



International Federation of Accountants

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Agenda Item

8

Committee: IAASB

Meeting Location: London

Meeting Date: December 4-8, 2006

Quality Control

Objective of Agenda Item

To review as a first read the proposed redrafted ISA 220, “Quality Control for Audits of Historical Financial Information.”

Task Force Members

The members of the Task Force are:

Bodo Richardt (Chair)	IAASB Member
Will Rainey	IAASB Member
David Swanney	IAASB Member
John Fogarty (as an advisor)	IAASB Member

Background

ISA 220 (Revised) was issued in 2004 and was effective for audits of historical financial information for periods beginning on or after June 15, 2005. At the same time ISQC 1, “Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance Engagements and Related Services Engagements” was issued and was effective as of June 15, 2005. Conforming amendments were made to ISQC 1 as a result of the issue of ISA 230 (Revised), “Audit Documentation” that were effective June 15, 2006. No conforming amendments have been made to ISA 220 since its issue.

Matters for IAASB Consideration

The Task Force has been asked to prepare a clarity draft of ISA 220, however the IAASB has not yet concluded as to the treatment of ISQC 1. For the purpose of this meeting, the Task Force has not included any material related to ISQC 1; however it will be asking the IAASB for input regarding the way forward for that Standard.

I. Suggestions on How to Review the Accompanying Material

The Task Force has followed a two-step approach to redrafting ISA 220. It found it to be beneficial to prepare a draft that only reflected the mechanical clarity changes (refer to #2 below), before moving on to the more difficult and fundamental issues (refer to #3 below). It felt that by splitting the changes in this manner, the process was more transparent and it was easier to identify the more complex issues. Since the same approach might be beneficial to IAASB members, we suggest that IAASB members read this material in the following order:

1. Read part II of this paper in which the Task Force addresses more fundamental issues that the Task Force would like to obtain input from the IAASB.
2. Begin with Agenda Item 8-C, referring to Agenda Items 8-D and 8-E, as necessary. Agenda Item 8-C reflects the basic clarity changes (referred to as “Level I changes”). These changes include:
 - a. Re-ordering extant ISA 220 into clarity format.
 - b. Setting the objective, using the form and wording discussed at the September IAASB meeting.
 - c. Changing “shoulds” to “shalls” (“shall consider” is not addressed at this level).
 - d. Elevating or redrafting sentences containing the present tense paragraphs, except for specific highlighted cases.
 - e. Adopting approved conforming change from other Standards (limited to a change to the definition of network firm to conform to the change in definition in the Code of Ethics).
 - f. Integrating public sector footnotes into the body of the ISA.
3. Review Agenda Item 8-B. This Agenda Item presents a clean version of Agenda Item 8-C (i.e., the changes proposed in Agenda Item 8-C have been accepted), and shows in mark-up specific additional wording changes proposed by the Task Force. These changes include:
 - a. Perceived inconsistencies between extant ISA 220 and ISQC 1.
 - b. Removal of duplicative material.
 - c. Clarification of language (e.g. dealing with “shall consider” wording).

For review purposes, the Task Force has provided some comments beneath the proposed text to explain the reasons for the proposed changes.

Material Presented

Agenda Item 8-A (Pages 3111 - 3124)	Proposed Redrafted ISA 220 (Clean)
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Agenda Item 8-B (Pages 3125 - 3138)	Proposed Redrafted ISA 220 (Mark up to Reflect Additional Proposed Redrafting Changes)
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Agenda Item 8-C (Pages 3139 - 3152)	Proposed Redrafted ISA 220 (Mark up to Reflect “Level I” Proposed Redrafting Changes)
Agenda Item 8-D (Pages 3153 - 3160)	Disposition of the Present Tense in Extant ISA 220
Agenda Item 8-E (Pages 3161 - 3172)	ISA 220 Mapping Document

Action Requested

The IAASB is asked to consider the accompanying material and:

- Give direction to the Task Force on the issues presented in Part II of this paper.
- Comment on the proposed redrafted ISA 220, including the Task Force’s proposed disposition of the present tense in extant ISA 220, proposed rewording and structure.

II. Issues on Which the Task Force Requires Input

The Task Force has identified some fundamental issues that it believed would be worthwhile to bring to the attention of the IAASB.

A. EXTANT PARAGRAPH 16 (ISA 220) – APPLICATION GUIDANCE REGARDING ACCEPTANCE AND CONTINUANCE OF CLIENT RELATIONSHIPS

- A1. As part of preparing the proposed redrafted ISA 220, the Task Force considered items in ISQC 1 that may have an impact on ISA 220 if and when ISQC 1 is clarified.
- A2. While completing this review, the Task Force identified a difference between the two Standards. Paragraph 28 in ISQC 1 is a black letter paragraph that requires firms to establish policies and procedures on acceptance and continuance of client relationships and specific engagements¹. The corresponding paragraph at the engagement level in extant ISA 220 (paragraph 16) is not black lettered.
- A3. In its review of the present tense material, the Task Force believed that the material in extant paragraph 16 was application material in nature rather than a requirement, since the requirement of the engagement partner is found in paragraph 14 of extant ISA 220. This paragraph is A9 in Agenda Item 8-C (“Level I” draft of ISA 220).

¹ “The firm should establish policies and procedures for the acceptance and continuance of client relationships and specific engagements, designed to provide it with reasonable assurance that it will only undertake or continue relationships and engagements where it:

- (a) Has considered the integrity of the client and does not have information that would lead it to conclude that the client lacks integrity;
- (b) Is competent to perform the engagement and has the capabilities, time and resources to do so; and
- (c) Can comply with ethical requirements.”

- A4. Even though it could be seen as already covered by the broader requirement in paragraph 14, to avoid any doubt the Task Force believed that it is appropriate it repeat this requirement at the engagement level. Therefore this paragraph has been elevated as presented in paragraph 10A in Agenda Item 8-B.

B. BOLD LETTER PARAGRAPH IN ISQC 1 THAT IS NOT IN ISA 220

- B1. During the review referred to in A1, the Task Force identified one black letter paragraph in ISQC 1 that does not appear in ISA 220. Paragraph 28² in ISQC 1 (the part of the paragraph below the a-c list) requires the firm to obtain such information considered necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement and when considering acceptance of a new engagement with an existing client. It also requires the documentation of resolution of issues when issues are identified.
- B2. The Task Force reviewed extant ISA 220 and believes that it might not be sufficiently clear that such procedures should be performed before accepting or continuing the engagement.
- B3. The Task Force believes that this point should be clarified and has included proposed paragraph 11A in Agenda Item 8-B.

C. DIFFERENCES OF OPINION

- C1. Extant ISA 220 paragraph 34 states that the engagement team should follow the firm's policies and procedures when differences of opinion arise. Paragraph 35 states that the engagement partner informs members of the engagement team that they may bring matters involving differences of opinion to the attention of the engagement partner or others within the firm without fear of reprisals.
- C2. The Task Force questioned whether this should be a requirement of the partner at the engagement level or whether it is self-evident that the firm's policies and procedures can be followed by members of the engagement team.
- C3. Currently as placed and as worded in extant ISA 220, the paragraph seems to apply only when differences of opinion occur. The Task Force believes that this material relates to the actions of the engagement partner in generally addressing the engagement team as described in paragraph A14 (8-B).
- C4. The Task Force recommends that the material be included in the bullet point list in paragraph A14. However it is concerned that to move it would change the ISA beyond clarification. For this reason, the Task Force has left the extant wording unchanged, as shown in Agenda Items 8-B and 8-C.

² "...The firm should obtain such information as it considers necessary in the circumstances before accepting an engagement with a new client, when deciding whether to continue an existing engagement, and when considering acceptance of a new engagement with an existing client. Where issues have been identified, and the firm decides to accept or continue the client relationship or a specific engagement, it should document how the issues were resolved."

D. ISQC 1

- D1. ISQC1 and ISA 220 are closely linked – many paragraphs deal with the same issues at the firm level and the engagement level, respectively. Further, ISA 220 states that the engagement team is entitled to rely on the firm’s policies and procedures established under ISQC 1, therefore there should be consistency between the two standards. To maintain this consistency after clarification of ISA 220, ISQC 1 should also be clarified.
- D2. On the other hand, ISQC 1 is not an auditing standard. Clarification of ISQC 1 might need additional considerations.

Action Requested

The IAASB is asked to consider whether they agree with the Task Force’s recommendations noted above.

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