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Our ref: ICAEW Rep 27/13

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Dear Keith

FRC Invitation to Comment: *Analysis of the Main Potential Changes in Auditing Standards Arising from the Exposure Draft of ISA 720 (Revised)*

ICAEW welcomes the opportunity to comment on the FRC's Invitation to Comment *Analysis of the Main Potential Changes in Auditing Standards Arising from the Exposure Draft of ISA 720 (Revised)* published by the IAASB in December 2012, a copy of which is available from this [link](#). Our comments are in the appendix to this letter.

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Yours sincerely

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APPENDIX

We are pleased to attach a draft of our response to IAASB on its IASA 720 proposals. This draft response may change in substance before it is sent.

1. The FRC's 'Analysis' and the extent to which it sets a precedent

While we applaud the FRC's efforts to inform stakeholders about IAASB's proposed changes to ISA 720, we think it would have been better had the FRC:

- made clear the purpose of the analysis;
- provided a genuine qualitative analysis of the differences, rather than a mere statement thereof.

Going forward, we strongly suggest that FRC makes a public statement about the circumstances in which it will issue such analyses, their purpose, and provide some evaluation of the differences listed.

2. Comments in ICAEW's July 2012 response to FRC on the auditing aspects of its effective company stewardship proposals

Members have expressed concern that little account seems to have been taken of any of the observations made in our July 2012 response to FRC on the auditing aspects of its effective company stewardship proposals¹ and, more importantly, that the effect of the changes has been to increase the differences between the UK position and that of the IAASB.

We re-iterate our belief that attempting to influence IAASB by making changes to the UK position risks damaging the UK's current good standing and influence internationally. The tone of the proposals implies that FRC is now indifferent to a growing gulf between international and UK standards.

Our members, who include more preparers and investors than auditors, need certainty and it would help if they were clearer about the FRC's direction of travel. At present, the FRC's status in this area is grounded partly in its contribution to international standard-setting, but mostly in its commitment to the adoption of international standards. We fear that both will be lost if the FRC is equivocal in its commitment to adoption and we do not wish to see this happen.

We remain firm in our belief that the adoption of ISAs is in the best interests of investors, preparers and practitioners in the UK, Europe and elsewhere and that UK auditing standards should be as close as

¹ Paragraphs 11-13 of that response stated that:

11. Given our support for the APB's established position to keep UK and Ireland pluses to the absolute minimum, we have major concerns about the FRC's proposal to add pluses to the ISAs (UK&I) as a matter of principle. We support the adoption of the IAASB ISAs as they are, both for listed companies as well as all other entities. If it is felt necessary or desirable to make changes to the standards, the mechanism for doing this should be through the IAASB, particularly given the IAASB's current top priority project on auditor reporting (as referred to in paragraph 8 above). Before going ahead with the proposals, the FRC should at the very least assess whether the proposed approach to UK and Ireland audit reports can be reconciled to the IAASB's proposals. The IAASB is consulting specifically on the possibility of tailoring the IAASB proposals to accommodate national regimes and the FRC will need to communicate with the IAASB regarding this.

12. There is resistance to the proposal to adopt ISAs throughout the EU and we hope that all the UK and Ireland bodies will continue to argue forcefully for the benefits of ISA adoption. Our arguments will be undermined if the UK and Ireland adopt standards with national pluses beyond legal and regulatory pluses.

13. If the UK and Ireland wish to adopt regulatory measures impacting auditors, providing guidance for auditors would be a more appropriate vehicle than making changes to auditing standards. For example, the APB has in the past issued a number of Bulletins that cover auditors' responsibilities arising from specific regulatory developments including specific requirements relating to listed or financial services companies. We consider that using this type of mechanism would be far more appropriate than making changes to the ISAs (UK&I).

possible to ISAs. Attempts to lead the debate internationally by making pre-emptive unilateral changes are misguided and, more importantly, risk being ineffective.

3. The substance of FRC's 'analysis' and IAASB's proposals

The draft response attached is critical of many aspects of IAASB's proposals. However, we do not believe that significant differences in auditing practices are intended by the IAASB and FRC. For example, the UK definitions refer to knowledge acquired *in the course of performing the audit* and material misstatements of fact that are *otherwise misleading*, as against IAASB's proposal that inconsistencies be determined with reference to *the auditors knowledge of the business*. If the FRC believe that these definitions are different in substance, as noted above, it would have been helpful for this to have been highlighted and explained in the analysis of differences. Ditto IAASB's *read and consider* requirements and the *read to identify* requirements of the FRC. Without a clear explanation of the significance (if any) of the differences, there is a risk of inconsistent interpretation of the differences, which is important where global methodologies are based on ISAs. Some firms might differentiate between the two sets of requirements where no substantive difference is intended, and others might read them as meaning the same thing in substance, even if that is not the intention. The FRC's intentions with respect to these differences are important but unclear.

In some respects, the current UK definitions and requirements are clearer than IAASB's proposals but we do not believe that the quality of UK audits will be affected in substance, regardless of whether the IAASB's proposals are adopted in the UK. This, together with the need to maintain the UK's influence internationally, is justification for adopting the international position should the FRC be unable to argue its case successfully within IAASB.

We note in the draft response to the IAASB attached our belief that significant additional requirements can no longer be justified by IAASB merely on the basis of unsubstantiated claims about improvements to audit quality. Similarly, we consider that as a mature standard-setter, the FRC needs to support the maintenance of minor wording differences with international standards with substantive evidence regarding improvements to audit quality, rather than on the basis of its beliefs alone.