

INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD

ANNUAL REPORT 2005



The Drive for Clarity and Convergence



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## THE INTERNATIONAL AUDITING AND ASSURANCE STANDARDS BOARD

The International Auditing and Assurance Standards Board (IAASB) is a standard-setting body designated by, and operating under the auspices of, the International Federation of Accountants (IFAC), and subject to the oversight of the international Public Interest Oversight Board (PIOB) for the accountancy profession.

The objective of the IAASB is to serve the public interest by setting, independently and under its own authority, high quality standards dealing with auditing, review, other assurance, quality control, and related services, and by facilitating the convergence of national and international standards. This objective contributes to enhancing the quality and uniformity of practice throughout the world and strengthening public confidence in financial reporting.

The IAASB consists of a full-time Chairman and 17 volunteer members from around the world. It comprises practitioners in public practice with significant experience in the field of auditing and other assurance services, as well as individuals who are not in public practice (“public mem-

bers”). Members are appointed by the IFAC Board based on recommendations from the IFAC Nominating Committee. Member appointments are subject to the approval of the PIOB. At present, the IAASB meets five to six times a year.

The IAASB is supported financially by IFAC, which itself is funded by membership dues from more than 160 accountancy bodies based in 120 countries, and by contributions from the Forum of Firms. The Forum of Firms is an organization of public accounting firms that share the objective of promoting consistently high standards of financial reporting and auditing worldwide in the interests of the public and users of the profession’s services. Funding includes staff costs, the costs of the Chairman and the travel costs of the public members of the IAASB, as well as a contribution towards the travel costs of the other members. The IAASB is a component of the overall IFAC reporting entity and, accordingly, its financial results are included within the audited financial statements of IFAC. These financial statements are published as part of IFAC’s annual report, which is available on [www.ifac.org](http://www.ifac.org).



*Back row (standing), left to right: Josef Ferlings, Bodo Richardt, Rogério Gollo, Will Rainey, Roger Simnett, Ian McPhee, Gérard Trémolière, John Fogarty, Sukanta Dutt. Front row (seated), left to right: Philip Ashton, Craig Crawford, Mowafak Al Yafi, Denise Esdon (Deputy Chair), John Kellas (Chairman), Gen Ikegami, Roberto Tizzano, Jan Bo Hansen. Not pictured: Inga-Britt Ahlenius.*





## REPORT OF THE IAASB CHAIRMAN

I am pleased to present the IAASB's annual report for 2005. It has been a year of much activity and significant progress. One of the fundamental objectives of the IAASB as an international standard setter is global convergence to IAASB Standards. Making sure that the Standards we set are of high quality is our top priority; without this, convergence would be an idle dream.



John Kellas, Chairman

I wish to focus on two aspects of our drive for quality and convergence. First, we have tackled the immediate concerns regarding the clarity and perceived complexity of our Standards – concerns raised by certain regulators, among others, and by the Wong Report.<sup>1</sup> Secondly, we have devoted considerable effort to ensuring that we meet the needs of our stakeholders and earn their acceptance of, and respect for, our Standards. I believe that we have made substantial progress towards these objectives. This report highlights our achievements for the year and reflects on the challenges ahead.

### THE DRIVE FOR CLARITY OF IAASB STANDARDS

As a prerequisite for global convergence, international standards should be clear, understandable, and capable of implementation throughout the world. As I reported last year, the IAASB undertook a review of its drafting conventions in 2003 to identify ways to improve the clarity of its Standards and the consistency of their application (the Clarity project). The impetus for this project came primarily from regulators, who suggested that the way our Standards were drafted gave rise to ambiguity regarding the level of obligation placed on auditors and other professional accountants. This led us to consider more generally how to make our Standards clearer, and at the same time deal with the issues raised by the regulators.

### *Clarity Exposure Draft and Consultation Paper*

In September 2004, we issued an exposure draft (ED), Proposed Policy Statement, *Clarifying Professional Requirements in International Standards Issued by the IAASB* (Clarity ED), and a Consultation Paper, *Improving the Clarity and Structure of IAASB Standards and Related Considerations for Practice Statements* (Clarity Consultation Paper).<sup>2</sup> The Clarity ED dealt with the language used to describe the professional accountant's responsibilities and contained, in particular, a proposal to discontinue the use of the present tense to describe actions by the professional accountant. In the Clarity Consultation Paper, we consulted on other aspects of the Standards that could affect their clarity, including their understandability, how they are structured, and their applicability to audits of large entities and of small- and medium-sized entities (SMEs).

The success of all our projects is heavily dependent on constructive comment on our proposals, and we are pleased that so many different stakeholders take an interest in our work, and in this project in particular. We received responses from a wide range of stakeholders, including regulators, oversight bodies, national standard setters, public accounting firms, professional accountancy organizations, and individuals. Many of the responses confirmed that our current Standards are of high quality and provide a sound basis for high quality assurance engagements. But there was clear support for the project, although there was a wide range of views and recommendations on how to improve the clarity of the Standards. We therefore agreed on a proposal to take the project forward, while trying to meet the needs of the widest practicable range of stakeholders.

### *The Clarity Proposal*

The improvements we have built into the Clarity proposal broadly comprise:

- Setting an objective for the professional accountant in respect of each Standard;

<sup>1</sup> The Wong Report, *Challenges and Successes in Implementing International Standards: Achieving Convergence to IFRSs and ISAs*, issued by IFAC in September 2004 and written by former IFAC Board member Peter Wong, can be accessed on IFAC's website at [www.ifac.org](http://www.ifac.org).

<sup>2</sup> These documents, which include background to the consultation, are available on the IAASB website at [www.iaasb.org](http://www.iaasb.org).

- Clarifying the obligations imposed on professional accountants by the requirements of the Standards, using revised language;
- Eliminating any ambiguity about whether the use of the present tense in current Standards imposed any obligation on the professional accountant; and
- Improving the overall readability and understandability of the Standards through structural and drafting improvements, including clarifying the application material in the Standards.

I believe that these improvements will make the Standards clearer (leading to more consistent application), promote their adoption, and facilitate international convergence. We have taken great care to ensure that the changes will not result in any weakening of the Standards.

#### ***The Consultative Forum***

To determine whether the proposal was likely to be acceptable and worthwhile, we presented it to an invited forum in July 2005. The members of the forum included representatives of regulators, national auditing standard setters, oversight authorities, firms (including representatives of small- and medium-sized practices), professional organizations, and INTOSAI<sup>3</sup>. Although this was no substitute for the subsequent open consultation, I was pleased that the proposal, as a whole, was accepted by a significant majority of participants as a reasonable solution to varying international needs. We felt able to press ahead with confidence.

#### ***Implementation***

Taking into account all the advice given to us, we have agreed on new drafting conventions for our Standards and an aggressive timetable to redraft as many Standards as practicable in the shortest possible time, without compromising due process. We are focusing initially on our auditing Standards (ISAs), as opposed to the other international standards,

reflecting the public interest in audits.

As a first output of this implementation plan, we issued four exposure drafts<sup>4</sup> prepared under the new drafting conventions in October 2005. We shall consider the need to refine these drafting conventions when we review comments on their application to these exposure drafts. The Technical Director's report contains further details on the drafting conventions and the implementation plan.

We believe that our proposals appropriately and comprehensively respond to the issue of the clarity of our Standards. They also respond in a timely manner to many of the findings of the Wong Report, which identified the length and complexity of international Standards as major challenges to convergence. Our significant progress on this project, however, represents only one part of our response to the challenge of international convergence. We have also actively pursued other initiatives during the year to promote global acceptance of IAASB Standards.

### **TOWARDS GLOBAL ACCEPTANCE OF IAASB STANDARDS**

It is fundamental to acceptance of our Standards that they be developed through a comprehensive due process that all our stakeholders recognize and accept. Equally important is building strong relationships with stakeholders through which we can develop appropriate communication and enhance mutual understanding. Our initiatives during the year towards these aspects of achieving global acceptance are highlighted below.

#### **Working with the PIOB**

In February 2005, international regulators and related organizations, comprising the International Organization of Securities Commissions (IOSCO), the Basel Committee on Banking Supervision, the International Association of Insurance Supervisors, the World Bank, and the Financial Stability

<sup>3</sup> The International Organization of Supreme Audit Institutions (INTOSAI) has as a goal the development of Guidelines for Financial Audit that will provide its members with practical guidance on the application of INTOSAI auditing standards to financial audits of public sector entities. INTOSAI has resolved that these Guidelines should, as far as possible, draw upon ISAs.

<sup>4</sup> An explanatory memorandum, a Basis for Conclusions document, and a proposed implementation timetable accompanied the exposure drafts.



Forum, formally announced the establishment of the Public Interest Oversight Board (PIOB). I am pleased to note that, pending final assessment of the IFAC reforms, the European Commission (EC) has recently nominated two senior observers to PIOB meetings. The PIOB oversees the public interest activities of IFAC, including the IAASB's standard-setting work. The formation of the PIOB is the result of a collaborative effort between the international financial regulatory community and IFAC, to ensure that IFAC and its standard-setting boards act in the public interest when issuing auditing and other standards.

I welcome this important development. I am confident that under the chairmanship of Prof. Stavros Thomadakis, supported by a distinguished membership, the PIOB's independent oversight will enhance the public credibility of our standard-setting activities. Our discussions with the PIOB during the year included assisting them to understand our due process and working procedures and briefing them on the Clarity project and our current agenda. PIOB members also started observing our meetings and those of the IAASB Consultative Advisory Group (CAG). I have already felt the benefit of the PIOB's oversight and have no doubt that our relationship with the PIOB will bring us considerable advantages.

### Enhanced Due Process for Standard Setting

During the year, we finalized enhancements to our due process and working procedures to make our activities even more transparent. The key enhancements, which build on an already effective and transparent process, include:

- Extending the comment period on exposure drafts from 90 days to 120 days (to allow greater time for translation and domestic consultation by national standard setters).
- Further explaining how we decide whether to re-expose a proposed pronouncement.

- Increasing transparency regarding how projects are identified and approved.
- More completely explaining our views on the main issues in the explanatory memorandum accompanying each exposure draft.
- Issuing a staff document, a Basis for Conclusions, with each final Standard, explaining how we have dealt with respondents' comments on an exposure draft.

We discussed with the PIOB the revised due process, which is consistent, and was developed concurrently, with the proposed due processes for other IFAC Public Interest Activity Committees.<sup>5</sup> The PIOB approved the due process and working procedures in September 2005.

### Achieving Closer Consultation With Our Stakeholders

We maintained contact with a broad range of stakeholders during the year in our efforts to understand their needs. By holding Board meetings in different parts of the world, IAASB members have the opportunity to meet and hear the views of standard setters and others from a range of jurisdictions.

#### REGULATORS

##### *European Commission (EC)*

This is a significant time of change for auditing regulation in Europe. In this respect, the European Union's (EU's) recent finalization of the revised Eighth Company Law Directive is a significant and welcome development for the IAASB. The revised Directive is expected to be effective early in 2006, when translation into the official languages of the EU is completed. EU Member States then have two years to implement the Directive. The Directive specifies that international standards on auditing will be used for all audits in all Member States, and the EC has indicated that it is considering the endorsement of ISAs as those international standards. No target date has been set but the EC has begun discuss-

<sup>5</sup> The due process and working procedures document can be accessed on the IAASB's website at [www.iaasb.org](http://www.iaasb.org). The Public Interest Activity Committees are the International Auditing and Assurance Standards Board, the International Accounting Education Standards Board, the International Ethics Standards Board for Accountants and the Compliance Advisory Panel.

ing the possibility of adoption of the Standards with oversight authorities. We shall continue to monitor progress on the mechanism and timetable for the EC's endorsement of ISAs.

The EC has accepted our invitation to send an observer, with speaking rights, to IAASB meetings to join our other observers from the U.S. Public Company Accounting Oversight Board (PCAOB) and Japanese Financial Services Agency (FSA).

#### ***International Organization of Securities Commissions***

We met representatives of IOSCO's Standing Committee No. 1 and Auditing Subcommittee to provide updates on the IAASB's activities. Our discussions with IOSCO centered mainly on developments arising from the Clarity project and the proposed enhancements to our due process, in light of their regulatory importance. We continue to discuss with IOSCO the possibility of their formally endorsing ISAs, for example, for use on cross-border listings.

#### ***Basel Committee on Banking Supervision***

We continue to benefit from the Basel Committee's close involvement with auditing standard setting, particularly through its participation on the IAASB CAG and its commitment of resources to respond to our exposure drafts.

During the year, the seminars for the Financial Stability Institute allowed us to broaden awareness of IAASB developments, through presenting updates on our activities and agenda to an international audience.

#### **STANDARD SETTERS**

##### ***U.S. Public Company Accounting Oversight Board***

Our observer status at meetings of the PCAOB's Standing Advisory Group (SAG) allows us to keep in touch with U.S. standard setting and related developments. In this respect, I attended the PCAOB SAG meetings during the year, which enabled us to provide the PCAOB with an international view on a number of topics on its agenda. We are also pleased to welcome PCAOB representatives as observers at our board meetings.

##### ***National Auditing Standard Setters (NSSs)***

The IAASB hosted its fifth meeting of the most active NSSs in February 2005, attended by representatives from eleven countries<sup>6</sup>. The meeting enabled us to obtain the views of the NSSs on various topics of direct relevance to our work, including the meaning of and how to achieve international convergence, the clarity of IAASB Standards, developments pertaining to reporting on internal control, performance measures for standard setters, and the need to explore a conceptual framework for assurance engagements. This close liaison with NSSs, though informal, is an essential contribution towards convergence.

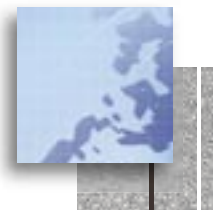
Two NSSs continue to contribute directly to our standard-setting work through their participation on three joint projects, namely: the audit of accounting estimates and audit materiality (UK Auditing Practices Board), and communication with those charged with governance (Australian Auditing and Assurance Standards Board). The experience from these joint projects will help us to refine how we continue to work with standard setters in the future.

It is heartening to note the extent of the NSSs' commitment to convergence. For example, I visited New Zea-



<sup>6</sup> The eleven countries represented were Australia, Canada, France, Germany, India, Japan, the Netherlands, New Zealand, South Africa, the United Kingdom, and the United States.





land and South Africa towards the end of the year; both countries are among those that have taken policy decisions to adopt ISAs, and I was interested to learn how they have implemented these decisions. To date, more than 70 countries around the world have adopted, or announced a policy intention to adopt, ISAs.

#### ***European National Auditing Standard Setters***

IAASB representatives regularly attend the meetings of the EU national auditing standard setters hosted by the Fédération des Experts Comptables Européens (FEE). Considering that the EU is examining the possibility of adopting ISAs, which are already followed in a number of Member States, the views of European standard setters are of particular importance to us. It is also helpful for us to understand how some significant standard setters are attempting to deal with problems that may be more widely relevant.

#### ***Chinese Auditing Standards Board (CASB)***

During the year, China established the policy of converging its national auditing standards with the ISAs. It also reformed its standards system and planned a schedule for international convergence. As part of this process, China has recently issued 17 exposure drafts, with another five expected to be issued soon. The Chinese Ministry of Finance and the CASB believe that these, together with the 26 existing effective standards, will lead to a body of Chinese auditing standards that will cater to the development of the Chinese economy and respond to the demand for international convergence. I applaud the enormous progress that China is making towards convergence. Such great progress and efforts serve as a model for developing countries and countries with economies in transition.

Representatives of the CASB and the IAASB met to discuss the progress being made towards convergence. I was pleased to be able to sign a joint statement with the Vice-Minister of China's Ministry of Finance (who is also Chairman of the CASB) to record that meeting and to recognize China's efforts in this direction.<sup>7</sup>

#### ***International Organization of Supreme Audit Institutions (INTOSAI)***

We have further developed our relationship with INTOSAI's Professional Standards Committee to ensure that ISAs provide an appropriate basis for INTOSAI's Guidelines for Financial Audit. We have observer status on the INTOSAI Professional Standards Committee. Five representatives of INTOSAI currently actively participate on IAASB projects. We welcome their technical contributions.

#### **IAASB CONSULTATIVE ADVISORY GROUP**<sup>8</sup>

I believe that the CAG has been reinvigorated by having an independent chairman, who is a respected investment professional who has worked hard to ensure that CAG's input directly relates to our agenda and who, as CAG Chairman, is an observer with speaking rights at IAASB meetings. CAG meetings were held in June and November 2005, during which we sought and obtained its advice on a number of our projects. There was specific debate on the applicability of ISAs in the SME and developing nations arenas. CAG members suggested that the development of implementation guidance would help to alleviate the concerns of small and medium practitioners and developing nations about the applicability of ISAs to their circumstances. The CAG's suggestion has provided encouragement to the IFAC Small and Medium Practices (SMP) Committee, which has been considering the need to develop such implementation guidance.

#### **OUR CHALLENGES AHEAD**

Our highest priority for 2006 is to take the necessary actions to implement the improvements from the Clarity project as soon as practicable. I know that this project is of key importance to many of our stakeholders. Given the developments I have mentioned, taking those actions is particularly relevant to the EC's adoption of ISAs for statutory audits in the EU. The Clarity Consultation Paper asks for views on our timetable. I fully expect that responses will indicate a desire for us to take the project forward even faster than proposed. The

<sup>7</sup> The joint IAASB-CASB statement can be viewed on the IFAC website at [www.ifac.org/Downloads/Joint\\_Statement\\_December\\_2005.pdf](http://www.ifac.org/Downloads/Joint_Statement_December_2005.pdf).

<sup>8</sup> Further information on the activities of the CAG is provided in the report of the CAG Chairman on pages 21-22.

IAASB will consider all options for accelerating the project. We have already arranged an extra meeting during 2006 to help us to make the progress we need.

We recognize that contributing to public confidence in the audit of financial statements is fundamental to our role. Our agenda over the past few years has reflected this and much has been achieved. We shall continue this focus, but it is right to acknowledge that the answer is not solely in our hands. Regulators have also done much, as have professional bodies and auditors themselves. In setting our agenda, however, we shall address the challenge of appropriately balancing the need to develop and update our ISAs and the need to develop standards and guidance on other emerging topics.

There is no shortage of potential topics to look at. The IAASB will continue to monitor these topics and respond appropriately to significant identified needs. Projects recently begun, or about to begin, reflect important trends – for example, the use of experts (important in the context of fair value accounting, for example) and the audit approach to the use of service organizations (in response to the more widespread use of outsourcing in recent years). Matters we are monitoring include the use of XBRL; reporting on sustainability information; internal control developments; and reporting requirements in prospectuses under recent European Directives. Our priorities will be established by their perceived importance in protecting the public interest.

### IAASB MEMBERSHIP

Eight members of the board came to the end of their appointed terms on December 31. Three of these were eligible and willing to be reappointed. In particular, I should like to express my appreciation for the contribution of the five retiring IAASB members: Mowafak Al Yafi (Lebanon), Philip Ashton (United Kingdom), Rogério Gollo (Brazil), Gen Ikegami (Japan) and Roger Simnett (Australia).

I welcome the following new appointments or re-appointments to the IAASB, which the PIOB has endorsed, from January 1, 2006, for terms ranging from one to three years:

#### ***Nominated by IFAC Member Bodies***

- Philip Cowperthwaite, *Canada*;

- Marcel Pheijffer, *The Netherlands*;
- Makoto Shinohara, *Japan*; and
- Gérard Trémolière, *France* (re-appointed).

#### ***Nominated by IFAC Transnational Auditors Committee***

- Denise Esdon, *Ernst & Young* (re-appointed); and
- Diana Hillier, *PricewaterhouseCoopers*.

#### ***Public Members***

- Ian McPhee, *Australia* (re-appointed); and
- David Swanney, *United Kingdom*.

Membership of the IAASB represents a substantial commitment, usually at least 500-600 hours a year. I am grateful to all IAASB members who made the IAASB a clear priority among their competing responsibilities.

### ACKNOWLEDGEMENTS

The success of the IAASB depends upon many others. I should like to recognize the contributions of the technical advisors supporting the IAASB members, the external experts participating on various IAASB task forces, and national standard setters and their representatives and staff working on joint projects. I should also like to thank the U.S. PCAOB and the Japanese FSA for their positive contributions as observers. It is also appropriate to recognize the significant support, encouragement and advice we have received from the PIOB, the IAASB CAG, the IFAC Board and the IFAC Transnational Auditors Committee, regulators, national standard setters and others, for which the IAASB is grateful. Last but not least, I wish to record my appreciation of the IAASB Technical Director and his staff for their dedication, support and commitment to the IAASB's work and objectives.

Thank you for taking the time to read about our work. I very much welcome your comments.



John Kellas  
Chairman

## KEY FEATURES OF THE IAASB'S DUE PROCESS AND WORKING PROCEDURES

The IAASB's due process and working procedures include:

### I. TRANSPARENCY

- IAASB meetings are open to the public.
- Free access to the agenda papers of each meeting is provided on the IAASB website in advance of the meeting.
- Highlights of each meeting and updated project summaries are posted to the IAASB website after the meeting. Audio recordings of the meeting are also made publicly available on the website after the meeting.
- Each exposure draft is accompanied by an explanatory memorandum that highlights the objective(s) and significant proposals of the proposed pronouncement and explains the IAASB's views on the main issues addressed.
- Exposure drafts and final pronouncements are available for download free-of-charge on the IAASB website.
- Comment letters received on exposure drafts are posted to the IAASB website after the end of the exposure period.

### II. CONSULTATION

#### *Agenda-Setting and Work Program*

- The IAASB obtains the PIOB's input into its agenda and work program. The PIOB can request the IAASB to add issues to its work program.
- The IAASB consults the CAG, national standard setters and others on its agenda and project priorities.

#### *Development of Proposed International Pronouncements*

- A proposal to start a new project is prepared based on research and appropriate consultation within the IAASB and with the CAG, with consideration given to the costs and benefits of the proposed project.
- The IAASB considers whether to hold a public forum or to issue a consultation paper in order to solicit views on a matter under consideration. The IAASB also considers the appropriateness of conducting a field test of the application of a proposed new Standard.
- Exposure drafts are made available for public comment, ordinarily for a period of 120 days.

### III. RESPONSIVENESS TO THE INPUT RECEIVED

- IAASB members familiarize themselves with the issues raised in comment letters on an exposure draft to be able to make well-informed decisions as they finalize an international pronouncement.
- The IAASB reviews a project task force's analysis that summarizes the significant issues raised by respondents, outlines the task force's proposed disposition, and explains why the task force has, or has not, accepted respondents' significant proposed changes. The IAASB deliberates the significant issues, with significant decisions recorded in the minutes.
- Project task forces also consider significant points made at CAG meetings and respond in writing to the CAG explaining how the matters raised have been dealt with.
- The IAASB considers whether changes to the exposed document warrant re-exposure. If so, the explanatory memorandum accompanying the re-exposure draft includes the reasoning for re-exposure and sufficient information to allow an understanding of the changes made.
- For each final Standard, IAASB staff issues a Basis for Conclusions document that explains how the IAASB has dealt with respondents' comments on an exposure draft.
- The IAASB communicates alleged breaches of due process and their resolution to the PIOB.

### IV. APPROPRIATE APPROVAL

- The IAASB Technical Director advises the IAASB and the PIOB whether due process has been followed before a final pronouncement is approved for issue.
- The affirmative votes of at least two-thirds of the members present at a meeting in person or by simultaneous telecommunications link or by proxy, but not less than twelve, is required to approve exposure drafts and re-exposure drafts, or to approve or withdraw International Standards and Practice Statements.

## REPORT OF THE TECHNICAL DIRECTOR ON THE HIGHLIGHTS OF THE YEAR

### INTRODUCTION

In 2005, the IAASB achieved significant progress in meeting its goals of transparency, due process and quality of output, and international convergence through strong global partnerships. The following highlights the key accomplishments of the IAASB and the progress it has made over the past year towards developing Standards, strengthening its partnerships, and communicating with stakeholders.

### DEVELOPMENT OF STANDARDS

The IAASB held five meetings during the year, totaling 22 days of full Board deliberations. In addition, about 60 task force meetings (in person and through conference calls) were held during the year.

The IAASB issued two new or revised Standards in final form, and 11 new, revised or redrafted ISAs for public exposure. In addition, significant progress has been made on nine other projects. This significant output reflects the IAASB's commitment to increasing audit quality worldwide by improving auditor performance in the addressed areas. It also reflects the IAASB's determination to make clarity of Standards a priority (further details below).

Reflecting our focus on greater transparency, IAASB staff has started issuing a Basis for Conclusions document for each final approved Standard, beginning with the revised ISA 230, *Audit Documentation*. Basis for Conclusions documents explain the rationale for IAASB decisions on significant comments respondents made on exposure drafts. These non-authoritative documents do not form part of the final IAASB Standards and are not discussed by the IAASB. Nevertheless, they help readers understand the final Standards. They can be accessed from the "Recently Completed Projects" section on the IAASB website.

#### *The Clarity Project*

As reported by the IAASB Chairman, the Clarity project culminated in the set of new drafting conventions for IAASB Standards. The key features of the project's



James M. Sylph  
IAASB  
Technical Director

main improvements, and the implementation plan, are discussed below.

### CLARITY IMPROVEMENTS

#### *Objectives-based Standards*

Each Standard will state the objective to be achieved in relation to the subject matter of the Standard. The professional accountant will always be required to achieve the objective stated in each Standard where the Standard

is relevant in the circumstances of the engagement.

The professional accountant is expected to achieve that objective by complying with the requirements of the Standard, and by performing other procedures judged necessary in the circumstances.

#### *Clarifying Professional Requirements*

Each Standard will, in a separate section, specify requirements that assist the professional accountant in achieving the Standard's objective. Requirements are those actions or procedures considered sufficiently important to be generally required to meet the stated objective. The professional accountant will meet all requirements of a Standard that are relevant in the circumstances of the engagement. Requirements will be identified by the word "shall."



The Financial Stability Forum, a consortium of national authorities responsible for financial stability in significant international financial centers, has recognized ISAs as one of 12 core sets of standards that must be implemented as part of the improvement of the global financial architecture.





In exceptional circumstances where the professional accountant judges it necessary to depart from a requirement to achieve its purpose, the professional accountant will be required to document (a) how alternative procedures achieved the requirement's purpose, and (b) unless otherwise clear, the reasons for the departure. The professional accountant is expected to depart from a requirement only where a specifically required procedure would be ineffective in the specific circumstances of the engagement.

#### ***Eliminating Ambiguity Arising From Use of the Present Tense***

Standards will no longer use the present tense to describe actions or procedures of the professional accountant. In applying the new drafting conventions to existing Standards, sentences describing the professional accountant's actions or procedures in the present tense will be redrafted either by elevating the action or procedure to a requirement or by using words that make it clear that there is no intention to impose a requirement. The application of the new drafting conventions to the actions or procedures described in the present tense will be made case-by-case, bearing in mind the benefits and disadvantages of an increase in the extent and specificity of requirements.

#### ***Improving Readability and Understandability***

New terms or expressions will be defined in a Definitions section of a Standard. All Standards will contain the following four principal sections:

- Introduction – the scope and effective date of the Standard;
- Objective – the objective to be achieved by the professional accountant;
- Requirements – the requirements to be complied with, together with explanatory material necessary to make the section understandable by an experienced professional accountant; and
- Application Material – material, supplemented in some cases by appendices, that provides further explanation and guidance supporting proper application of the Standard.

Material contained in both the “Requirements” and “Application Material” sections will be cross-referenced.

In addition, drafting changes will be made to improve the readability and understandability of the Standards. These changes include eliminating duplication within individual Standards, highlighting considerations specific to small entities and public sector entities, and following “plain language” (or “plain English”) guidelines.

#### **IMPLEMENTATION PLAN**

The IAASB intends to apply the new drafting conventions to as many Standards as practicable and as quickly as the need for due process will permit.

#### ***Existing Exposure Drafts***

The IAASB will consider comments arising from exposure of Standards presently under revision in the current format and decide whether changes made based on those comments necessitate re-exposure. Before finalizing the proposed revised ISAs, the IAASB will redraft them using the new drafting conventions and re-expose the redrafted documents. Comments will only be sought, however, on changes resulting from applying the new drafting conventions and not on substantive issues addressed in the first exposure (unless changes made as a result of the original exposure would lead to re-exposure). This implementation plan will result in deferring finalization of those ISAs by approximately one year.

#### ***Exposure Drafts Approved After September 2005***

The new drafting conventions will be applied to all exposure drafts approved for issue by the IAASB after September 2005.

#### ***Other ISAs***

The IAASB also plans to apply the new drafting conventions to recently issued ISAs that were revised in the current format.

The new drafting conventions will then be applied to the remaining ISAs, in conjunction with their revision and updating. The IAASB will determine the priorities and schedule for this as soon as possible.

## Standards Approved in 2005

The IAASB finalized two Standards in 2005. The following highlights the significant features of these new Standards.

### *ISA 230 (Revised), Audit Documentation*

Audit documentation is a critical element of an audit, as it provides a record of the audit work and audit evidence that supports the auditor's report. The IAASB approved a revised ISA on audit documentation at its September 2005 meeting. The Standard introduces important changes designed to improve the quality of audit documentation the auditor prepares and retains.

To establish the level and completeness of documentation, the Standard requires the auditor to prepare audit documentation sufficient to allow an experienced auditor, having no previous connection with the audit, to understand the audit work, the audit evidence, significant matters arising during the audit, and the auditor's conclusions.

The Standard also establishes new requirements for the auditor to prepare audit documentation promptly and to close the audit files within a reasonable time. It explicitly restricts amendments to a closed audit file to certain exceptional circumstances. New documentation requirements are included for those very rare instances when an auditor finds it necessary to depart from the requirement of an ISA to achieve the objective of the audit. The IAASB believes that it is in the public interest for those circumstances to be documented.

The Standard is effective for audits of financial information for periods beginning on or after June 15, 2006. As part of this project, the IAASB also approved amendments to International Standard on Quality Control 1, *Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements*.

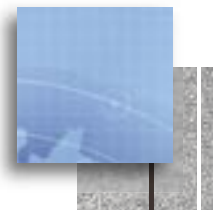
### *ISRE 2410 for Reviews of Interim Financial Information*

In June 2005, the IAASB issued a new International Standard on Review Engagements (ISRE) 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*, to assist auditors in carrying out their professional responsibilities when reviewing the interim financial information of an audit client. The new Standard responds to a need in those jurisdictions that use ISAs and that require or permit entities (primarily listed companies) to issue interim financial information that has been reviewed by their auditors.

The Standard outlines the general principles of a review of interim financial information, provides guidance on the inquiries and the analytical and other review procedures the auditor is to perform, and prescribes the content of the review report. The Standard also provides guidance on the engagement and management representation letters the auditor may obtain when performing the review and includes illustrative review reports.

The IAASB believes that the Standard will enhance consistency and quality in auditor performance and reporting on these review engagements. The Standard is effective for periods beginning on or after December 15, 2006.





## Exposure Drafts Issued in 2005

The following highlights the significant elements of the proposed new or revised Standards that the IAASB exposed during the year.

### ***Proposed Standards Redrafted Under the Clarity Convention***

As the first step in implementing the new drafting conventions under the Clarity project, the IAASB issued exposure drafts of four existing Standards in October 2005. These proposed redrafted ISAs are:

- ISA 240, *The Auditor's Responsibility to Consider Fraud in an Audit of Financial Statements*;
- ISA 300, *Planning an Audit of Financial Statements*;
- ISA 315, *Obtaining an Understanding of the Entity and Its Environment and Assessing the Risks of Material Misstatement*; and
- ISA 330, *The Auditor's Procedures in Response to Assessed Risks*.

The exposure draft of ISA 550 (Revised), *Related Parties*, issued in December 2005, was also drafted using the new drafting conventions (further details on ISA 550 are provided below).

In addition, to conform the Preface to the Clarity drafting conventions, the IAASB issued an exposure draft of proposed amendments to the *Preface to the International Standards on Quality Control, Auditing, Assurance and Related Services*.

### ***Proposed New Standards on Reporting on Other Historical Financial Information and Summary Audited Financial Statements***

At its June 2005 meeting, the IAASB approved the exposure drafts of the proposed new ISA 701, *The Independent Auditor's Report on Other Historical Financial Information*, and the proposed new ISA 800, *The Auditor's Report on Summary Audited Financial Statements*. In developing these proposed new Standards, the IAASB made changes necessary for consistency with the recently revised ISA 700, *The Independent Auditor's Report on a Complete Set of General Purpose Financial Statements*.

The proposed ISA 701 addresses auditors' reports for a wide variety of engagements, including reporting on a single financial statement or on a specific element of a financial statement. It also provides guidance on (a) determining the acceptability of the financial reporting framework used in preparing and presenting the financial information, and (b) matters the auditor considers in forming an opinion on the financial information. It includes considerations relevant both to financial statements designed to give a true and fair view or fair presentation and to financial statements prepared under a compliance framework.

The proposed new ISA 800 recognizes that criteria for preparing and presenting summary financial statements may not exist. It contains new standards and guidance on the criteria and procedures applicable to an engagement to report on summary financial statements.

In developing these two exposure drafts, the IAASB sought to reach an appropriate balance between trying to achieve consistency in practice and the fact that auditors may be subject to different legal or regulatory regimes around the world.

### ***Proposed Group Audit Standard***

In March 2005, the IAASB approved for re-exposure the proposed revised ISA 600, *The Audit of Group Financial Statements*, designed to enhance the quality of group financial statement audits.

This re-exposure draft was developed based on comments received on an earlier exposure draft. To reflect the importance placed on sufficient involvement of the group auditor in the work of other auditors participating in the group audit, the proposed Standard requires the group auditor to perform the work, or be involved in the work of other auditors, on all significant components of the group. The group auditor is also required to perform specific procedures in relation to the work performed on a component of the group by any other auditor and to consider its adequacy for the purposes of the group audit.

The IAASB has considered the comments on the re-exposure draft and will issue a redrafted proposed Standard for exposure under the Clarity drafting conventions in 2006.

### ***Proposed Standard on Communication With Those Charged with Governance***

Recognizing that sound corporate governance depends in part on a proper relationship between the auditor and those charged with governance, in March 2005 the IAASB approved for exposure the proposed revised ISA 260, *The Auditor's Communication with Those Charged with Governance*. The proposed Standard is designed to improve the quality and relevance of the discussions between the auditor and those charged with governance.

The proposed Standard includes new guidance dealing with the communication process, reflecting its importance in audit effectiveness, and sets out a framework for communication with those charged with governance. The proposed Standard describes more specifically than the existing Standard what the auditor should communicate, and why. Included in matters to be communicated are those outside the financial reporting and disclosure process that the auditor becomes aware of and that are considered so serious as to require communication. For listed entities, it also proposes to require certain categorized disclosures about fees charged for audit and non-audit services provided by the audit firm in the previous 12 months.

The IAASB has considered comments on the exposure draft and will issue a redrafted proposed Standard for exposure under the Clarity drafting conventions in 2006. The IAASB was pleased to work with the Australian Auditing and Assurance Standards Board on this project.

### ***Proposed Standards on Modified Opinions and Emphases of Matter***

In March 2005, the IAASB also approved exposure drafts of the proposed ISA 705, *Modifications to the Opinion in the Independent Auditor's Report*, and the proposed ISA 706, *Emphasis of Matter Paragraphs and Other Matters Paragraphs in the Independent Auditor's Report*. These exposure drafts are intended to drive greater consistency of auditor reporting among jurisdictions.

The proposed ISA 705 establishes standards and provides guidance, including illustrative examples, on circumstances that may cause the auditor to modify the opinion

on the financial statements. It aims to clarify when the opinion should be modified, explains the different possible types of modifications appropriate to the circumstances, and proposes general requirements for the form and content of modified auditors' reports.

As part of this project, the IAASB concluded that it would be clearer to separate the Standards on modifications to the opinion from those dealing with emphasis of matter and other matters paragraphs in the auditor's report. The IAASB therefore also exposed the proposed ISA 706, which contains standards and guidance on when the auditor should emphasize specific matters, or bring "other matters" to users' attention, in the auditor's report. This draft includes proposals on the form and placement of the paragraphs to be used to communicate such matters in the auditor's report.

I anticipate that the IAASB will consider comments and issue two redrafted ISAs for exposure under the Clarity drafting conventions in 2006.

### ***Proposed Related Parties Standard***

In December 2005, the IAASB approved the exposure draft of the proposed revised ISA 550, *Related Parties*, drafted under the new clarity conventions. This proposed Standard sets out more extensive requirements and application material that recognize the particular risks associated with related parties, including the risks of non-identification and non-disclosure and fraud.

The proposed Standard strengthens current practice by requiring the auditor to obtain an understanding of the nature and business rationale of an entity's related party relationships and transactions, sufficient for the auditor to identify, assess and respond to the risks of material misstatements resulting from them. It also requires the auditor to perform procedures to identify related party relationships and transactions not identified or disclosed by management.

The proposed Standard places new emphasis on evaluating the effects of related party relationships and transactions on the financial statements, even where the financial reporting framework does not establish related party accounting or disclosure requirements.





I expect the IAASB to consider comments on the proposed ISA in the second half of 2006.

A full listing of the Standards and exposure drafts issued in 2005, along with the status of other current projects, is provided in the Standards and Guidance section of the Appendix. Further details, including copies of IAASB pronouncements and exposure drafts, can be accessed on the IAASB website.

### STRENGTHENING RELATIONSHIPS WITH OUR PARTNER ORGANIZATIONS

The following highlights the actions taken by the IAASB during the year in strengthening its working relationships with its partner organizations.

#### ***IFAC International Ethics Standards Board for Accountants***

The IAASB has built upon its close working relationship with the IFAC International Ethics Standards Board for Accountants (“Ethics Standards Board”) to ensure that coordinated efforts are made to address issues of mutual relevance. Thus, IAASB representatives met a working group of the Ethics Standards Board in May 2005 to discuss the independence implications for the IFAC *Code of Ethics for Professional Accountants* of direct reporting assurance engagements, as recognized in the IAASB Assurance Framework. At its subsequent meeting in June 2005, the Ethics Standards Board approved revisions to the Code of Ethics that take such engagements into account.

The IAASB will continue to liaise with the Ethics Standards Board to address common issues promptly and consistently.

#### ***Small- and Medium-Sized Practices***

To enable the IAASB to give due consideration to issues relevant to SMEs and SMPs, the IAASB actively solicited input, and received submissions, from the IFAC SMP Committee on 12 projects at all the key stages of their development, from the project proposal stage to proposed exposure draft. This represented a sig-

nificant increase in interaction, demonstrating the IAASB’s commitment to taking the views of SMPs into account in developing its Standards. The IAASB also invited a member of the IFAC SMP Committee to join the Clarity task force in April 2005, recognizing the significance of this project to the SMP constituency.

In addition, an IAASB staff member attended the March 2005 IFAC SMP/SME and Developing Nations Consultative Conference. More than 125 representatives of IFAC member bodies, other professional and accounting associations, and development and funding agencies attended this conference, which focused in part on establishing an international response to the needs of SMEs and SMPs.

The issues SMPs face in implementing and applying ISAs also received prominent consideration at the IAASB CAG meetings held in 2005. On invitation, an SMP representative attended the meetings and participated in discussions with the CAG. Further details on this can be found in the reports of the Chairmen of the IAASB and IAASB CAG.

#### ***Developing Nations***

The IAASB acknowledges the important role its Standards can play in (a) strengthening the integrity of the financial reporting processes of entities based in developing nations,



(b) supporting the development of the accounting profession in these nations, and (c) facilitating their greater economic development. Thus, the IAASB has established a connection with the IFAC Developing Nations Committee and started more direct interaction with developing nation representatives during the year.

In addition, recognizing that many developing nations have adopted or are in the process of adopting IAASB Standards, the IAASB now invites specific comments from developing nations on exposure drafts issued during the year, particularly with regard to whether the proposed Standards will be difficult to implement in the developing nation environment.

#### ***Fédération des Experts Comptables Européens (FEE)***

FEE has regularly issued discussion papers addressing topics that directly concern practitioners in the EU. The IAASB maintains a watching brief on FEE's work and considers whether to respond to FEE where such work may have wider relevance to or implication for the IAASB's standard-setting work program.

Thus, during the year the IAASB task force addressing the auditor's involvement with comfort letters reviewed FEE's April 2005 discussion paper, *Comfort Letters Issued in Relation to Financial Information in a Prospectus*. The task force subsequently submitted a comment letter (which did not represent a formal IAASB response) to FEE.

In addition, the IAASB Steering Committee considered the March 2005 FEE discussion paper, *Risk Management and Internal Control in the EU*, and issued a general comment letter to FEE. Subsequently, in October 2005, an IAASB representative had the opportunity to participate in a forum organized by FEE on the same subject. This enabled the IAASB to update the participants on the IAASB's new project on clarifying the meaning of material weaknesses in internal control.

#### ***Royal NIVRA and the Global Reporting Initiative***

IFAC's member body in the Netherlands, Koninklijk Nederlands Instituut van Registeraccountants (Royal NIVRA), issued two exposure drafts on sustainability assurance in January 2005. An IAASB task force, with input from the IFAC Sustainability Experts Advisory Panel<sup>9</sup> (SEAP), responded to the exposure drafts in July 2005. While this was not a formal IAASB response, the IAASB considered it important to provide some input to the work of the Royal NIVRA, as the final Dutch Standards may provide a basis for an IAASB international Standard on sustainability assurance.

SEAP and IAASB staff continue to work with the Global Reporting Initiative (GRI), particularly in relation to the suitability of the GRI's Sustainability Reporting Guidelines as criteria for an assurance engagement. The next version of the GRI Guidelines is expected to be released in 2006.

#### ***Academia***

The IAASB maintained liaison with the academic community during the year through participation and speeches at a number of conferences and seminars. This allowed the IAASB not only to provide updates to the academic community on its work program and activities, but also to maintain general awareness of the latest auditing research undertaken by the academic community.

The IAASB welcomes academic participation on its project task forces where it believes that expertise can contribute to the development of its Standards.

## **COMMUNICATIONS**

### ***Informing Stakeholders***

Part of the IAASB's strategy is to raise public awareness of its work by communicating with stakeholders and promoting a greater understanding of its activities and outputs.

IAASB members and staff showed their commitment to this strategy during the year by (a) closely monitoring

<sup>9</sup> In 2004, the IAASB established an advisory panel of 14 experts, chaired by Roger Simnett, a member of the Board, to monitor developments in the field of assurance on sustainability reports. One of the terms of reference of the panel is to collaborate with the Global Reporting Initiative (GRI) to identify aspects of the GRI Guidelines where improvement can be made to make them more suitable as criteria for assurance reporting. The panel provides an important source of input and guidance to the IAASB as it considers whether to develop assurance standards in the field of sustainability reporting. The panel also monitors developments in this area.



external developments relevant to the IAASB's work, and (b) informing regulatory, standard-setting, academic and practitioner communities of the IAASB's activities, ongoing projects, and related developments.

The IAASB delivered that information in a variety of ways throughout the world, which has helped raise the IAASB's profile. These included:

- Presentations of updates on IAASB developments in the auditing and assurance fields to international and regional organizations;
- Presentations to the academic community on IAASB projects and activities;
- Meetings with regulators, the accountancy profession and IFAC member bodies on important issues of mutual relevance, such as the effects of regulatory developments, the role of auditors in the global economy, strategies for international convergence, and issues of translation;
- Press interviews by key IAASB representatives;
- Issuance of electronic IAASB news summaries; and
- Regular updates on the IAASB web pages.

The Appendix provides further details on the meetings IAASB representatives attended and the presentations they gave during the year.

The extent of this communication reflects the IAASB's continuing belief that communicating with stakeholders about its objectives, work program and activities, and outputs, and listening to their concerns or suggestions, are critical to wide recognition and acceptance of IAASB Standards.

### ***Translation of IAASB Pronouncements***

To increase the worldwide accessibility of IFAC standards and guidance, and to enable high-quality translations into languages other than English, in 2004 IFAC approved a Policy Statement, *Translation of Standards and Guidance Issued by the International Federation of Accountants*,<sup>10</sup> that outlines the procedures to be followed by external organiza-

tions in translating its pronouncements.

In the context of this effort to encourage wider translation of IFAC standards, I welcome the April 2005 agreement that IFAC signed with two of its member bodies – Compagnie Nationale des Commissaires aux Comptes (CNCC) in France and Institut des Reviseurs d'Entreprises (IRE) in Belgium – to translate the ISAs into French.

This agreement is significant in the context of the EU's consideration of the adoption of ISAs following the EC's recent finalization of the Eighth Company Law Directive. It also represents a timely reaction to the findings of the Wong Report, which identified the translation of Standards as a major challenge in achieving global convergence to international Standards.

CNCC and IRE Belgium worked with other French-speaking professionals from Canada, Luxembourg, and Switzerland, and from the Fédération Internationale des Experts-Comptables Francophones to build on existing translations and develop a single French version of ISAs for implementation throughout the world.

The involvement of several organizations in different French-speaking countries in reaching this agreement helps to support the strong quality control over translation encouraged by the IFAC translation policy. This means that the EC can look forward to adopting a set of standards in French that have been prepared using all the quality control processes set out in that policy.

The success of this initiative has led to the formation of a similar working group between IRE Belgium and Royal NIVRA, aimed at producing a single, agreed translation of ISAs into Dutch.

**During the year, IFAC granted permission for the ISAs to be translated into Bulgarian, German, Lithuanian, Mongolian, Polish, Romanian, Russian, Serbian, Slovak, and Spanish.**

<sup>10</sup> The Policy Statement on translation can be downloaded from IFAC's website at [www.ifac.org](http://www.ifac.org).

The French and Dutch translation efforts may represent appropriate models for cooperation for translation of the Standards into other languages. I expect IFAC's translation policy to lead to further improvement in the consistency and quality of translations of the IAASB's pronouncements by national standard setters and others.

#### ***Publications and Distribution***

To achieve the widest use and recognition of IAASB Standards, the IAASB makes its pronouncements available on its website free-of-charge. IFAC and the IAASB jointly released the 2005 edition of the *Handbook of International Auditing, Assurance, and Ethics Pronouncements*, containing all IAASB pronouncements issued as of December 31, 2004. Starting in 2005, a searchable electronic eComPress version containing the international auditing, assurance, and ethics pronouncements has been produced for

During 2005, the IAASB website attracted 96,600 visitors. Nearly 90,000 copies of final IAASB publications, including Standards, and nearly 22,700 copies of exposure drafts were downloaded. 2,466 print copies of the 2005 *Handbook of International Auditing, Assurance, and Ethics Pronouncements* were ordered.

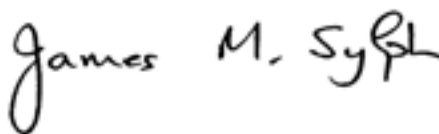
sale to the public. Individual publications continue to be available for download free-of-charge from the website.

IFAC member bodies are encouraged to promote IAASB Standards and guidance to their members and can link their websites to the IAASB website.

#### **ACKNOWLEDGMENTS**

I would like to express my gratitude to the Chairman for his leadership and extend my appreciation to the Board members and all those who continue to support the work of the IAASB. And to

my highly competent and hard-working team, especially my two senior technical managers, a big thank you.



James M. Sylph  
IAASB Technical Director

#### **IAASB Technical Staff**



IAASB Technical Staff: (l. to r.) Alta Prinsloo, Michael Nugent, James L. Gunn, James M. Sylph (IAASB Technical Director), Ken Siong, and Jan Tyl.



## APPENDIX

# IAASB MEMBERS, TECHNICAL ADVISORS, OBSERVERS, AND TECHNICAL STAFF

*As at December 31, 2005*

**BOARD MEMBERS****TERM ENDING****TECHNICAL ADVISORS*****Nominated by IFAC Member Bodies***

John Kellas (Chairman), *United Kingdom*

2006

Mowafak Al Yafi, *Lebanon*

2005

Sukanta Dutt, *Malaysia*

2006

Josef Ferlings, *Germany*

2006

John Fogarty, *United States*

2006

Rogério Gollo, *Brazil*

2005

Gen Ikegami, *Japan*

2005

Will Rainey, *United Kingdom*

2007

Roberto Tizzano, *Italy*

2007

Gérard Trémolière, *France* \*

2005

David Kazi, *Lebanon*

Tan Shook Kheng, *Malaysia*

Wolfgang Böhm, *Germany*

Chuck Landes, *United States*

Makoto Shinohara, *Japan*

Jon Grant, *United Kingdom*

Cédric Gélard, *France*

***Nominated by the IFAC Transnational Auditors Committee***

Denise Esdon (Deputy Chair), *Ernst & Young* \*

2005

Philip Ashton, *PricewaterhouseCoopers*

2005

Craig Crawford, *KPMG*

2007

Jan Bo Hansen, *Deloitte Touche Tohmatsu*

2007

Bodo Richardt, *KPMG*

2006

George H. Tucker, *Ernst & Young*

Diana Hillier, *PricewaterhouseCoopers*

Sylvia Smith, *KPMG*

Jennifer Haskell, *Deloitte Touche Tohmatsu*

***Public Members***

Inga-Britt Ahlenius, *United Nations*

2007

Ian McPhee, *Australia* \*

2005

Roger Simnett, *Australia*

2005

Kelly Ånerud, *Norway*

Richard Mifsud, *Australia*

**OBSERVERS**

David Damant (IAASB CAG Chair, *United Kingdom*)

Thomas Ray (Public Company Accounting Oversight Board, *United States*)

Dr. Hisashi Yamaura (Financial Services Agency, *Japan*)

**IAASB Technical Staff**

Technical Director

James M. Sylph

Senior Technical Managers

James L. Gunn

Alta Prinsloo

Technical Managers

Michael Nugent

Ken Siong

Jan Tyl

Executive Assistant

Sara Clark

Administrative Assistant

Dorothy Ofori

\* These members were re-appointed after their terms ended at the end of 2005. For other appointments effective January 1, 2006, see the report of the Chairman.

## IAASB STANDARDS AND GUIDANCE

The following standards and guidance were issued or are under development by the IAASB. Additional information on these projects can be found on the IAASB's website at [www.iaasb.org](http://www.iaasb.org).

### 2005 ACHIEVEMENTS

#### *Approved and Issued*

#### *Approved*

##### INTERNATIONAL STANDARDS ON AUDITING

ISA 230 (Revised), *Audit Documentation*

September

##### INTERNATIONAL STANDARDS ON REVIEW ENGAGEMENTS

ISRE 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*

June

#### *Approved for Public Exposure*

##### INTERNATIONAL STANDARDS ON AUDITING

ISA 260 (Revised), *The Auditor's Communication with Those Charged with Governance*

March

ISA 550 (Revised), *Related Parties*\*

December

ISA 600 (Revised), *The Audit of Group Financial Statements*

March

ISA 701, *The Independent Auditor's Report on Other Historical Financial Information*

June

ISA 705, *Modifications to the Opinion in the Independent Auditor's Report*

March

ISA 706, *Emphasis of Matter Paragraphs and Other Matters Paragraphs in the Independent Auditor's Report*

March

ISA 800, *The Auditor's Report on Summary Audited Financial Statements*

June

##### INTERNATIONAL STANDARDS ON AUDITING – EXPOSURE DRAFTS OF ISAs

##### REDRAFTED UNDER THE CLARITY CONVENTION

ISA 240 (Redrafted), *The Auditor's Responsibility To Consider Fraud in an Audit of Financial Statements*

October

ISA 300 (Redrafted), *Planning an Audit of Financial Statements*

October

ISA 315 (Redrafted), *Obtaining an Understanding of the Entity and*

*Assessing the Risks of Material Misstatement*

October

ISA 330 (Redrafted), *The Auditor's Procedures in Response to Assessed Risks*

October

##### OTHER

Amendments under the Clarity convention to the *Preface to the*

*International Standards on Quality Control, Auditing, Assurance and Related Services*

October

### IN PROGRESS

The IAASB is currently working on a number of other projects and initiatives. A large part of this work deals with the redrafting of ISAs under the Clarity project; see discussion of the Clarity implementation plan in the Technical Director's report.

\* The exposure draft of the proposed ISA 550 was issued under the Clarity drafting conventions.



## COMMUNICATING WITH STAKEHOLDERS

The following lists the most significant events IAASB members or staff attended during the year, including those at which presentations were given.

- Accounting Association of Australia and New Zealand – Annual Conference
- American Accounting Association – Auditing Section Meeting
- Arab Federation of Certified Public Accountants – Convention
- Association of Chartered Certified Accountants – Auditing Committee
- Australian Institute of Social and Ethical Auditing – Sustainability Assurance Workshop
- Basel Committee on Banking Supervision – Accounting Task Force Meeting
- Canadian Public Accountability Board – IAASB Update
- Contadores Publicos del Peru – Seminar
- Environmental Management Accounting Network – EMA Update
- European Auditing Research Network – Oversight of the Auditing Profession
- Fédération des Experts Comptables Européens
  - European Auditing Standard Setters Meeting
  - Forum on Risk Management and Internal Control in the EU
  - Sustainability Working Party Meeting
- Fédération des Experts Comptables Méditerranéens
  - Annual Meeting
  - SME/SMP Seminar
- Financial Stability Institute – Advanced Accounting and Auditing Seminar
- Forum of Firms – IAASB Update
- IFAC SMP/SME and Developing Nations Consultative Conference
- Institute of Chartered Accountants in England and Wales – Conference on the Future Role of Auditing in the Global Capital Markets
- Institute of Chartered Accountants in India – International Conference: International Auditing and Assurance Standards – Convergence Issues
- International Consortium of Governmental Financial Management
- International Organization of Securities Commissions – Emerging Markets Regional Training Seminars
- International Symposium on Audit Research – Annual Conference
- National Board of Accountants and Auditors of Tanzania – Annual Seminar on the Application of IFRSs and ISAs in Financial Reporting in Tanzania
- New Zealand Institute of Chartered Accountants – Conference
- Shanghai International Forum – Market Access and Fair Competition
- Society of Certified Accountants and Auditors of Kosovo – 2005 Annual General Meeting
- Sustainability and Environmental Management Accounting Conference
- World Bank – ROSC Dissemination Conference

## REPORT FROM THE CHAIRMAN OF THE IAASB CONSULTATIVE ADVISORY GROUP

The IFAC Reform Proposals of September 2003 included the enhancement of the IAASB's Consultative Advisory Group (CAG) in order that the CAG should bring forward for consideration by the IAASB the views of a wider constituency of stakeholders in the auditing process. As the first independent Chairman of the IAASB CAG, I therefore took steps to enlarge the membership of the CAG.

The membership of the CAG as at December 31, 2005, is listed in the Appendix to this report and is now almost complete. The aim has been to cover the main geographical areas and include professions and organizations with interests in the development of auditing standards. It should be noted that membership of the CAG is by organization, rather than individual. In this way, the authority of the discussions at the CAG by the representatives of those organizations is significantly increased.

Within the IFAC structure, the IFAC Monitoring Group comprises a number of regulatory and similar bodies. Of these, the Basel Committee on Banking Supervision, the European Commission, IOSCO and the World Bank are represented on the CAG for the discussion of technical points. This adds a regulatory dimension to the geographical and professional inputs to the CAG.

At the same time, I have been concerned to improve the processes by which the CAG operates. As new IAASB topics for the establishment or revision of an International Standard on Auditing (ISA) are introduced, the CAG appoints a working group of two or three members to study the subject in detail. The working group then generates issues and concerns to bring forward in the discussions at CAG meetings, at which the IAASB project task force itself seeks CAG's counsel on key matters arising out of the project. Representatives of the IAASB leadership and the relevant task forces attend all CAG meetings, and through these processes, therefore, the discussion on each proposed ISA can be detailed and informed.

I have, in addition, instituted a feedback mechanism. Significant points made in the CAG discussions are minuted, and the relevant IAASB task force will subsequently

produce a report commenting on the points in the minutes and explaining why certain of these points might not have been taken up in the resulting ISAs. This is an important mechanism which is especially appropriate in the discussion of complex matters at the international level.

During 2005, the Public Interest Oversight Board (PIOB) came into existence, and I have liaised with the PIOB on the development of the CAG and on the CAG Terms of Reference

and allied documentation. My liaison includes the distribution of CAG documents to the PIOB Secretariat, and where appropriate, to members of the PIOB. In addition, during 2005, I met the PIOB on two occasions in formal session.

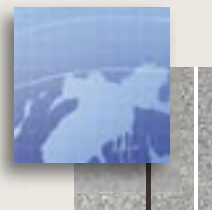
During 2005, it was decided by the IAASB CAG, and approved by the PIOB, that from 2006 onwards the meetings of the CAG should be open to the public. We shall establish procedures for this similar to those of the IAASB, which is already open to the public. There will, however, be some closed sessions for discussing administrative, personnel and similar matters. I believe that all standard-setting processes, especially those operating internationally, should be as transparent as possible. I have noted on becoming the Chairman of the CAG that the processes of the IAASB itself are transparent to a high degree, and I intend to ensure that the same is true of the CAG.

The technical discussions of the IAASB CAG during 2005 have followed the work program of the IAASB itself. I will refer, in particular, to the Clarity project. This is of the first importance in the development of ISAs since it imposes a clear and understandable structure on the standards and resolves long-standing problems in the use of language and some fundamental points such as rules versus principles. On the latter point, the IAASB's explanatory memorandum for



*David Damant*  
Chairman  
IAASB Consultative  
Advisory Group





the October 2005 Clarity exposure drafts indicates that the Clarity project orientates each ISA on an objective. This is a central proposal and all interested parties throughout the world should consider whether this move, backed up by a clear delineation of an appropriate number of requirements placed upon the auditor, provides a suitable template for the development of ISAs in future.

The Clarity project also resolves some other questions such as the need for inputs in the development of ISAs from small- and medium-sized practices and from developing nations. These inputs are explicitly mentioned in the Clarity proposals and I have, in addition, in the work of the CAG, taken steps to ensure that the views of these constituencies are taken into account. I shall take similar action as the views of other constituencies come forward.

The development of high quality auditing standards remains central to the evolution of the auditing function worldwide. It is sometimes said that auditing standards alone will not ensure a high quality audit. This may well be true, but this is not an argument against the development of high quality audit standards in themselves, without which

the other elements – such as regulation or ethics – will not be firmly based.

Thus, the development of the ISAs is of crucial importance, and I would like to address my thanks to the distinguished organizations and representatives who now contribute to the debate in the CAG and provide a high quality interface and focused inputs to the work of the IAASB itself. In this context, I must, in addition, mention the significant part played by the IFAC staff whose intelligent and professional work makes such a large contribution to the efficiency of the operation. I should also like to thank John Kellas and Denise Esdon, the Chair and Deputy Chair of the IAASB, for their constant encouragement and attention to the views of the CAG.

David Damant  
Chairman, IAASB Consultative Advisory Group



## APPENDIX

## CONSULTATIVE ADVISORY GROUP MEMBERS

The Consultative Advisory Group (CAG) is an integral and important part of the IAASB's formal process of consultation. As of December 31, 2005, the membership of the IAASB's CAG comprised:

- Asian Financial Executives' Institutes
- Basel Committee on Banking Supervision
- CFA Institute
- Eastern, Central and Southern African Federation of Accountants
- European Commission
- European Federation of Accountants and Auditors for SMEs
- European Financial Executives' Institutes
- Fédération des Experts Comptables Européens
- Foundation Institute Capixaba of Research in Accounting, Economy, and Finance
- Information Systems Audit and Control Association
- Institute of Internal Auditors
- Institute of International Finance
- International Accounting Standards Board
- International Actuarial Association
- International Bar Association
- International Corporate Governance Network
- International Organization of Securities Commissions
- International Organization of Supreme Audit Institutions
- Islamic Financial Services Board
- Japan Securities Dealers Association
- National Organization for Financial Accounting and Reporting Standards in Russia
- North American Financial Executives' Institutes
- United Nations Conference on Trade & Development
- World Bank
- World Federation of Exchanges

Observers to the IAASB are also observers to the CAG.



## **IAASB CONTACT INFORMATION**

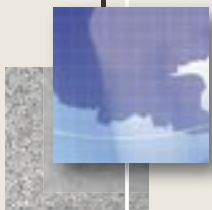
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