

## MINUTES

**MEETING OF:** THE AUDITING PRACTICES BOARD

**DATE AND TIME:** Tuesday 25 July 2006 at 9.30am

**PLACE:** Aldwych House  
London WC2

### PRESENT:

<b>Members</b>	R Fleck (Chairman)	K Nicholson
	J Grant (Executive director)	M Powell
	A Chambers	D Thomas
	L Hughes	T Troubridge
	R Nolan	S Turley
	G Pimlott	M Ward

**Observers** R Leyland (UK Department of Trade and Industry)  
R Thorpe (Financial Services Authority)

**In attendance** Ms K Cearns P Rowley (for item 6)

**Staff** K Billing D Marston  
S Leonard Mrs H O'Sullivan

### ABSENT:

**Member** W Rainey

**Observers** I Drennan (Republic of Ireland Auditing and Accounting Supervisory Authority)  
D Loweth (ASB)

## **1. Introduction**

### Regulatory strategy

Mr Jon Grant drew attention to the recently-published FRC report on the AIU's 2005/6 audit quality inspections. Copies were made available to Board members.

### IAASB meeting

Mr Grant reported on a meeting of the IAASB held the previous week in Brussels. He noted in particular that the working party on management representations was rethinking the rationale for obtaining representations on general management responsibilities. They now saw these more as assumptions underlying an audit which first needed to be established in audit engagement letter and then confirmed annually. Mr Grant also reported that IAASB had commenced a project to define material weaknesses in internal control. Although the project is at a relatively early stage he noted a personal concern that there was a risk that it could add to the complexity of the audit and be difficult for auditors, especially of SMEs, to apply.

### SME sub-committee

Mr Grant reported on a recent meeting of the APB's SME audit sub-committee, at which the ICAEW's proposed new review product (SEAS) was discussed. The sub-committee was not in favour of this project proceeding at present primarily as it was likely to cause confusion amongst companies and users of accounts as to how it differed from an audit. The APB shared this concern which it thought would compound the difficulties identified by the recent POBA review of how accountants support the needs of SMEs and their stakeholders. It was agreed that copies of the latest draft of the ICAEW proposals would be sent to Board members in due course.

### Bulletin 2006/5

The Chairman noted recent discussions concerning the wording of one paragraph in proposed Bulletin 2006/5 on corporate governance, which was otherwise ready for publication. The issue in question was the extent to which material weaknesses identified by auditors should be linked to the significant weaknesses to be considered by directors. The Chairman was discussing the matter with the Chairman of the Turnbull Review Group. In the event that it is thought appropriate to revise the wording in the Bulletin it would be circulated to the Board for approval.

### Conflicts of interest

The Chairman noted recent discussions within the FRC on possible conflicts of interest between operating boards. It was agreed that Board members would discuss activities that could present a conflict with the Chairman before agreeing to take them on.

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

The Chairman noted that the minutes of the meeting held on 27 June had been approved following circulation to Board members.

## **3. ESRA**

Mr Grant introduced a short paper describing, for information purposes, the main issues that had been raised by commentators on the ESRA exposure draft and the

working party's proposals as to how they should be addressed. He observed that it was intended that meetings would be held with bodies such as LIBA, the London Stock Exchange and the Takeover Panel to discuss the proposed changes to the draft ESRA before it is reconsidered by the Board at its September meeting.

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

Mr Steven Leonard introduced a discussion on Bulletin 2005/4: Auditor's reports on financial statements in Great Britain and Northern Ireland. He noted that since the Bulletin had been issued there had been changes in legislation relating to the auditor's report on the directors' report. It would therefore be necessary to update the Bulletin in the near future.

Mr Leonard also drew the Board's attention to further changes to the auditors' report that would be needed if the Company Law Reform Bill was finalised in its present form. The CLR changes to auditor's reports are likely to become effective for accounting periods commencing after October 2007 and the Board discussed whether any of the changes should be applied before that date. Board members concluded that the current format of auditors' report mirrored existing legislation and, as the legislation had not been finalised, it would be unwise to anticipate it for the 2006 reporting cycle. The position would however be reviewed once the CLR had been enacted.

It was agreed that work should proceed on revising Bulletin 2005/4 taking account of changes in legislation already enacted. A marked-up version of a revised Bulletin would be circulated to Board members in due course.

#### **5. ISA 600**

Mr Keith Billing introduced a draft APB letter of comment to the IAASB on a revision of ISA 600: The audit of group financial statements. He noted that views on the draft ISA had been obtained from meetings with a selection of larger audit firms and at a recent open meeting with other interested parties. The draft had also been discussed by the SME audit sub-committee.

Board members made a number of comments on the draft letter. The Board supported the view that the definition of Group Auditor as being under the 'direct supervision' of the group engagement partner should be reconsidered, as should the wording in paragraph 40 of the ISA relating to the communication of significant risks between other auditors and the group auditor. The Board also supported the view that auditors should not always decline an audit appointment where there was a likelihood that they would need to disclaim an opinion because there was not enough information concerning significant associates.

It was agreed that the draft letter would be approved by the Chairman following changes to reflect the comments made, and the letter would then be submitted to the IAASB before the end of the month.

#### **6. PN 15**

Mr Peter Rowley introduced a proposed revision of PN 15: The audit of occupational pension schemes in the United Kingdom. He noted that there had been a number of changes to the laws and regulations applicable to pension schemes since the current

PN 15 was issued in 2004, some of which had been addressed by additional guidance for auditors in Bulletin 2005/5. The draft PN was relatively long because these laws and regulations were extensive. Furthermore, there were a large number of smaller firms involved in the audit of pension schemes which would appreciate detailed guidance. It was intended that a consultation draft of the revision would be issued for a three month consultation period ending in November, with a final revised PN being published before scheme year-ends in spring 2007.

The Board discussed the impact of the change in legislation to allow materiality to be taken into account by auditors when reporting on the statement about contributions. It was suggested that a specific question should be asked in the consultation draft as to whether there was enough guidance on this matter. It was also agreed that wording amendments should be made to the guidance on the audit team's level of knowledge of pensions law and regulations. In addition it should be made clear that there is no responsibility on auditors to audit information, such as scheme membership data, used in actuarial calculations. The Board approved the revision for issue as a consultation draft, and the Chairman thanked Mr Rowley for his assistance in developing the draft. It was also agreed that role of Practice Notes and the future process for keeping them up-to-date should be discussed at the APB's Awayday in November.

## **7. Audit Quality**

The Chairman introduced a discussion of the latest draft of a consultation paper on audit quality. He reported that a meeting had recently been held with the chairmen of a number of FTSE 100 audit committees to discuss the subject but this, and various other views that had emerged, were not as yet fully reflected in the draft. Board members made a number of comments on the draft consultation paper largely around three themes.

Firstly, some Board members thought that the key issues for consultation related to the quality of financial reporting not the quality of audit. They took the view that issues such as the role of the annual financial statements, the accounting framework used and the timing of financial reporting should be more fully addressed either in the early sections of the paper or in a separate paper.

The second general theme related to the role of the audit committee in relation to audit quality. Some Board members thought that more emphasis should be given to the enhanced role of the audit committee post Cadbury. Others thought that the consultation paper provided a useful opportunity to explore how audit committees are currently undertaking their Combined Code role of reviewing the effectiveness of the audit.

The third theme related to whether there was a proven case for the need to improve current audit quality. Some members thought that there was a danger that some failures of financial reporting were being unfairly characterised as failings of audit quality.

The Chairman thanked Board members for their comments. He acknowledged that there was still a considerable amount of work that needed to be done before the paper was ready for publication. He planned that the paper would be reconsidered by the APB at its 26 September meeting.

**8. Next meeting**

It was noted that the next meeting of the Board would be held on Tuesday 26 September. The APB Awayday is scheduled for 3 November.

## **NOTICE TO READERS**

**© The Auditing Practices Board Limited**

This document has been obtained from the website of the Financial Reporting Council (FRC) and its subsidiary Boards, which includes the Auditing Practices Board (APB). Use of the website is subject to the WEBSITE TERMS OF USE, which may be viewed in a separate section of the website. Readers should be aware that although the FRC and its subsidiary Boards seek to ensure the accuracy of information on the website, no guarantee or warranty is given or implied that such information is free from error or suitable for any given purpose: the published hard copy alone constitutes the definitive text.