

**International
Auditing and
Assurance
Standards
Board**



**2002 Annual
Report**

*Strengthening
Public Confidence
in the Global
Auditing Profession*

International Federation of Accountants



The International Federation of Accountants

The International Federation of Accountants (IFAC) is the worldwide organization of the accountancy profession. Its mission is the worldwide development and enhancement of the profession with harmonized standards able to provide services of consistently high quality in the public interest.

IFAC comprises 155 member organizations from every part of the globe, representing more than 2.5 million accountants in public practice, education, government service, industry and commerce. No other accountancy body in the world, and few other professional organizations, has the broad-based international support that characterizes IFAC. Membership in IFAC is open to accountancy organizations recognized by law or general consensus within their countries as substantial national organizations in good standing.

For more information, visit IFAC's web site at www.ifac.org.

IFAC, IAASB and the Public Interest

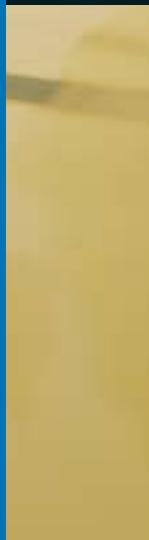
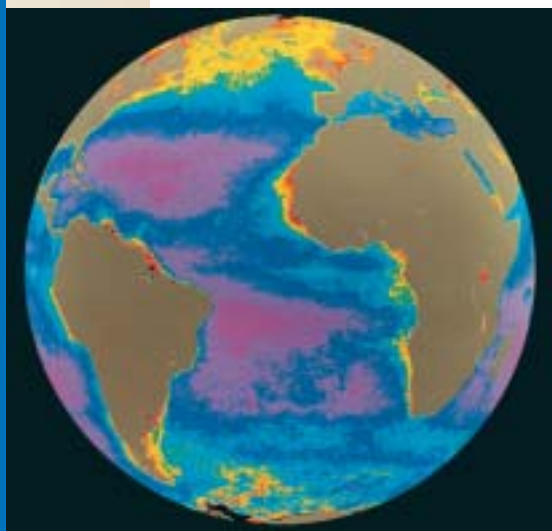


The “worldwide” and “public interest” aspects of IFAC’s mission serve as guiding principles for the organization. IFAC recognizes that a fundamental way to protect the public interest is to require the application of a core set of internationally recognized standards as a means of ensuring the credibility of the information upon which investors and other stakeholders depend. In recent years, IFAC has launched a major drive to promote sound global financial reporting practices and to create a framework for auditing and assurance services to provide users of those services with enhanced information and thereby facilitate capital flows and, ultimately, enable social stability and economic well-being. The International Auditing and Assurance Standards Board (IAASB) plays a key role in achieving this objective.

This report outlines IAASB’s activities over the past year, highlighting, in particular, the ways in which it serves both the worldwide accountancy profession and the public interest.

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The International Auditing and Assurance Standards Boards

The International Auditing and Assurance Standards Board (IAASB), formerly the International Auditing Practices Committee (IAPC), functions as an independent standard setting body under the auspices of IFAC. The IAASB develops standards and guidance for financial statement audits and other assurance or related services pertaining to both financial and nonfinancial information, and establishes quality control standards covering the conduct and performance of such services. The IAASB issues International Standards on Auditing (ISAs) and International Auditing Practice Statements (IAPs), which serve as the worldwide benchmark for high quality auditing standards and related guidance. They establish basic responsibilities for auditors, help them cope with increased and changing demands for credible financial information and provide guidance in specialized areas.



IAASB members: (back row, left to right) Gérard Trémolière, Suresh Kana, Denis Desautels, John Archambault, Roger Simnett, Ian Plaistowe, Edmund R. Noonan, John Kellas; (front row, left to right) Roberto Tizzano, Gen Ikegami, Philip Ashton, Denise Esdon, Dietz Mertin (Chair), Roger Dassen, Jan Bo Hansen, Ana Maria Elorrieta, Ian McPhee, Yang Zbiguo

IAASB Processes

The IAASB works closely with major national standard setters to develop high quality standards and guidance and to promote international convergence of standards. In developing these standards, the IAASB seeks out the views of its stakeholders, prioritizes the issues identified and develops standards and guidance in the best interest of the public and the profession. It also promotes debate with users, regulators and practitioners to identify needs for new standards and guidance.

The IAASB follows a rigorous due process to ensure that it takes into account the views of those affected by its standards and guidance

To date, more than 70 countries have indicated that they either have adopted ISAs or noted that there are no significant differences between their national standards and ISAs. ISAs have been translated by member bodies into more than 20 languages, including French, German, Russian and Spanish. Moreover, the Financial Stability Forum, a consortium of national authorities responsible for financial stability in significant international financial centers that seeks to improve the functioning of markets, recently recognized ISAs as one of a set of 12 core standards that must be implemented as part of the revamping of the global financial architecture.

before pronouncements are issued. Draft pronouncements are exposed for public review and comment and all comments received are posted on the IAASB's web site. The due process is transparent – IAASB meetings are open to the public and related agenda materials are available on the IAASB's web site prior to each meeting.

The IAASB holds four full Board meetings annually. The IAASB ordinarily appoints task forces to assist it in the development of guidance on specific subject matters. These task forces may include individuals who are not members of the IAASB, and information may be sought from other organizations so as to obtain a broad spectrum of views. Task force meetings ordinarily are scheduled between full Board meetings.

IAASB Composition

The IAASB consists of members from around the world with significant experience in the field of auditing and assurance services, comprising practitioners in public practice as well as public members. IAASB members are appointed by the IFAC Board based on recommendations from the IFAC Nominating

Committee. All IAASB members contribute their time and expertise on a volunteer basis, without remuneration from IFAC. Exhibit 1 contains a list of current IAASB members, their technical advisors and the IAASB technical staff.

IAASB Operations

The IAASB is supported financially through the IFAC membership dues assessed to its member bodies and by direct funding received from the Forum of Firms. The Forum of Firms is a collaboration of public accounting firms that share the common objective to promote consistently high standards of financial reporting and auditing worldwide in the interest of users of the profession's services and the general public. With the exception of certain costs of the public members of the IAASB that are funded by IFAC, some member bodies and the Forum of Firms provide further financial support for the costs of travel, accommodations and ancillary expenses for the volunteer IAASB members and their technical advisors.

IAASB Mission

The mission of the IAASB is to establish high quality auditing, assurance, quality control and related services standards and to improve the uniformity of practice by professional accountants throughout the world, thereby strengthening public confidence in the global auditing profession and serving the public interest. In promulgating standards and guidance that are acceptable to a broad constituency of international stakeholders, the IAASB works toward the continuing convergence of national and international standards and it encourages participation in joint projects with experienced standard setters from around the world.

Chair's Report



Dietz Mertin
Chair

It is with great pleasure that I present the IAASB's first annual report. Events over the last two years have seen tremendous change in the marketplace – intensified regulatory and stakeholder scrutiny, shaken investor confidence in governance and oversight practices – and presented a clearer view of the challenges our profession will be facing in the future. Global stock markets also have been severely hit by a series of corporate scandals that have brought into question the quality of accounting and auditing standards and the performance, independence and objectivity of those applying them.

Despite these tumultuous events, criticism was generally not directed at auditing and assurance standards *per se*, but rather at the performance of auditors and other market participants. Regulators in many countries are introducing processes aimed at setting more rigorous standards for executives, audit committees and analysts. The methods of assessing auditor performance are being considered throughout the world. Global convergence of standards for accounting and auditing, as well as enhanced quality control considerations, have risen to the forefront of stakeholders' interests. Improvement in corporate governance is being viewed as a critical, if not fundamental, component of necessary change.

This report highlights some of the IAASB's achievements in global convergence of standards and some of the fundamental changes taking place within the IAASB. With the formation of the new IAASB in April 2002, we have gained a clearer vision of the goals that need to be achieved and "new thinking" on how they should be accomplished.

STRUCTURE OF THE IAASB

Recognizing the need for strengthened processes and broader membership of the IAPC (now the IAASB) to facilitate development of high quality international standards, the IFAC Board commissioned in 2001 a Review Task Force to undertake a comprehensive review of the IAPC's membership, organization and processes. The final report was presented to the IFAC Board and Council at the end of 2001. The report called for wide-ranging changes to



the IAPC's structure and processes to significantly upgrade and accelerate its standard-setting activities and to improve its transparency.

The Task Force review was viewed as a necessary and valuable exercise. In 2002, the IFAC Board and the IAASB took the following actions that, in combination, improve both its transparency and effectiveness:

- Effective April 1, 2002, the IAPC's name was changed to the IAASB to better reflect its role, mandate and structure, and the new IAASB was created. The new IAASB is just that – a “new” Board. The IAASB comprises eighteen members, ten of whom are put forward by member bodies of IFAC, and for the first time, five of whom are put forward by the Forum of Firms, and three public members who may be members of IFAC member bodies but may not be members in public practice. Ten of the 18 members are new. The new Board continues to have broad geographic representation – Europe, the Americas, Asia Pacific and Africa.
- Ms. Denise Esdon was appointed the IAASB's Vice-Chair and Mr. James Sylph as its full-time Technical Director. These appointments were coupled with an increase in the complement of professional staff supporting the IAASB – important steps in accelerating the IAASB's activities.
- A fourth full Board meeting of the IAASB has been added to its annual agenda. To provide for more full Board meeting time at each of the four annual meetings, task force meetings addressing individual projects now ordinarily occur between full Board meetings.
- The IAASB strategy and medium-term agenda were extensively updated and streamlined, with specific focus on the global acceptance of ISAs.
- An ambitious agenda to develop its own processes and to set and implement its action plan is being set. Recent IAASB discussions included such matters as structure of the IFAC IAASB Handbook (including the clear separation of ISAs and standards for other assurance engagements), the types of documents that IAASB should issue and the differing rules that might be associated with their drafting, approval and publication.
- Amendments to the Preface of the IFAC IAASB Handbook, redefinition and confirmation of the bold/gray lettering as a convention to be used in ISAs, and the IAASB Terms of Reference on how it will be structured and operate have recently been exposed for public comment.
- IAASB's meetings to discuss the development of standards and guidance were made accessible to the public, as were the agenda material, minutes and other relevant documents. In addition, all final IAASB

pronouncements will now be available free of charge in electronic form through the IFAC web site effective January 1, 2003.

FOCUS OF THE IAASB

As Chair of the IAASB, I have overseen a number of important developments and initiatives that have shaped the activities and future plans of the IAASB. To achieve its mission, the IAASB focuses on the following strategic objectives:

- **Development of standards** – Establishing high quality auditing, assurance, quality control and related services standards.
- **Global acceptance** – Promoting the adoption and acceptance of IAASB pronouncements.
- **Convergence and partnership** – Supporting a strong and cohesive international auditing profession by coordinating with our Consultative Advisory Group, regional organizations, member bodies, and national standard setters.
- **Communications** – Improving the quality and uniformity of auditing and assurance practices and related services throughout the world by encouraging debate, presenting papers and issuing pronouncements on a variety of audit and assurance topics.

In 2003, we will be publishing an IAASB Action Plan covering the years 2003-2004 during which we will focus on these and other objectives. We welcome public input to our action plan which I expect will be updated later in 2003.

Development of Standards

The IAASB supports changes in auditing standards that provide shareholders and the general public with greater confidence in the financial information circulating in the capital markets. In this regard, the IAASB has undertaken a number of fundamental steps to

The IAASB continues to believe that high quality standards based on basic principles and essential procedures will best serve the public interest by eliciting thoughtful auditor assessment of the particular circumstances of each engagement.

complete and update its auditing and assurance standards as well as enhance the processes underlying their development. The IAASB's recently issued proposed standards on assessing and responding to audit risk, for example, have been a significant project designed to enhance the auditor's implementation of the audit risk model and, ultimately, improve auditor performance. On an international level, the proposed standards represent significant changes to the body of auditing standards governing audits of financial statements.

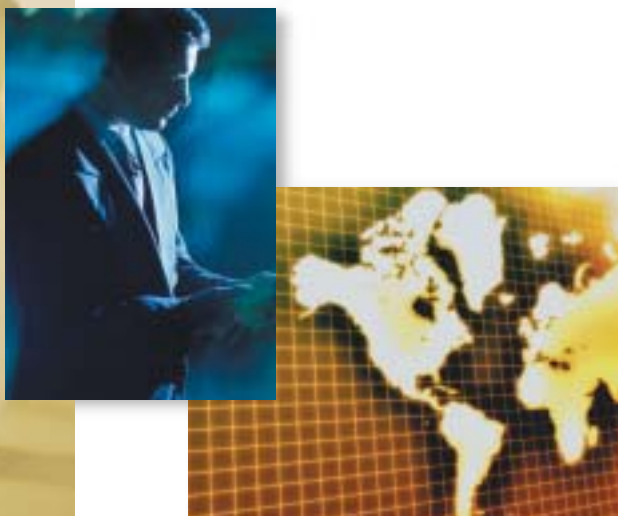
Corporate failures over the recent past have also raised questions about other areas of corporate financial responsibility requiring auditor attention. Accordingly, the IAASB also has begun a series of individual but interrelated projects aimed at addressing these issues. These projects include a revision to standards dealing with the auditor's responsibility to consider fraud and error in the audit of financial statements, examination of current guidance on audit materiality, accounting estimates, review of interim financial information, and a review of the wording of the auditor's report. These and other priority projects are further discussed in the "Technical Director's Report" section of this publication.

Any new standards or changes to current standards will be evolutionary and based on wide consultations that support the belief that such standards will produce long-term gains. The IAASB continues to believe that high quality standards based on basic principles and essential procedures will best serve the public interest by eliciting thoughtful auditor assessment of the particular circumstances of

each engagement. It is recognized that related guidance and explanatory material needs to be sufficiently comprehensive and complete to drive auditor behavior and eliminate differences in practice. This approach to standards also assists with convergence of standards on a worldwide level.

Global Acceptance

One of the IAASB's main challenges is to consolidate and complete the global acceptance of its standards – a goal toward which, I am pleased to announce, significant progress has been made. Endorsement and adoption of ISAs by the European Commission (EC), the International Organization of Securities Commissions (IOSCO) and other stakeholders are key components of this major strategic objective and, ultimately, an important step toward international convergence of standards.



Endorsement of ISAs by the European Commission

Ongoing communication with the EC has been, and remains, intense and very positive. The EC is currently proposing that by 2005 national auditing standards in the European Union should require auditors of financial statements to comply with ISAs in the performance of their audits. This proposal has been well received by most Member States and

bodes well for the adoption of ISAs. Although specific changes to existing ISAs are not prerequisite to this adoption, it nevertheless is essential that we utilize our Consultative Advisory Group to allow early and effective EC input into the agenda and project work plan of the IAASB.

The IAASB updates the EC's Committee on Auditing on the latest developments in international standard setting, and considers views expressed by the EC regarding the IAASB's agenda and exposure drafts very carefully. We will consider and implement, whenever appropriate, the EC's recommendations from a worldwide standpoint as the IAASB develops and updates its ISAs.

The Fédération des Experts Comptables Européens (FEE) and other stakeholders have been very active during these discussions and I am grateful for their support and encouragement.

The IAASB will continue to work closely with the EC and others to ensure a smooth adoption of ISAs in Europe.

Endorsement of ISAs by the International Organization of Securities Commissions

Over the last year, much progress has been made through open and thoughtful discussion with IOSCO. IOSCO has begun a phased program of reviewing existing ISAs as well as commenting on exposure drafts of new standards. Commentary on five ISAs has been received to date. The IAASB is considering these comments and will assess whether these standards should be modified. To support this process, the IAASB has offered coordination between itself and IOSCO to avoid any unnecessary review of, and comment on, current standards.

By opening and maintaining active communication channels, the IAASB and IOSCO have established an effective working relationship. The IAASB intends to build upon

this relationship with a view toward ensuring that, on completion of IOSCO's review and evaluation by the Board of any resulting comments, both the IAASB and IOSCO will be satisfied that ISAs represent a high quality set of standards that can be endorsed.

Related to this process is the work of the IAASB Revisions Committee, a standing committee established by the IAASB to review all of its pronouncements periodically and to consider whether individual ISAs need to be revised to address current thinking and experience. The objective of the IAASB Revisions Committee is to ensure IAASB pronouncements continue to provide, in the public interest, a single set of high quality global standards. Comments offered by IOSCO provide useful input to the work of the IAASB Revisions Committee as it considers the need to revise individual ISAs.

Cooperation with Others — Continuing Dialogue

Our relationship with the Basel Committee on Banking Supervision continues to be close and constructive. We continue to update the Basel Committee through our Consultative Advisory Group about current developments and our work program.

Exploratory meetings were recently held between representatives from the IAASB and the International Organization of Supreme Audit Institutions' (INTOSAI) Auditing Standards Committee at a meeting initiated by the World Bank. Following these meetings, INTOSAI, through its Auditing Standards Committee, has expressed an interest in contributing to the work of the IAASB in their work to review and develop ISAs. The goal of INTOSAI is to develop Audit Guidelines for INTOSAI members based on ISAs. These guidelines would consist of certain ISAs as endorsed in their current form by INTOSAI, other ISAs supplemented by practice notes indicating how and whether they can be applied

in a public sector context, and additional guidelines written by INTOSAI specific for public sector audits. While clearly an important step towards the globalization of auditing standards, the approach to and implications of such an endeavour requires careful deliberation by the IAASB.

The IFAC Public Sector Committee (PSC) continues to consider the output of the IAASB from a public sector perspective. At a future date, enhanced relationships with INTOSAI and the direct participation of IAASB members with public sector auditing experience may alter the relationship with the PSC.

IAASB develops its standards to be applicable for audit engagements of all sizes. The interests of small- and medium-sized practices (SMPs) are considered during the development of all ISAs. To increase input from this important constituency, the IAASB has sought support from the IFAC Small / Medium Practices Task Force. This group is providing input through its network of contacts.

Partnerships Toward International Convergence

The IAASB is conscious of the need for extensive consultation and transparency as it moves forward. The following describes some of our key initiatives and recent developments in working toward solid international partnerships and convergence of standards.

Communication with the IAASB Consultative Advisory Group

The Consultative Advisory Group (CAG) constitutes an important forum to give representatives of regulators, investors, users and others the opportunity to influence the IAASB's agenda and to contribute to the development of international auditing and assurance standards and guidance. The ongoing exchange of views with our stakeholders is the necessary basis for our agenda to make sure

that expectations of the community are considered and met.

The CAG is an active and valued contributor to the IAASB and is seen as an integral and important part of the IAASB's work structure. The CAG meetings have attracted more and more interest every year, with IAASB matters moving more into the focus of discussions. Exhibit 2 contains a list of the current CAG members.

In May, we initiated discussion with the CAG about our present working relationship and how we might improve it, operating procedures and our future strategy. CAG members also were invited to assist in the development of a strategic plan for IAASB. As a result, we are jointly undertaking actions to require CAG members to play a greater role in assisting with convergence and global acceptance of IAASB guidance. These include increasing the number of meetings with the CAG to two each year, focusing the CAG meeting agenda more on IAASB's technical agenda, soliciting comments from the CAG on proposals for new projects at an earlier stage and monitoring progress throughout their duration, and reviewing the CAG's terms of reference to better structure the group's activities and to improve transparency. In addition, steps are underway to expand the CAG's global representation and to review its member nomination process.

In October, we held another very successful meeting with the CAG, acting on decisions made during our May meeting. Valuable input was received on several of the IAASB's current projects, including Audit Risk, Quality Control, Considering the Work of Other Auditors, Audits of Group Financial Statements, and Review of Interim Financial Information, as well as receiving constructive feedback on proposed new projects.

Cooperation with National Auditing Standard Setters

In 2001, we initiated the development of a network of the 10 most active national auditing standard setters to discuss current and, more important, future agendas for standard setting. The objective of this network is to achieve closer cooperation with an aim to share resources, minimize duplication and reach consensus and convergence of standards at an early stage in their development.

Since its inception, the network of national auditing standard setters has held its first two annual meetings. Its continuing focus is on the possibilities of further joint projects that could be developed on a worldwide basis and for which a national standard setter or the IAASB would be ready and able to take the lead.

At its 2002 meeting, every member of the network agreed to take the lead in a project, to be a member of a joint task force or to send experts, members of their own committees or technical staff to support IAASB activities.

We have had a very successful start to cooperation and partnership with national auditing standard setters. A number of important collaborative efforts and joint projects have come from this initiative, including the joint task force with the U.S. Auditing Standards Board (ASB) on the Audit Risk and Using the Work of an Expert projects and two new projects with the U.K. Auditing Practices Board (APB): Materiality and Audit of Estimates Involving Measurement Uncertainty. Clearly, such close cooperation will be the most promising way of working on worldwide convergence of standards and acceptance of the IAASB as the leading authority for global auditing and assurance standards.

The objective of the next meeting, scheduled for early 2003, is to further improve the working relationship between national standard setters and the IAASB and to explore additional opportunities for closer collaboration on projects as well as options to improve

processes, particularly for those standard setters not directly represented on the IAASB.

Communications

The way in which IAASB activities are communicated and its pronouncements are disseminated continued to be challenged and enhanced. The IAASB created a new web site within the IFAC structure to contribute to the transparency of its operations and increase awareness of its work program. The site features expanded information on IAASB projects, enables visitors to register online to attend IAASB meetings, and includes background papers and agendas for its meetings. Since the site was launched in March 2002, it has attracted over 28,700 visitors, more than triple the number that visited the previous site on IFAC's auditing activities. Additionally, close to 2,600 IAASB documents were downloaded from the site in 2002.

Member bodies are encouraged to promote IAASB guidance to their members and can include links from their web sites to the IAASB's. All IAASB pronouncements are available free of charge in electronic form through the IFAC web site effective January 1, 2003. We also, for the first time, will be offering our 2003 IFAC IAASB Handbook in a CD-Rom format which will be available in early 2003.

Building on Change

It has been a year of tremendous change. I would like to acknowledge the dedication, cooperation and support demonstrated by my fellow Board members and by their technical advisors, by IAASB technical staff, by member bodies and the CAG, by national standard setters, and by all stakeholders that have helped the IAASB in meeting its objectives.

Looking forward, we have adopted an ambitious program to move further ahead on these strategic initiatives – initiatives that we hope will see achievement of IAASB's mission –

to establish high quality auditing, assurance, quality control and related services standards and to improve the uniformity of practice by professional accountants throughout the world, thereby strengthening public confidence in the global auditing profession and serving the public interest.



Dietz Mertin
Chair



Technical Director's Report



James M. Sylph
Technical Director

Our focus is on developing and issuing quality auditing and assurance standards that are sufficiently specific, understandable and definitive to influence and guide the judgments of auditors in designing and carrying out their work. They are to be comprehensive in scope and establish a worldwide benchmark for the performance of high quality audits.

The action plan of the IAASB for the next two years is driven by our principal and overall goal, which is to develop high quality standards in our capacity as the global auditing and assurance standard setting authority. Of immediate importance, however, is to review and update our set of standards with due regard towards 2005 when ISAs will be the basis of the audit in Europe. To this end, we are conscious that this effort needs to be properly balanced with other projects necessary to provide timely standards and guidance addressing issues relevant to the international marketplace.

Achievements

Over the last year, the IAASB has continued to respond diligently to the wide-ranging needs of its stakeholders. It has issued three new standards and guidance in final form, including a new ISA on auditing fair value measurements and disclosures, released four new ISAs for public exposure, and has a number of significant projects currently underway.

Exhibit 3 contains a description of IAASB standards and guidance issued in 2002 and other 2002 and 2003 priority projects.

Three of the IAASB's most significant projects in progress are the recently exposed Audit Risk standards, new Quality Control standards, and revised standards for Assurance Engagements – projects that, respectively, will significantly drive change in auditor behavior, enhance quality control processes and expand service capability. These three projects are discussed below.

Audit Risk

Our most ambitious and highest priority project today is the completion of the Audit Risk project, a comprehensive review and update of our core auditing standards.

Recent changes in the business environment have included the way entities are organized and conduct their businesses, the effects of globalization and technology, and significantly increased pressures that may lead to fraudulent financial reporting. In light of these changes, the IAASB embarked on a project to address one of the most critical issues facing the accountancy profession today and those it serves: audit risk. In close partnership with the U.S. Auditing Standards Board (ASB), the IAASB reviewed its core auditing standards that address various aspects of audit risk, and as a result, has released exposure drafts of three new ISAs:

- *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement;*
- *The Auditor's Procedures in Response to Assessed Risks;* and
- *Audit Evidence.*

In addition, the IAASB is proposing an Amendment to ISA 200, *Objective and General Principles Governing an Audit of Financial Statements*.

The new proposed ISAs are designed to enhance the auditor's implementation of the audit risk model and ultimately improve auditor performance. They require the auditor to have a deeper understanding of an entity's business environment, to make risk assessments on all audits and to link the nature, timing and extent of audit procedures to the assessed risks. The requirements and guidance related to internal control have been substantially increased including specification of the components that comprise internal control, the extent of the required understanding of each of the components of internal control, and the

The IAASB believes the proposed ISAs will:

Increase audit quality as a result of better risk assessments and improved design and performance of audit procedures to respond to the assessed risks.

Improve linkage of audit procedures and assessed risks, resulting in a greater concentration of effort on areas where there is greater risk of misstatement of the financial statements.

Result in an overall increased work effort by the audit team, particularly for new engagements or when first implemented on continuing engagements.

Require new skills and competencies to implement, and may increase the need for specialist assistance on audits.

auditor's procedures to obtain an understanding of internal control.

Given the extensive changes contemplated under the proposed standards of the Audit Risk project, revisions to existing ISAs are underway to ensure consistency and conformity with the concepts and terminology of the proposed new standards. The IAASB will continue to work on these conforming changes during the exposure period.

These draft standards were exposed for public comment in October 2002. Because of the importance of this project, the exposure period has been extended from the customary three to five months, with the final approval of these three main standards planned for the end of 2003.

Careful consideration of the future curriculum and training of audit staff has to follow. An effective date of these standards will be set to provide the profession enough time for a thorough implementation and training period.

Quality Control

This project will revise ISA 220, *Quality Control for Audit Work*, to establish standards and guidance on the quality control policies and procedures that firms performing audit and assurance engagements should put in place. The project will develop standards in two parts:

- A quality control standard (ISQC 1) setting out the responsibilities of firm-wide quality control for engagements that fall within the scope of IAASB engagement standards, forming the first of a new series of International Quality Control Standards.
- A revised ISA 220, *Quality Control for Audit Work*, that provides engagement-related standards for audits of financial statements, with specific requirements for an independent reviewer to perform an objective evaluation of the compliance of a relevant engagement with applicable professional standards, including the appropriateness of the report, for public entities and others where considered appropriate.

Ultimately, the goal is to establish engagement-level standards for all engagements that fall within the scope of the IAASB engagement standards.

The IFAC Board, working closely with the IAASB, is concurrently developing a new proposed document, *Statement of Member Obligations No. 1*, to provide guidance on quality assurance at the level of IFAC member bodies.

The IFAC Board and the IAASB believe that issuing the three documents simultaneously is necessary to clarify both the overall quality control activities and responsibilities of IFAC member bodies, accounting firms and engagement teams and the manner in which the three documents interrelate. An exposure draft of these documents is expected by the middle of 2003.

Assurance Engagements

ISA 100, *Assurance Engagements*, establishes basic principles and essential procedures for professional accountants in public practice who perform audit-level assurance engagements on a range of subject matters far broader than financial statements. With the recent publication of the findings from the IAASB commissioned research on the determination and communication of levels of assurance other than high, the IAASB has started to revise ISA 100 to include basic principles and essential procedures for review-level assurance engagements.

Under the current project plan, ISA 100 will be split into two documents: a *Framework for Assurance Engagements* that sets out the underlying concepts, definitions and elements of an assurance engagement; and ISAE 2000, *Assurance Engagements*, which establishes the basic principles and essential procedures for, and provides guidance to, the performance of assurance engagements on subject matters other than historic financial information.

This project is particularly important in today's environment as demand for such services continues to grow. It will provide a comprehensive framework for the development of future assurance standards on specific subject matters or topics.

An exposure draft of a revised ISA 100 and ISAE 2000 is expected to be released by the middle of 2003.

Meeting Future Challenges

The combination of our current projects and new projects approved for 2003 and those in the "pipeline" represents a demanding work plan and timetable. Undoubtedly, there will be challenges – challenges, however, that only come from such an important mandate.

During the year, we undertook a worldwide search to increase the depth and quality of staff resources to better serve the greater demands

of the IAASB and the expectations of our stakeholders around the globe. This team brings together many years of experience in auditing and assurance standard setting from such diverse environments as Australia, Canada, Hong Kong, New Zealand, South Africa, and the United Kingdom.

I thank them for their support of the IAASB and me. I am confident that our team is well positioned to meet the objectives of the IAASB. Finally, my thanks to the Board members themselves for their support and counsel during a year of unprecedented challenge to our profession.

James M. Sylph

James M. Sylph
Technical Director



Exhibit 1: IAASB Members, Technical Advisors and Technical Staff

As at December 31, 2002

Board Members

Dietz Mertin (Chair), *Germany*
Denise Esdon (Vice-Chair), *Canada*
Philip Ashton, *United Kingdom*
John Archambault, *United States*
Roger Dassen, *Netherlands*
Ana Maria Elorrieta, *Brazil*
Jan Bo Hansen, *Denmark*
Gen Ikegami, *Japan*
Suresh Kana, *South Africa*
John Kellas, *United Kingdom*
Edmund R. Noonan, *United States*
Ian Plaistowe, *United Kingdom*
Roberto Tizzano, *Italy*
Gérard Trémolière, *France*
Yang Zhiguo, *China*

Public Members

Denis Desautels, *Canada*
Ian McPhee, *Australia*
Roger Simnett, *Australia*

Technical Advisors

Wolfgang Böhm, *Germany*
George H. Tucker, *United States*
Diana Hillier, *United Kingdom*

Hans Verkruijsse, *Netherlands*

John Fogarty, *United States*
Yuichi Yamamoto, *Japan*
Karen Lauf, *South Africa*
Sylvia Smith, *Canada*
Susan Jones, *United States*
Jon Grant, *United Kingdom*
Emilio Palma, *Italy*
Cédric Gélard, *France*
Xi Wu, *China*

Paul Lohnes, *Canada*
Richard Mifsud, *Australia*

IAASB Technical Staff

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Exhibit 2: Consultative Advisory Group Members



The Consultative Advisory Group (CAG) is seen as an integral and important part of the IAASB's work structure. At present, CAG has the following members:

Association for Investment Management and Research
Basel Committee on Banking Supervision
Council of the Bars and Law Societies of the European Union
European Banking Federation
European Commission
European Federation of Accountants and Auditors for SMEs
European Federation of Financial Executives' Institutes
European Federation of Investment Funds & Companies
European Financial Reporting Group
European Savings Banks Group
Fédération des Experts Comptables Européens
Federation of European Stock Exchanges
Information Systems Audit and Control Association
Institute of Internal Auditors
International Accounting Standards Board
International Actuarial Association
International Association of Insurance Supervisors
International Bar Association
International Monetary Fund
International Organization of Securities Commissions
International Organization of Supreme Audit Institutions
United Nations Conference on Trade & Development
World Bank
World Federation of Exchanges

Exhibit 3: IAASB Standards and Guidance: 2002 Achievements, Projects in Progress and 2003 Projects

In addition to the Audit Risk, Quality Control and Assurance Engagement projects discussed in the Technical Director's Report, the following standards and guidance were issued, are in progress of development, or under consideration by the IAASB. Additional information on these standards and guidance and IAASB projects can be found on the IAASB web site at www.iaasb.org.

2002 Achievements

Approved and Issued

- **ISA 545, Auditing Fair Value Measurements and Disclosures**, which responds to the increasing prevalence of complex accounting pronouncements containing measurement and disclosure provisions based on fair value. This new ISA addresses audit considerations relating to the valuation, measurement, presentation and disclosure for material assets, liabilities and specific components of equity presented or disclosed at fair value in financial statements. This ISA is effective for audits of financial statements for periods ending on or after December 31, 2003. Recognizing the important need for guidance in this area, the U.S. ASB has used this ISA as its basis in issuing an exposure draft on the same subject within the U.S.
- **IAPS 1013, Electronic Commerce – Effect on the Audit of Financial Statements**, which responds to the increasing use of the Internet for business-

to-consumer, business-to-business, business-to-government and business-to-employee e-commerce and how emerging new elements of risk need to be considered when planning and performing the audit of financial statements. This new IAPS helps auditors address e-commerce issues by focusing on, among other matters, the level of skills and knowledge required to understand the effect of e-commerce on the audit; the business, legal, regulatory and other risks faced by entities engaged in e-commerce activities; internal control considerations, such as an entity's security infrastructure and transaction integrity; and the effect of electronic records on audit evidence.

- **IAASB Study 1: The Determination and Communication of Levels of Assurance Other Than High**, which was commissioned by the IAASB and conducted by an international network of auditing academics, is an extensive study of the determination and communication of levels of assurance other than high. The accurate determination and effective communication of levels of assurance provided in assurance engagements are critical issues for the future development of assurance services. The information contained in this study, which consists of an extensive literature review of related initiatives within and outside the profession, accompanied by two empirical studies, is important input for decision making by standard setters regarding the determination and communication of levels of assurance.

Approved for Public Exposure

- **Compliance with International Financial Reporting Standards** – With the increasing use of International Financial Reporting Standards (IFRSs), formerly known as International Accounting Standards (IASs), there have been situations where reporting entities under a different financial reporting framework have stated that their financial statements comply with IFRSs when, in fact, they do not comply with all of the

requirements of the IFRSs. This includes situations where an entity uses wording such as “The accounting policies used meet substantially all the requirements of International Accounting Standards” as well as situations where an entity lists its accounting policies and asks its auditor to report in terms of compliance with IFRSs.

The IAASB intends to issue an IAPS providing guidance for auditors on what to do in such circumstances. This draft statement is in exposure for public comment at the time of issuance of this publication.

In Progress

The IAASB is currently working on a number of projects and initiatives, the majority of which are planned to be exposed for public comment during 2003.

- **Considering the Work of Other Auditors** – This project intends to establish revised standards on considering the work of other auditors in the context of the audit of consolidated financial statements presented by a parent company. In particular, the project will revise existing ISA 600, *Using the Work of Another Auditor*, and addresses considerations relating to ethical requirements, auditing and quality control standards to be used and communicated by the principal and other auditor, and the nature and extent of work to be performed when using the work of another auditor.
- **The Audit of Group Financial Statements** – Closely related to the project on considering the work of other auditors noted above, a new IAPS providing guidance on the application of existing ISAs to the audit of group financial statements is also being developed.
- **Update of IAPS 1005, *The Special Considerations in the Audit of Small Entities*** – With the number of new standards and statements recently issued, work on revising and updating IAPS 1005 is underway to ensure its applicability and

relevance to small- and medium-sized practitioners

- **Review of Interim Financial Information** – This project intends to establish standards and provide guidance for auditors who review the interim financial reporting of audit clients required or allowed by legislation or regulation to issue interim financial information to shareholders. An exposure draft of this standard is expected to be released by the middle of 2003.
- **The Auditor’s Report** – This project aims to revise ISA 700, *The Auditor’s Report on Financial Statements*. The project will address a number of issues regarding the guidance in the ISAs on the form and content of the auditor’s report in an audit of financial statements and in other types of engagements.
- **Materiality** – This project intends to update the standards and guidance in ISA 320, *Audit Materiality*. The project is being undertaken jointly with the U.K. APB and will address issues such as qualitative factors that affect materiality, encouraging correction of identified misstatements, evaluating materiality of individual misstatements with respect to qualitative and quantitative factors, and reporting responsibilities.
- **Audit of Estimates Involving Measurement Uncertainty** – This project intends to revise ISA 540, *Audit of Accounting Estimates*. The project will provide a risk-based approach to assessing accounting estimates, including consideration of how accounting estimates may be affected by management motivation and “earnings management.” This project also is being undertaken jointly with the U.K. APB and is closely linked to the new project on materiality.

Looking Ahead – 2003 Projects

- **Using the Work of an Expert** – The IAASB has recently reviewed ISA 620, *Using the Work of an Expert*, and believes it should

be revised now because a number of other standard setters are developing guidance on the coverage of experts employed by audit firms and treatment of employee auditors with special skills. Initially, this project will focus primarily on developing a revised standard covering only the audit of financial statements. Considerations that will be addressed when further developing this project include:

- whether experts employed by an audit firm should be covered by this standard or the standard addressing quality control, or both;
- whether employee auditors with special skills are “experts”;
- whether undertaking additional audit procedures or seeking audit evidence from another expert should be mandatory if an auditor is concerned about the competence or objectivity of an expert;
- the circumstances, if any, in which an expert can be referred to in an auditor’s report; and
- standards and guidance on using an expert in all phases of an audit.

This project will be undertaken jointly with the U.S. ASB.

- **Fraud** – This project is to update ISA 240, *The Auditor’s Responsibility to Consider Fraud and Error in an Audit of Financial Statements*, which establishes standards and provides guidance on the auditor’s responsibility to consider fraud and error in a financial statement audit.

The IAASB plans to converge ISA 240 with the principles in new SAS 99, *Consideration of Fraud in a Financial Statement Audit*, issued by the U.S. ASB in September 2002, subject to any differences to take into account the international environment, and to conform ISA 240 to the guidance in the proposed Audit Risk standards. In addition, the proposed output of this project is an ISA that deals only with fraud, rather than its

current emphasis on the auditor’s responsibility to detect fraud and error. This will give greater emphasis to fraud and will permit the standard to focus on the specific characteristics of fraud.

- **Audit Planning and Supervision** – A revision of the existing ISA on these matters in light of the developments in the Audit Risk project, including the expansion of guidance on the allocation of work to, and supervision of, those engaged in an audit.
- **Documentation** – A revision to current ISA 230, *Documentation*, to strengthen the standards and guidance pertaining to, among others, the nature and extent of matters to be documented and working paper considerations. The project will take into account recently developed and revised standards issued by other standard setters, as well as the suggestions for improvement provided by IOSCO.
- **Comfort Letters** – The IAASB has charged an IAASB member to establish a group of international experts to conduct research and to develop a “white paper” on the auditor’s involvement in and responsibilities for letters provided to underwriters/investment bankers for public or private offerings. The envisioned “white paper” would be used to seek the views of key stakeholders on national and international issues pertaining to this subject.

Projects to complete standards for assurance engagements on sustainability reporting, prospective financial information and reporting on internal controls – topics of importance in today’s business environment and of interest to regulators and market participants – are being considered for further development.

In addition, the IAASB is monitoring developments on the topic of continuous auditing with a view to consider this subject for a joint project with national standard setters and academics. IAASB involvement is to be determined, depending mainly on the availability of resources.



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