

## MINUTES

**MEETING OF:** THE AUDITING PRACTICES BOARD

**DATE AND  
TIME:**

Wednesday 12<sup>th</sup> May 2010 at 9.30am

**PLACE:**

Aldwych House,  
71-91 Aldwych,  
London WC2

**PRESENT:**

**Members**

J Adam	R Nolan
R Fleck (Chairman)	I Pickering
R Frith	R Sriskandan
M Grabowski (Executive director)	R Talbut
J Hughes	D Thomas
P Lee	M Ward

**Observers**

J Bellingham (UK, Department for Business, Innovation and Skills)  
Ms P Sucher (Financial Services Authority)

**In attendance**

Ms K Cearns P George

**Staff**

J Grant Mrs H O'Sullivan  
S Leonard

**ABSENT:**

**Members**

Ms A Coates A Wilson  
S Turley

**Observers**

I Drennan (Irish Auditing and Accounting Supervisory Authority)

## **1. Introduction**

The Chairman welcomed new Board members.

Mr Grabowski explained that a recent press release from the EU had promised a Green Paper in the autumn to cover issues on the role and scope of audit such as the concentration in the audit market, small and medium sized practitioners, the audit of SMEs and international standards on auditing.

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

The minutes of the meeting held on 21<sup>st</sup> April were approved.

## **3. Ethics**

The Chairman explained that before the next meeting all of the issues papers would be combined into one document that would be used for consultation on proposed amendments. Each of the individual issues papers were dealt with separately as follows:

### Banding of non-audit services

In discussion it was agreed that guidance in the ESs should explain that the threats arising from audit related services were normally clearly insignificant meaning that safeguards were not required. It was agreed that work in connection with investment circulars would not be included in the list of audit related services as it was not necessarily the case that associated threats were clearly insignificant and there was also an element of choice associated with who would perform this work.

It was agreed that the feedback paper needed to emphasise that there is a wide range of services included in 'other non-audit services', including some that are uncontroversial.

### Audit committee involvement in non-audit services

The Chairman reported that revisions to the FRC Guidance on Audit Committees would be exposed at the same time as the feedback and consultation paper on the Ethical Standards.

The Board discussed the draft words relating to pre-approval and compared these to the US position. It was agreed that there would be merit in clarifying that in this context pre-approval was the approval, in advance, as a matter of policy rather than the specific approval of an engagement before it was contracted. It was also agreed that pre-approval of the use of the external auditor may be appropriate where the threats to auditor independence are considered low, for example if the engagement is:

- (a) routine in nature and the fee is very small in the context of the audit fee, or
- (b) for an audit related service.

### Extended and internal audit services

Mr Grant highlighted that internal audit services had always been an area where widely varying views were expressed and this had been highlighted further in 2009 by discussions on extended audit. The Board discussed proposed wording that provided a definition of the type of 'extended audit' services that should be classified as audit-

related services. It was agreed that more thought needed to be given to the treatment of subsidiary statutory audit fees.

In seeking to distinguish what was 'extended audit' from what might be considered as 'internal audit' it was thought that it was not only a timing issue that determined whether work should be classified as such, but the extent to which the work is an integrated part of the audit. Additionally, the terms and conditions of engagement should be the same as for the audit, but there does not necessarily need to be a separate engagement letter.

#### Impact of magnitude of non-audit services

It was thought that where an audit engagement partner was considering the threats associated with non-audit services, it was the magnitude of the total non-audit fees that should be considered and audit related services should not be excluded from this analysis.

#### Restructuring services

The Chairman indicated that an open consultation was proposed on this subject where two or three different options are set out. However, he noted that there was a growing recognition that where going concern is an issue for the audit, it is not a good idea for the auditor to be heavily involved in a restructuring plan.

In discussion it was thought that a graduated series of possible approaches should be consulted upon, recognising that there may be a wide range of services that could be provided to entities in distress, with some work that could be undertaken by the auditor with the application of safeguards and other situations where no appropriate safeguards are available to eliminate or reduce the threats to an acceptable level. The consultation paper should include a question on whether the same approach should apply to all entities or whether there should be a distinction for listed entities and/or smaller entities.

It was agreed that revised drafting on this subject would be circulated to Board members at the same time as it is circulated to the Ethics sub-committee.

#### Conflicts of interest

Mr Grabowski introduced the background to proposed new guidance paragraphs in respect of conflicts of interest. It was agreed that the inclusion of material in respect of competitors was too wide. However, it was agreed that there is a concern which is relevant to auditor independence in the case of services supplied to other parties which are inconsistent with the interests of the audited entity's stakeholders.

#### Contingent fees

Mr Grabowski summarised the concerns that have been expressed over the current definition of contingent fees. The proposed amended definition was agreed.

It was agreed that the threats associated with contingent fees are mostly associated with a perception that there is a mutuality of interest with management and the self-interest threat, particularly where the contingent element of the fee is significant. There was discussion about the relative extent of the threats in relation to corporate finance services and transaction services. There was also some discussion of the

impact of any further prohibitions on choice in the market place as prohibiting contingent fees in certain markets could in effect exclude the auditor from competing for such services for audit clients.

It was agreed that there should be an open consultation on the approach to be taken to contingent fees in the Ethical Standards and that consideration should be given to recommending the inclusion of some guidance material on this subject in the Guidance on Audit Committees.

#### Ethics Partners

The additional proposed guidance was agreed, although it was noted that the guidance on Ethics Partners not being part of the management team would be appropriate only in the case of firms that audit listed entities, since smaller firms would have difficulty in meeting this suggestion.

#### Threats and safeguards

The Chairman indicated that the additional guidance on threats and safeguards was being proposed in order to improve practice in this area. It was agreed that the guidance should suggest that both the individual and cumulative effects are considered at all stages when threats to auditor independence and objectivity are being considered. It was agreed that an additional paragraph could be added on situations where staff other than the audit engagement partner make approvals of non-audit services.

#### **4. Auditor's reports**

A discussion of the issues associated with this topic was deferred until a future meeting. In the meantime it was agreed that further example descriptions of the scope of an audit should not be developed, but that the examples which are included on the APB website should be made more generic. However, it was noted that a further example may need to be developed for use by public sector entities.

#### **5. Auditor scepticism**

It was agreed that this topic would be deferred until a future meeting, but in the meantime a smaller group would meet to discuss the issues raised in the paper.

#### **6. Practice Note 25 – Attendance at Stocktaking**

It was agreed that Board members would be asked to submit any comments and that approval of the Exposure Draft would be sought electronically.

#### **7. Letter to the Takeover Panel in response to Consultation on Profit Forecasts and other matters**

This letter was approved to be sent.

#### **8. Next meeting**

It was noted that the next meeting of the Board will be held on Tuesday 8<sup>th</sup> June.