determining the specificity of requirements determined by the board as suggested in our recommendations.

#### **4. Do respondents agree with the proposed requirement for the professional accountant, when departing from a presumptive requirement, to document why the professional accountant decided to depart, and how the alternative procedure(s) performed in the circumstances were sufficient to achieve the objectives of the presumptive requirement?**

Yes; to be implemented as we recommended as part of adopting the proposed definitions and applying them to the existing standards. We see no substantive reason not to apply the proposed definition of presumptive requirements “should” to the existing usages of “should” in the basic principles and essential procedures in the existing standards. In and of itself this would clarify that the use of the present tense does not establish a presumptive requirement. We are not aware that “shall” or “must” are used in the existing standards in the context of establishing performance obligations for the auditor.

**5. Do respondents agree with the applicability of the proposed documentation requirement to departures from existing International Standards before they are revised?**

Yes; to be implemented as we recommended as part of adopting the proposed definitions and applying them to the existing standards.

**6. Will the proposed terms ‘shall’ and ‘should’ result in translation difficulties? The IAASB had considered the word ‘must’ as an alternative to ‘shall’ – would this alternative resolve identified translation difficulties?**

Yes. The use in the English language of different moods for the modal “shall” (the indicative vs. the conditional) permits to distinguish the respective strength of the requirements. However, translation of “should” by the conditional mood may in certain other languages such as French weaken the strength of the presumptive requirements. Although clearer in English, use of the word “must” instead of “shall” is not likely to resolve the translation problem with respect to “should”.

**7. Does the anticipated increase in the number of bold type professional requirements that may arise by adopting the proposals raise concern over the specificity and level at which professional requirements are set?**

As described in our recommendations we do not believe the issue of the specificity and number of requirements will be resolved by the proposal. The IAASB should determine the principles for determining the level of specificity of requirements.

**8. Do respondents agree with the decision of the IAASB to retain the bold type convention?**

In the existing structure of the standards the bold type convention continues to make sense for the purpose of improving readability. As standards are revised using the new structure the bold type convention would no longer be necessary to improve readability.

**Implementation of the Proposals**

**9. Do respondents agree that the IAASB should apply the proposals on a prospective basis?**

We agree that the proposals should apply on a prospective basis as described in our recommendations.

## Appendix 2 - Response to the Consultation Paper

### **1. Has the length and style of these standards aided or impaired their understandability and clarity?**

We have divergent views on this point within our member firms.

Some believe that recent ISAs have moved away from the previous widely-accepted principles basis (repeatedly confirmed by the IAASB), to lengthy, detailed, repetitive, complex rules, inspired by highly regulatory environments applicable to public interest entities. This has impaired the overall understandability of the standards. Moreover this trend has clearly called into question the applicability and relevance of the standards to small and medium size entities. The recently issued standards such as those dealing with fraud or the audit risk model illustrate the concern.

Others believe that the length and style of the recent ISAs are appropriate to the issues faced by the profession and that they are quite understandable and clear. They believe that the objections to length and style really are objections to the number and specificity of requirements.

### **2. If there is concern over the length of the standards, please also explain what is viewed as being problematic – the amount of explanatory guidance provided, the scope of matters addressed or other aspects of the standards. How do respondents consider such matters be resolved?**

There are two fundamental issues about the length of the standards:

- The level of detail and specificity of the requirements
- The amount of explanatory guidance and its level of detail

With respect to the level of detail and specificity of the requirements different cultures have significantly different views. This is why agreeing upon the principles for the determination of the requirements is essential. Our recommendations included some thoughts on these principles. We believe the level of specificity and detail exemplified in the reworked ISA 315 is acceptable.

With respect to the amount and level of detail of explanatory guidance, the restructuring should help address concerns but it is important for the requirements to have sufficient context to understand them.

Some people question the need for greater specificity and, therefore, numbers of requirements for audits of smaller entities. When requirements clearly are necessary for listed entities only, the standards should reflect that.

In addition the legislation in certain countries provides legal backing to the standards, by incorporating them into national law. The more explanatory text is inserted in the ISAs which are not by nature suitable for inclusion in a legal instrument, the more difficult it will be to converge national and international standards.

**3. Has the degree of detail provided in the standards aided or hindered their adoption or implementation?**

As indicated in the Wong report, the detail and complexity of recent standards has caused implementation difficulties in some jurisdictions. However the IAASB should not sacrifice what is needed to meet the objectives of high quality standards because their implementation is difficult. It should be no surprise that substantive change is difficult.

**4. Are there other options for improvement in standards that should be considered by the IAASB?**

See our recommendations. In addition, establishing clear linkages between the different levels and cross-references from one ISA to another instead of having each ISA “retell the entire story” will reduce repetition.

**5. Do respondents believe that the IAASB should continue with its present style of ISAs or is there a need for ISAs to be restructured?**

Some of our member firms believe that restructuring is essential. Others do not believe it is necessary or urgent. We do have a consensus view that the ambiguity of the use of the present tense must be eliminated. We have a consensus view that restructuring using option B is acceptable provided that appropriate principles for the determination of requirements are adopted. We believe the example of the reworked ISA 315 is acceptable.

**6 If ISAs are to be restructured, which option should be pursued and why? Are there other options that the IAASB should consider, particularly in helping with the ability for auditors of both large and small- and medium-sized entities to implement ISAs?**

We support option B because, while permitting a clear distinction between the professional requirements and the “application material” by locating them in two distinct sections, it centralizes in one single document the requirements and the relevant explanatory material supporting proper application in specific circumstances (complex environments, small entities, etc.) in a comprehensive manner.

We believe, moreover, that there would be a serious risk of relevant and important text in the application material not being considered by auditors if the two were separated. National standard-setters should not be allowed to present one without the other, or to make any changes to the application material in the course of the translation process that could weaken their substance.

**7. Notwithstanding the decisions of the IAASB regarding the proposed Policy Statement, in the event there is strong support for the restructuring of ISAs, do respondents agree that any such restructuring should be applied on a prospective basis? Or should restructuring be applied prospectively, but on a priority basis first**

**to a limited number of ISAs that have attracted concerns about their length and complexity, namely the IAASB’s recently issued audit risk and fraud ISAs?**

Although a big-bang approach is desirable in a perfect world, time considerations make it impossible.

As suggested earlier we believe the standards should all be revised over a 5 year period beginning as soon as the principles for the determination of requirements and the structure are agreed. Some of our member firms believe the oldest standards should be revised first because the newer ones have undergone recent consideration and identification of requirements and therefore have less ambiguity with respect to the use of the present tense. Other member firms prefer the approach of addressing the Risk Assessment and Fraud standards early because they form the underpinning of many other standards. We believe there are merits to both and can accept either approach.

**8. Do respondents believe that identifying “fundamental principles underlying an ISA audit” would aid in communicating the principles that underlie the professional requirements in ISAs and ultimately help drive the auditor’s professional judgement?**

We believe that identifying the “fundamental principles underlying an ISA audit” is a prerequisite to communicating the professional requirements and will:

- enhance the distinction of “shall”s from “should”s,
- provide criteria for the justification of departures from professional requirements,
- set a frame of reference for developing new standards.

**9. Should the establishment of such principles be considered a high, medium or low priority of the IAASB for the immediate future?**

Since the entire restructuring process needs to flow from the identification of the “fundamental principles underlying an ISA audit” the establishment of such principles should be considered a high priority.

**10. Do respondents consider the proposed fundamental principles to be complete and appropriate, and do respondents believe the method by which they have been derived to be appropriate?**

The proposed fundamental principles appear appropriate.

**11. Do respondents believe that the fundamental principles should be expanded to serve as a basis for all assurance engagements?**

We believe that audit should be given priority. In light of the difficulties encountered in establishing the International Framework for Assurance Engagements and the complexity

of the matter, we feel that expanding fundamental principles to serve as a basis for all assurance engagements would inappropriately complicate and delay their establishment.

**12. Do respondents agree with the proposed authority to be afforded the fundamental principles?**

We do agree.

**13. Do respondents believe the present description of the authority of Practice Statements to be clear and understandable? If so, do respondents agree with the authority that is afforded them? If not, what should be the authority of Practice Statements?**

We do as long as it relates to present IAPs or IAPs remaining after the restructuring under option B.

Should option A of the restructuring (which we do not support) be adopted, then the description would have to be amended to include “explanatory guidance to standards”, “industry considerations”, “public sector matters”, and “emerging issues”. Their current authority is similar to that afforded to the explanatory guidance contained in current ISAs and would not need to change. On the other hand, language codification changes (i.e. deletion of “should”s, use of the present tense) would have to be considered as well as reclassifying into ISAs any material that represents essential procedures.

**14. Given the existing authority of Practice Statements and their use in providing additional guidance to International Standards, should the IAASB change the style in which the Practice Statements are written? To the extent they are derived from professional requirements contained in an International Standard, should Practice Statements enunciate professional requirements?**

We think that the move towards restructuring involves a “top down” approach. Since the philosophy of IAPs is then to provide explanatory and interpretative material, they should not, in the name of consistency with the “top down” approach, enunciate additional professional requirements.

**15. Taking account of the options identified above, what future role should the IAASB consider for Practice Statements? Are there other options that the IAASB should consider?**

In light of the “top down” approach mentioned above, assuming option A is adopted; IAPs that are not closely related to any specific ISA should no longer exist and should instead be moved to training material (not issued by the standard-setting body). Similarly under option B, existing IAPs should be either (1) reclassified under “essential procedures” and “application material” sections or (2) simply withdrawn.