

## MINUTES

**MEETING OF:** THE AUDITING PRACTICES BOARD

**DATE AND TIME:** Thursday 11<sup>th</sup> March 2010 at 9.30am

**PLACE:** Aldwych House,  
71-91 Aldwych,  
London WC2

**PRESENT:**

**Members**

R Fleck (Chairman)	I Pickering
Ms A Coates	M Powell
R Frith	D Thomas
M Grabowski (Executive director)	S Turley
J Grant	A Wilson

**Observers**

J Bellingham (UK, Department for Business, Innovation and Skills)  
I Drennan (Irish Auditing and Accounting Supervisory Authority)  
D Loweth (ASB)  
R Thorpe (Financial Services Authority)

**In attendance**

J Dean (for item 6)

**Staff**

K Billing	Mrs H O'Sullivan
S Leonard	

**ABSENT:**

**Members**

J Hughes	G Pimlott
P Lee	T Troubridge
R Nolan	M Ward

## **1. Introduction**

The Chairman introduced Mr Marek Grabowski as the new Executive Director of APB. The former Executive Director, Mr Jon Grant, will continue to be involved with APB as he is continuing as the UK representative on IAASB.

### Recent meetings

Mr Jon Grant reported that a recent EC ISA sub-group meeting had been cancelled and no further meetings are yet scheduled. There is a concern that the process for adoption of ISAs in the EU will be somewhat delayed.

The Improving the Audit Report Working Party has met a number of times and members of staff recently briefed a meeting of the Corporate Reporting Action Group (CRAG), an investor group, on the direction that the working party's discussions were taking. Members of CRAG expressed support for the approach being taken and the staff undertook to update them on further developments in the autumn.

### Other matters

The Chairman reported that the European Parliament had recently approved changes to EU accounting rules to allow member states to remove the requirement for micro-entities to produce annual accounts. Further substantive legislative steps are necessary before these changes can be given effect.

A review is to be undertaken on the effectiveness of each operating body for the new FRC Chairman. The Chairman proposed that the most recent Board evaluation be circulated to Board members for comment and this would then be updated in order to provide the status report.

## **2. Minutes of previous meeting**

The minutes of the meeting held on 15<sup>th</sup> December were approved.

## **3. Ethics**

Mr Jon Grant explained the context of the paper that had been circulated to the Board. No conclusions had been reached on any subject, but it was clear that there was further work to be done in some areas. The aim at this stage was simply to set out a roadmap for such work.

Two areas for improvements identified by respondents were to look again at disclosures about non-audit services made by audit committees (in particular explaining what their policy on non-audit services is and why they decided to buy particular services from their auditor) and at the categorisations used in regulations on disclosure of auditor remuneration (where it would be useful to tie together these categorisations with those used in ES 5). Additionally there was a suggestion by some investors that further work should be done on internal audit and restructuring services. The proposal is that issues papers on these subjects will be provided for the April APB meeting. It was acknowledged that the workplan is consequently very challenging.

In discussion Board members raised the following points:

- A clearer analysis of what each of the different groups of respondents said on each issue is needed. It was agreed that a more detailed summary would be circulated to Board members.
- Caution was advised on doing too much work on comments on particular matters that were raised by only one or two individuals, although it was also recognised that the merit of each suggestion should be considered, rather than just the volume of comment on a particular topic.
- The AIU inspection findings over the past year also need to be incorporated into this work and there will be an opportunity for a report to be made on this at the April meeting.
- It will be important that we keep up to date with other work being done by other parties (for example, auditor independence is being considered in some work currently being undertaken by the FSA).

#### **4. UK Corporate Governance Code**

Mr Marek Grabowski introduced a discussion of the changes that were being proposed to the UK Corporate Governance Code and the implications of these changes for the position that the APB had adopted in the past with respect to the auditor review requirement in the FSA's Listing Rules. He noted that staff had met recently with representatives of the FSA who indicated that they would be undertaking a limited and informal review of the corporate governance arrangements under the Listing Regime.

The purpose of the Board discussion was to seek to establish what the views of the current APB are on a number of questions relating to the auditor's role with respect to reports on corporate governance in annual reports so as to inform the FSA as part of their review.

The APB confirmed that it continues to believe that the requirement relating to eight of the nine Code provisions to be reviewed by the auditor have little merit. The Code provision that the APB believes should continue to be reviewed by the auditor is that relating to internal control because this is an area where the auditor ought to be able to provide meaningful assurance. However, it was recognised that removal of any requirements at this time would be seen as a weakening of regulation and that this may be difficult for the FSA to justify unless new requirements for auditor involvement could be introduced that would be perceived as being beneficial for investors.

It was agreed that the description of the auditor's role in terms of 'review' should be improved by the use of an alternative term. The APB did not conclude as to what the term should be but a number of Board members expressed support for the use of 'consider'.

It was suggested that reporting in terms of 'consistency with the knowledge of the auditor' may meet the objective of adding more value to the assurance provided by the auditor on corporate governance matters. However, one Board member cautioned that with respect to internal control that this may be a slippery slope to a SARBOX style of reporting.

The Board discussed whether there should be auditor involvement in the proposed new accountability provision relating to the business model and risk management processes. Although no consensus was reached some Board members expressed reservations about the merits of the auditor reporting on these matters. With respect to the “business model” it is unclear what is meant by this term and in the opinion of one Board member the expression is too bland for an auditor to provide meaningful assurance. With respect to risk management processes there seemed to be a clear linkage with internal control reporting. One Board member, however, commented that considerable misunderstandings could be created where auditors have legitimately adopted a substantive audit approach.

The Chairman summarised the implications of the discussion by commenting that at the moment different requirements are picked up by legislation, regulation and ISAs (UK and Ireland) creating a difficulty in practice. It may be possible to explain that proposed changes are aimed at simplifying things by bringing consistency to the form of reporting set out in different requirements. He concluded the discussion by noting that rather than the APB discussing these issues in isolation, there should be a wider discussion within the FRC before progressing this further.

#### **5. Update on plan to revise Practice Notes**

Mr Jon Grant explained that this item was for information only. The APB noted that some anticipated dates for the issuance of exposure drafts had changed.

#### **6. Revision to Practice Note 20 – a proposed exposure draft**

Mr James Dean, Chair of the ICAEW Insurance Committee, explained that the proposed exposure draft of a revision of Practice Note 20 on Insurance had been prepared to reflect the Clarity ISAs (UK and Ireland) and changes that had been made to legislation. No additional guidance was thought to be necessary as a result of the financial crisis.

In discussion on the ‘equalisation provisions’ that are included in financial statements prepared under UK GAAP it was noted that their disclosure in the auditor’s report (currently contained in the basis of opinion paragraph) highlights the existence of the provision and is primarily a message about the accounting framework. It was agreed that it would be inappropriate for the equalisation provision disclosure to be included as an emphasis of matter paragraph because the paragraph is not intended to highlight a problem or ring an alarm bell for the reader of the auditor’s report. It was suggested that the PN20 working party should consider the Board’s preference that the disclosure be included in the first paragraph of the auditor’s report where the accounting framework is described.

It was agreed that a revised draft of the proposed revised Practice Note would then be circulated for final approval for a three month exposure period.

#### **7. Practice Note 12 – Money Laundering**

Mrs Hazel O’Sullivan outlined the background to the current version of this Practice Note. It was agreed that due process should be followed and the Practice Note should be issued as an exposure draft prior to its finalisation. The accompanying press notice would state that the APB does not believe that there are any substantial changes and

that therefore HM Treasury will not be asked to reapprove the document following the exposure period.

#### **8. Status of IAPSs**

Mr Jon Grant explained that, although it was intended that IAASB would withdraw current IAPSs, work on complex financial instruments means the status of IAPSs nevertheless needs to be clarified. In discussion it was thought that the material should be no stronger than application material in the ISAs. There need to be tough criteria used to determine the need for such guidance, including that it should be genuinely international in applicability and expected to be applicable for a long period of time.

#### **9. Internal audit**

Mr Jon Grant explained that while the Exposure Draft of a revised ISA was not being approved at the forthcoming IAASB meeting, this was likely to be the main chance to influence its direction. It was agreed that enquiry of internal audit should always happen as part of an audit. The level of reliance on internal audit will depend on the subjectivity of judgments made by internal audit and the level of risk associated with the areas concerned. The independence of the internal audit function within the organisation is critical to the extent of reliance that can be placed on its work.

#### **10. Pro formas**

Mr Jon Grant explained that an Exposure Draft of ISAE 3420, which is an international version of SIR 4000, was expected to be approved at the forthcoming IAASB meeting. The Board had briefly discussed an earlier draft at its November 2009 meeting and the SIRs working party had also met to discuss earlier drafts. Mr Grant expressed the view that the latest draft addresses satisfactorily a number of the concerns that had been expressed with respect to earlier drafts. He commented that there would be a further opportunity for the Board to propose detailed changes to ISAE 3420 when it is exposed for comment by IAASB. On one detailed matter the Board agreed that IAASB should explore further the position in relation to prospective financial information.

#### **11. Next meeting**

It was noted that the next meeting of the Board will be held on Wednesday 21 April 2010 as part of the away day. In the meantime a draft of the APB Annual Report will be circulated to Board members for comment.