

MEETING SUMMARY

MEETING OF: APB SME audit sub-committee

DATE AND TIME: Thursday 11th January 2007 at 11.00am

PLACE: Aldwych House - London WC2

PRESENT:

Richard Fleck (Chairman)	Peter Hollis
Malcolm Bacchus	James Hunt
Alan Donaldson	Craig Jenkins
Jane Grant	Martin Longmore
Jon Grant	Prof Neil Marriott
Robert Holland	Martin Ward

Staff: Hazel O'Sullivan Keith Billing

In attendance: Julian Rose (part of agenda item 1)

APOLOGIES:

John Brace	Alan Farrelly
Jayne Clifford	Valerie Steward

1. Introduction

Jon Grant gave a summary of APB activities, including a summary of the discussions at APB meetings on the document *Draft Guidance on Smaller Entity Audit Documentation*. These had emphasised the concerns, already recognised, that the example material included as an appendix is more akin to training material than application guidance. A second Consultation Paper *The need for guidance to aid the implementation of Auditing Standards on smaller entity audits* has now been developed to stimulate debate on this issue in advance of the time when 'clarified' ISAs are implemented in the UK. It was recognised that writing such guidance, including examples and case studies, requires a large investment of resource and this needs to be taken into account when planning the timing of any implementation, such as that of ISAs (UK and Ireland) in 2004.

Julian Rose provided some statistics on annual accounts registered at Companies House, which indicated that the proportion of small companies having a voluntary audit had reduced from 16% to 11%. He reported that the DTI are preparing to consult on raising the threshold further and removing the asset test from the exemption criteria. At a CCAB meeting in November it was agreed in principle to work towards a cross-profession compilation report. This would include the ability to evidence that a professional accountant had been involved in the preparation of the accounts under the

new electronic filing system being developed by Companies House. There was some concern expressed by sub-committee members that the proposed report would not give any detail on the work that has been done by the accountant. It was agreed that APB would keep in touch with progress on this issue.

A subsequent discussion on this topic raised the following points:

- It was thought that, as more companies give up having an audit, there could be a drift towards a poorer quality of accounts on file and it was unlikely that the 'involvement' type of report proposed would prevent this trend.
- There might be a public interest case for developing a 'middle ground' report outlining any verification work done by an accountant, with a positive opinion given, but also noting any areas of the accounts that the work did not cover. This might encourage organisations such as the Charity Commission or the EC to consider raising exemption thresholds further.

2. IAASB Clarity Project

As proposed in the briefing paper for the meeting, the discussion of ISA 260 (Revised and Redrafted), ISA 320 (Revised and Redrafted) and ISA 450 (Revised and Redrafted) was led by Alan Donaldson and Jane Grant who had each prepared a short note on substantive issues that had been raised prior to the meeting through the discussion forum.

In respect of ISA 260:

- The focus on listed entities under paragraph 15, suggests that communications on independence for non-listed entities are not relevant, although application material suggests that communication would have been made with management. This would prove confusing guidance in the UK where communication is required with those charged with governance on all entities.
- Further guidance could be added to A35.

In respect of ISA 320:

- Paragraph 13 is unnecessary as it is covered by paragraph 12 and possibly by material in ISA 330. References to changes in materiality should be to materiality levels (plural) in all cases.
- Paragraphs 11 and A13 need to be made clearer.

In respect of ISA 450:

- The requirement for a summary of uncorrected misstatements to be attached to the written representation is unnecessary and it may be difficult to collate this information in a group situation.
- Paragraphs 15, 16 and 17 would be clearer written as a set of bullet points.

3. Promoting Audit Quality

As part of the previous discussion on compilation reports, sub-committee members had expressed concerns that, as audit registrations are surrendered by smaller firms, the traditional skills and culture within a smaller audit firm are changing. The pressure on this change will increase as the gap between accounting standards for different size companies increases and auditing standards are made increasingly costly for small entities as a result of greater specificity and increased documentation requirements. It was suggested that this might lead to a change in the training structure for an accountancy career, incorporating a base accounting qualification, which is then built on by experience in audit, tax or other specialist areas. Richard Fleck suggested that the Discussion Paper *Promoting Audit Quality* might start this debate as a means of preserving the integrity of audit, without affecting the market for professional accounting services provided to smaller entities.

In addition to the challenge of maintaining skills in audit as more companies opt out and the complexity of standards increases, sub-committee members felt that the following areas had a different emphasis when considering the drivers of audit quality in relation to the audits of smaller entities:

- The threat associated with 'client capture' is different:
 - There may be a close relationship between the auditor and client, but the result is better quality accounting.
 - The financial aspect of 'client capture' is covered by the economic dependence requirements of ES 4 - a partner's remuneration and ongoing career is closely linked with the continued success of the audit firm.
- The skills of staff performing the audits of smaller entities are focussed on accounting in addition to audit, so they are able to challenge the accounting treatments of their client where necessary. A question was raised as to whether the auditors of larger entities had adequate accounting expertise.
- Staff deal with relatively small and simple organisations and so can gain experience of a variety of entities quickly.

Once responses to the Discussion Paper have been analysed, the FRC will publish a feedback paper and it was envisaged that this might include a section on how the issues affect the audits of non-listed entities.

4. APB implementation survey

Hazel O'Sullivan summarised the activities that had been undertaken and the key messages provided by the meetings held and the responses to the survey. The exercise had provided a depth of understanding of the issues that were raised. However, it was agreed that further work would probably not prove useful. There would be more value on working with the accountancy bodies

and others on the issue of the need for guidance to aid the implementation of Auditing Standards on smaller entity audits.

5. Next meeting date

The next meeting is due to be held on Monday 26th March 2007. This meeting will include a discussion of the IAASB Clarity Project and six further ISAs that have been clarified. It was agreed that certain sub-committee members would each concentrate on one of these ISAs in preparation for the meeting.