

MINUTES

MEETING OF: THE AUDITING PRACTICES BOARD

DATE AND TIME: Tuesday 14 December 2004 at 9.00am

PLACE: Aldwych House
London WC2

PRESENT:

Members	R Fleck (Chairman)	I Plaistowe
	J Grant (Executive director)	M Powell
	J Beckerlegge	W Rainey
	Ms G Laver	D Thomas
	S Murray	T Troubridge
	K Nicholson	S Turley
	G Pimlott	

Observers G Innes/ Ms J Ford (UK Department of Trade and Industry)
D Loweth (ASB)
Ms P Sucher (Financial Services Authority)

In attendance	Ms K Cearns	S Takwani (for item 5)
	N Lerner (for item 5)	

Staff	K Billing	H Morgan
	S Leonard	Ms H O'Sullivan
	D Marston	

APOLOGIES:

Member L Hughes

Observer I Drennan (Republic of Ireland Auditing and Accounting Supervisory Authority)

1. Introduction

Publications

Mr Jon Grant noted that Bulletin 2004/3, giving guidance to reporting accountants on the Combined Code on Corporate Governance in the United Kingdom, had recently been issued, and that a version for use in the Republic of Ireland was to be issued shortly.

Mr Grant also noted the recent publication by the ASB of an exposure draft on the Operating and Financial Review. The ASB had also issued FRS 27 'Life Assurance' which, in the light of a Memorandum of Understanding between the ASB and the ABI, deferred proposals for reporting on 'realistic' liabilities in insurers' financial statements until the end of 2005.

IFAC Ethics

Mr Grant reported on a recent meeting of IFAC's Ethics Consultative Advisory Group to discuss that Group's future role. He noted that The IFAC Ethics Committee was planning to update the IFAC Code of Ethics and that he hoped APB would have an opportunity for participating in this work.

IAASB

Mr Ian Plaistowe reported on the meeting of the IAASB the previous week in New Orleans. He noted that exposure drafts of standards on materiality and accounting estimates had been approved, as had a draft revised ISA 700 on the auditor's report.

Investor views on audit quality

The Chairman noted that, as part of the auditor liability debate, investors and others were involved in discussions with the DTI in relation to audit quality. The NAPF had recently made written representations to the DTI, which included a proposal that the levels of materiality used by auditors should be disclosed in company financial statements. A copy of the representations would be circulated to Board members.

2. Minutes of previous meeting

The Chairman noted that the minutes of the meeting held on 23 November had recently been approved following circulation to Board members.

3. ISAs (UK and Ireland)

Mr Keith Billing introduced drafts of proposed ISAs (UK and Ireland) which had been amended to reflect both comments received during the consultation period and made by Board members at the November meeting. A proposed final draft of the revised statement on the APB's Scope and Authority of Pronouncements was also presented, together with a draft of ISQC (UK and Ireland) 1 and a proposed 'feedback' paper.

Board members made a number of detailed points on the drafts and, in response to a question raised by one member, it was reconfirmed unanimously that it was appropriate for the APB to embed supplementary standards and guidance within ISAs at this time. The Board voted unanimously for the ISAs (UK and Ireland) to be issued in final form, and the Chairman expressed his appreciation to members of the ISAs

Working Group, and particularly to Messrs Plaistowe and Hughes, for their efforts in developing these new standards.

4. IAASB consultation on Clarity

Mr Grant introduced a draft letter of comment to the IAASB on the consultation paper 'Clarifying professional requirements in international standards issued by the IAASB', an earlier draft of which the Board had discussed in October. While there was support for the approach adopted, a number of Board members thought that the style of the covering letter needed to be made more forceful. In particular further emphasis needed to be given to the likely adverse affects on audit quality of what appears to be a proposal to significantly increase the number of detailed procedural requirements within ISAs. It was agreed that an amended draft of the letter would be circulated for approval.

5. Ethical Standards

The Chairman reported on the most significant issues which had arisen from the consultation on ES – Exemptions Available for Small Entities, which concerned:

- economic dependency,
- safeguards needed to address the self-review threat when non-audit services, particularly tax and accountancy work, were provided to a small entity, and
- the reference to 'exemptions' from Ethical Standards in the audit report.

Mr Neil Lerner, Chairman of the CCAB Ethics Group, and Mr Sundeep Takwani, from ACCA, joined the meeting. They indicated that they had found the APB issues paper to be very useful, and commented favourably on the Board's consultation process. Mr Lerner noted that the extent to which accounting services were provided to entities with turnover in excess of £5.6m appeared to be more widespread than had first been thought and, as a result, the most problematic remaining issue concerned the approach to safeguards needed to address the self-review threat when accounting services were provided to entities that exceeded the APB definition of a 'small entity'. Possible solutions to this problem were to increase the size criteria for a 'small entity' or to introduce further transitional arrangements for those auditors already providing such services. Mr Takwani commented that ACCA wished a principles based approach to prevail; a degree of threat to auditor objectivity always exists and the safeguards required need to be proportionate. In his view the APB was not giving sufficient recognition to the safeguards that arise from professional qualification and training requirements. Messrs Lerner and Takwani responded to a number of questions from Board members and then withdrew from the meeting.

Board members discussed these issues and reached the following conclusions:

- concerning economic dependency, it was agreed that, other than in relation to listed companies, the 10% maximum limit on fees from one client should be increased to 15% . However such an increase in the case of companies with turnover of more than £5.6 million should only be allowed in cases where an external 'hot' review of the auditors' work was carried out. It was agreed that it was unnecessary to supplement these requirements with a 'de minimis' fee

amount which would add complexity to the Standards for little additional benefit;

- there was considerable debate regarding the self-review threat when tax and accountancy services were provided to a small entity. Some members of the Board took the view that while it was appropriate on cost / benefit grounds to exempt the auditors of small entities from the requirement to apply effective safeguards to address the self review threat, this should be flagged in the auditors' report as such. The majority of the Board, however, voted in favour of a proposal that safeguards in the form of 'informed management' and 'cold' reviews of a sample of audit engagements could be acknowledged as adequate in ES-PASE and in these circumstances a reference in the auditors' report would not be needed. The majority position was accepted by the Board as a whole only on the basis that over the next three years research would be undertaken to explore the viability of an alternative form of assurance for small entities in place of an audit. The Board was not prepared to extend this approach to the self-review threat to the audit of larger entities; and
- the Board concluded that, when the exemptions made available in ES – Provisions Available for Small Entities (ES-PASE) were utilised there was a need for a reference in the auditors' report although information relating to the circumstances could be provided in a note in the financial statements. The Board noted that the number of references to (ES-PASE) in auditors' reports was not expected to be large as this would arise from the relatively unusual circumstances of non-informed management, cooling off periods and tax tribunals.

It was agreed that a revised ES – PASE would be circulated shortly to Board members for final approval. In addition a small number of conforming and other changes to ES 1-5 were approved to ensure that the standards correctly reflected the Board's intentions at its October meeting. The Chairman expressed the thanks of the Board to the Ethics Working Group for its considerable efforts in bringing this project to a conclusion.

6. Mr Hugh Morgan

The Chairman noted that Mr Morgan finished his secondment to the APB staff at the end of the year, and thanked him for his work over the previous two years.

7. Next meeting

It was noted that the next meeting of the Board would be held on Tuesday 25 January 2005 commencing at 9.30am.

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