

21 September 2009

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Our ref: KC/TP/ASB/09.09

Your ref:

Dear Sirs

Response to APB Consultation Paper on Practice Note 26 – Guidance on Smaller Entity Audit Documentation (Revised)

Following the issue of your exposure draft of a revised version of Practice Note 26 – Guidance on Smaller Entity Audit Documentation, we are writing to express our views on the proposed amendments following the APB decision to adopt the Clarified ISAs for accounting periods ending on or after 15 December 2010.

Overall, we consider that the guidance contained in the Practice Note is helpful for auditors in understanding the level of documentation which is required on the audits of smaller entities in order to comply with the Clarity ISAs, and clarifying that such documentation, whilst necessarily requiring a certain amount of detail, does not need to be overly voluminous. Release of the Practice Note concurrently with the Clarity ISAs will certainly help mitigate implementation issues for smaller entity audits.

As another general point, although the examples of substantive audit work papers are useful, it would be helpful if additional guidance notes could be given (perhaps in italics) to the extent that the level of documentation will necessarily vary depending on the circumstances of the entity and the risks relating to a particular audit area.

We have commented specifically on some of the examples in turn below.

Example 1 and 2 – The Audit Strategy Memorandum

ISA 570 paragraph 2 states that when planning the audit the auditor should consider the appropriateness of management's use of the going concern assumption in the preparation of the financial statements. However the audit strategy documented in example 1 does not refer to certain key risks for a business such as going concern and the consideration of fraud. Because of the current economic situation, going concern is likely to be a key risk for many entities and in our opinion this should be included in the example in the risk assessment section.

We would also note that it should be made clear that the materiality level of 5% of profit used in example 1 is illustrative and that materiality will necessarily vary depending on the entity, its circumstances and (potentially) the methodology of the auditor.

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Example 3 – understanding the business

This example refers to the company (a small hotel business) having non-executive directors. In practice it is extremely unlikely that a small entity will have non-executive directors (except potentially connected persons, such as family members) and we would suggest that the example is re-written accordingly. Similarly in example 6 there is a reference to a non-executive director reviewing the bank reconciliation; it is (in our experience) highly unlikely a non-executive director would perform this role in practice.

Example 10 – Audit Working Paper: Property Valuation

Example 10, which gives an example of a substantive audit working paper, is useful particularly as there was no parallel example in the previous Practice Note. The choice of property valuation as the subject of the example is also topical. Again however there is a reference to a non-executive director. In order to address the point made above without losing the continuity of the examples, the non-executive directors could instead be minority shareholders (as might occur in reality were they to be, for instance, friends of the family which operates the business).

Example 11 – Audit Working Paper: Going Concern

We agree that an example work paper for going concern should be included in the Practice Note given current economic conditions and that the example will be useful for auditors in determining the necessary level of documentation in this area. However, a guidance note stating that the level of documentation required will potentially vary depending on the level of uncertainty over going concern and the quality of audit evidence available would be useful. This is particularly important where, for instance, an emphasis of matter paragraph may be required.

Example 12 – Evaluation of Misstatements identified during the audit

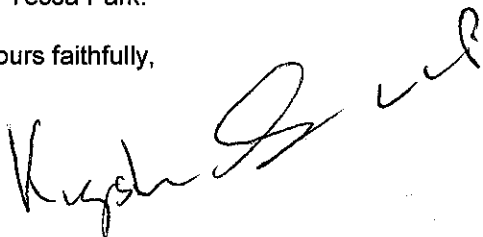
This is a new example introduced in the revised Practice Note and should be useful in ensuring that the adjusted and unadjusted errors and their effect on the 'bottom line' are documented on the audit file and concluded on. Again, a guidance note that the level at which potential adjustments are considered 'clearly trivial' will vary depending on the assignment, would be useful.

Conclusion

The additional examples and amendments are informative and should be included in the revised Practice Note 26. The only significant issue relates to going concern being omitted from the Planning Strategy Memorandum. We would suggest that this should be included in the example due to its importance and current relevance.

Should you have any questions on this letter, then please do not hesitate to contact Peter Holgate or Tessa Park.

Yours faithfully,



Kingston Smith LLP