



THE INSTITUTE
OF CHARTERED
ACCOUNTANTS
IN ENGLAND AND WALES

30 September 2009

Our ref: ICAEW Rep 111/09

Your ref:

Hazel O'Sullivan
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The Auditing Practices Board
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Dear Ms O'Sullivan

Practice Note 26 (Revised): Guidance on smaller entity documentation

The Institute of Chartered Accountants in England and Wales (the Institute) is pleased to respond to your request for comments on the the Exposure Draft of *Practice Note 26 (Revised): Guidance on smaller entity documentation*.

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

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ICAEW REP 111/09

PRACTICE NOTE 26 (REVISED): GUIDANCE ON SMALLER ENTITY AUDIT DOCUMENTATION

Memorandum of comment submitted in September 2009 by The Institute of Chartered Accountants in England and Wales, in response to the Auditing Practices Board Exposure Draft published in July 2009

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INTRODUCTION

1. The Institute of Chartered Accountants in England and Wales (the Institute) welcomes the opportunity to comment on the consultation paper *Practice Note 26 (Revised) - Guidance on smaller entity audit documentation* published by the Auditing Practices Board.

WHO WE ARE

2. The Institute operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 132,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 775,000 members worldwide.
3. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The Institute ensures these skills are constantly developed, recognised and valued.

MAJOR POINTS

4. The Institute welcomes the proposed revised Practice Note. We consider that the guidance is helpful, particularly the examples, which include alternative approaches to different situations. We believe that it should help practitioners to avoid unnecessary documentation, which in the context of smaller entity audits adds disproportionately to the cost of the work.
5. The Institute also supports the proposed timing of publication, to coincide with the issue of the 'clarity' International Standards on Auditing (UK and Ireland). This will enable auditors to undertake professional development to become familiar with the revised requirements, and prepare in good time for implementation at the end of next year. We recommend that the APB explain this context in the press release that will accompany publication of the revised Practice Note.
6. One point on which an example might usefully be added is illustration of the general requirement to document significant matters arising during the audit, the conclusions reached on these, and the significant professional judgments made in reaching the conclusions. In our experience, this is often dealt with too late in the audit, thus weakening the effectiveness of the work. It would also be helpful to illustrate documentation of significant matters and auditor conclusions thereon in the context of group audits.

RESPONSES TO SPECIFIC QUESTIONS

"APB is now seeking views on the proposed updates to Practice Note 26 and in particular on whether the new illustrative examples properly reflect the requirements of the proposed ISAs (UK and Ireland) and are a realistic illustration of appropriate audit documentation? If not, how should the examples be amended?"

7. We consider that the new illustrative examples are very useful. However, they are necessarily artificial, and the scenarios rather more straightforward than many smaller entities encountered by auditors in practice. It might be helpful to add guidance in the text to the effect that some situations might require more documentation, such as entities where there is no segregation of duties, close control by a dominant director and lots of cash in and out.

8. Example 3 includes the information that the company has non-executive directors, including a qualified accountant and a qualified property surveyor. We do not consider that it is realistic for an entity that employs only a part-time bookkeeper (example 6) to have non executive directors – or at least to describe those who do not participate in day-to-day management as such. We recommend that the notes under ownership and governance and control environment be changed along the lines that family members/friends who are investors in the company but not involved in day to day management include a surveyor and an accountant. In example 6, it is more likely that a director responsible for day to day management would review the bank reconciliation, rather than someone less closely involved in the business.
9. Example 1 uses a materiality example of 5% of profit. It needs to be made clear that the appropriate measure of materiality for the financial statements as a whole will vary according to the circumstances of each entity, and that 5% of pre-tax profit might be too low in some cases, or too high in others.

OTHER POINTS

10. We agree with the sentiment in paragraph 2 that the guidance is useful to entities that are exempt from audit but that have voluntarily submitted their accounts to audit. However, we think that this might unduly discourage use of the guidance by auditors of other simple entities, including charities and small subsidiaries of groups that are ineligible for audit exemption. We therefore suggest merging paragraphs 2 and 3 to make this point. .
11. We believe that it would be helpful to include an example of documentation for the ethical considerations arising from the 'special relationship' between smaller entities and their auditors (paragraphs 27 to 29), perhaps with reference to APB Ethical Standards – Provisions Available for Small Entities.

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