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Plenary 2

Accounting and Auditing – An International Perspective

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Bridging the gap with International Auditing Standards

The bedrock of our international commercial system is high quality financial information, based on high quality international accounting and auditing standards, that relies on internal and external professional accountants. Credible and reliable financial information is fundamental to investment.

Authoritative Body of Issuance of International Auditing Standards

International Federation of Accountants (IFAC) is the worldwide organisation of the accountancy profession. Founded in 1977, its mission also includes furthering the international convergence of standards.

International Auditing and Assurance Standards Board (IAASB) is an independent standard setting board within International Federation of Accountants (IFAC). Its objective is to serve public interest by setting high quality auditing and assurance standards and by facilitating the convergence of International and National standards, thereby enhancing the quality and uniformity of practice throughout the world. The Public Interest Oversight Board oversees the activities of the IAASB and, as one element of that oversight, establishes the criteria for its working procedures.

Comparison between AASs and International Standards

Right from its formation in 1949, the Institute of Chartered Accountants of India (ICAI) has been making efforts to harmonise and upgrade the auditing practices in India. These efforts have taken various forms. ICAI became a member of IFAC in 1977 and has been committed to integrating, as far as practicable, the auditing practices in India to those accepted globally. The setting up of the Auditing and Assurance Standards Board (earlier known as Auditing Practices Committee) by the ICAI to “review the existing auditing practices in India and to develop Statements on Standard Auditing Practices (SAPs)” followed a similar development at the international level, viz. setting up of the International Auditing and Assurance Standards Board (IAASB) by the IFAC

The Preface to the Statements on Standard Auditing Practices states that while formulating the Auditing and Assurance Standards (earlier known as SAPs) in India, the APC will give due consideration to the International Auditing Guidelines issued by the IAPC and try to integrate them, to the extent possible, in the light of the conditions and practices prevailing in India.”

Presently, AASB issues a single series of standards, namely, Auditing and Assurance Standards (though it also occasionally issues guidance notes). This is unlike IAASB which presently issues five distinct series of standards: International Standards on Auditing, International Standards on Review Engagements, International Standards on Assurance Engagements, International Standards on Related Services, and International Standards on Quality Control. IAASB also issues Practice Statements as appropriate to provide interpretive guidance and practical assistance in implementing its Standards and to promote good practice.

Of the thirty-four AASs, thirty-three are based on the ISAs or other international standards that were in force at the time of issuance of the respective AASs. Only one AAS, viz., AAS 12, Responsibility of Joint Auditors, has no corresponding ISA. This is due to the fact that appointment of joint auditors – a practice common in India in the case of audits of large enterprises, especially those in the public sector – is possibly unique to India, making the attendant issues like division of work among joint auditors and the rights and obligations of each of the joint auditors largely irrelevant in a global context.

Most of the international standards have been revised recently by IAASB. The need for this revision arose largely due to a number of scandals (e.g., Enron fiasco) that shook the commercial world a few years ago. The sheer magnitude of these scandals made it imperative for the global professional accountancy community to put the then current auditing standards under microscope so that recurrence of audit failures of this kind and magnitude could be avoided. The result of this exercise carried out by IAASB over the last few years is the wholesale revision of a few standards, substantive changes to many other standards, and conforming amendments to the rest of the standards.

Despite a considerable up gradation of auditing practices in India and their harmonization with the internally accepted practices, there are still some areas where significant differences do exist and the Indian auditing standards need a re-look to bring them at par with the internationally accepted standards or at least to ensure that the departures from the international standards are conscious, deliberate and rational. Also, there are certain areas on which there are no standards in India comparable to that issued by the IAASB such as:

- [Other Information in Documents Containing Audited Financial Statements](#)
- [Auditor's Report on Special Purpose Audit Engagements](#)
- [Auditing Fair Value Measurements and Disclosures](#)

AASB has already taken up the task of reviewing the AASs in the light of revisions to ISAs and it is quite possible that many of the differences will cease to exist once the relevant AASs are revised. AASB is also in the process of developing or proposes to develop AASs on several other topics on which IAASB has already issued standards but on which there is no comparative standard in India.

Though IAASB has 13 standards in the project stage, there are certain areas on which merit consideration for issuance of standards. On some of these areas, standards have already been issued by the American Institute of Certified Public Accountants (AICPA) and should be considered for convergence:

- [Consideration of Omitted Procedures After the Report Date](#)
- [Reporting on Financial Statements Prepared for Use in Other Countries](#)
- [Consideration of Internal Control in a Financial Statement Audit](#)
- [Letters for Underwriters and Certain Other Requesting Parties](#)
- [Communications Between Predecessor and Successor Auditors](#)
- [Audit Adjustments](#)
- [Audit Committee Communications](#)

- Inquiry of a Client's Lawyer Concerning Litigation, Claims, and Assessments
- Association With Financial Statements
- Substantive Tests Prior to the Balance Sheet Date
- The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles
- Establishing an Understanding With the Client
- Reports on the Application of Accounting Principles

There is an urgent need to review the Indian standards in the context of the recent revisions made to a large number of international standards which have made risk assessment the focal point of an audit. ICAI would have to ensure that apart from catching up with existing standards of IAASB by revision of AASs, development of new standards on areas on which there is no Indian Auditing Standard comparable to that issued by IAASB, it is also geared up to issue standards on the above areas to keep pace with IAASB and globally accepted auditing practices. Another aspect that AASB, or more appropriately the Council of ICAI, may need to look into is to model the operating procedure of AASB on the lines followed by IAASB which, some argue, is more transparent and conducive to greater accountability. For example, making the agenda and minutes of meetings of the board available on the website of ICAI, process of formal voting on each significant issue, making the meetings of the board open to public, etc. are some of the steps that may evoke greater interest and confidence among the user groups in the functioning of the AASB.

Another area which merits discussion is the need for an independent standard setter and regulator. The basic principle being recognised internationally is that the standard setting body and the regulator supervising the accounting profession is completely independent of the professional body. It is pertinent to add here that there are other compulsions which would drive the need for independent regulation of the profession in India. For instance, a CA firm in India which issues an audit report with respect to a company listed in the USA will be subject to regulation by the USA's Public Company Accounting Oversight Board. However, the Board is permitted to rely on the work of oversight systems in other countries based on a sliding scale – the more independent and more rigorous a local oversight system, the greater the Board's reliance on that system. Accordingly, for Indian companies, independent regulatory oversight would avoid unnecessary costs and potential conflicts of law.

GLOBAL DEVELOPMENTS ON THE RESEARCH FRONT

- In August 2006 American Institute of Certified Public Accountants (AICPA), American Accounting Association (AAA) and IAASB launched a research initiative to provide better understanding of users' perceptions of the financial statement audit and auditor's report.
- Researchers are required to submit a summary of results to ASB and IAASB by October 1, 2007 and more detailed report to the Board by January 7, 2008.



Accounting and Auditing

- An International Perspective

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Agenda

PANEL DISCUSSION

- Need for Auditing and Assurance Standards
- Authoritative Body for issuance of International Auditing and Assurance Standards
- Status of International Auditing Standards till January 2007
- Needs identified for development of IAAS
- The India situation

Credibility of financial statements questioned in the past?

Breaking news



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Authoritative Body for Issuance of Auditing Standards

- International Federation of Accountants (IFAC) is the worldwide organisation of the accountancy profession. Founded in 1977, its mission also includes furthering the international convergence of auditing standards.
- International Auditing and Assurance Standards Board (IAASB) is an independent standard setting board within IFAC.
- Public Interest Oversight Board oversees the activities of the IAASB and, as one element of that oversight, establishes the criteria for its working procedures.

Changing face of IAASB

- International standards have been revised recently by IAASB. The need for this revision arose largely due to sheer magnitude of the scandals (e.g., Enron fiasco).
- IAASB has issued 34 Auditing Standards till Jan 2007.
- IAASB has 13 standards in the project stage, however there are certain areas that merit issuance of new standards. On some of these areas, standards have already been issued by the American Institute of Certified Public Accountants (AICPA) and should be considered for convergence.

Illustrative needs identified for development of International Auditing Standards

- Establishing Understanding with the Client
- Audit Committee Communications
- Audit Adjustments
- Substantive Tests prior to the Balance Sheet Date
- Communication between the Predecessor and Successor Auditors
- Consideration of Omitted Procedures after the Report Date
- Reporting on Financial Statements Prepared for Use in Other Country
- Letters for Underwriters
- Inquiry of a Client's Lawyer Concerning Litigation, Claims
- Association with Financial statements
- Presenting Fairly in Conformity with Generally Accepted Accounting Principles
- Reports on application of Accounting Principles

(Source AICPA ASB standards-SAS)

Challenges faced:

Understanding with the Client

- Lack of proper clarity on the scope of engagement and identification of responsibilities between management and auditors may lead to potential conflicts.
- (Example- Internal control, compliance with laws and regulations is management's responsibility, detecting fraud is not auditor's responsibility)
- SET THE RIGHT EXPECTATION IN THE FIRST PLACE

Source SAS : 83 & 89

Audit Committee Communications

- Mandatory communication of specific matters to Audit Committee which inter-alia would include any significant change in accounting policy, process for formulating sensitive estimates, material audit adjustments impacting the financial statements.
- AUDIT COMMITTEE NEEDS TO BE COMMUNICATED ON SIGNIFICANT AUDIT ISSUES AND ACCOUNTING DEVELOPMENTS

Source SAS :61, 89 & 90

Challenges faced:

Communication gap between successor auditor and predecessor auditor.

- **SPECIFIC INQUIRIES SHOULD BE MADE WITH REGARD TO:**
 - Management Integrity
 - Significant disagreements with Management
 - Previous auditor's understanding for reasons for change
 - Any communication to Audit Committee regarding frauds etc.
- **CLIENT'S RISK QUOTIENT NEEDS TO DETERMINED PRIOR TO ACCEPTING THE ENGAGEMENT**

Inquiry with Lawyers about Litigations

- Inquire with Management
- Obtain written representations from the Client
- Thorough reading of client minutes, contracts and inquiry with Lawyer
- Limitation of lawyers response on the potential loss-auditor to make a judgement.
- Refusal of lawyer to response would lead to limitation of scope
- **POTENTIAL LITIGATION MAY LEAD TO DISCALIMER / QUALIFICATION IN THE AUDIT REPORT**

Challenges faced:

Substantive tests are performed before the Balance Sheet date

- It is important that the auditor designs suitable analytical procedures till the Balance Sheet date. **SAS 45** provides an insight into such procedures.
- Report on Financial Statements for Other countries
 - Lack on clarity of purpose may lead to design deficiencies in audit.
 - Home country procedures may not be sufficient
 - Professional expertise on applicable procedures may be required.
- **SAS 51** provides a guidance on designing the audit requirements for a report on Financial Statement for Other Countries including specific reporting requirements.

Challenges faced:

Association with Financial Statements

- Accountant needs to be cautious in case his name is being mentioned in an unaudited document as public would rely on the same.
- Precautions
 - Clear Disclaimer of Opinion
 - “Un-audited” on all pages
 - Disclosure in separate paragraph incase unaudited financials are given along with audited financials.

Source SAS :26, 35 & 72

Omitted Procedures After the Audit report date

- Incase the auditor concludes that one or more audit procedures were omitted based on existing circumstances, then he should :
- Assess the importance of the procedure by review of the working papers and if he concludes that without conducting the procedure he would be unable to support his previous opinion, he should apply the procedure
- If he is unable to apply the procedure then he should consider as a limitation of scope and take appropriate actions.

Source SAS :46

Actions taken towards convergence

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Comparison of AAS and International Auditing Standards

- Right from its formation in 1949, the Institute of Chartered Accountants of India (ICAI) has been making efforts to harmonise and upgrade the auditing practices in India.
- ICAI became a member of IFAC in 1977 and has been committed to integrating, as far as practicable, the auditing practices in India to those accepted globally.
- The setting up of the Auditing and Assurance Standards Board (**AASB**) by the ICAI to review the existing auditing practices in India and to develop Auditing and Assurance Standards (**AAS**) followed a similar development at the international level, viz. setting up of the International Auditing and Assurance Standards Board (IAASB) by the IFAC.

Indian Scenario on Auditing Standards

- AASB defines the scope and functions of the Auditing Practices Committee, and procedure for issuing Auditing and Assurance Standards, it states the position of existing Statements, and effective date for their implementation.
- AASB has issued 34 Auditing and Assurance Standards (AAS) till Jan 2007. These are in line with the International Auditing and Assurance Standards.
- Despite a considerable up gradation of auditing practices in India and their harmonization with the internally accepted practices, there are still some areas where Indian auditing standards do not exist at par with the internationally accepted standards
 - Other Information in Documents Containing Audited Financial Statements
 - Auditor's Report on Special Purpose Audit Engagements
 - Auditing Fair Value Measurements and Disclosures
- Standards which need to be developed internationally also need to be developed in India.

Action points for AASB

- Development of new standards which are more pertinent to the Indian context. A special project may be taken by AASB up to identify such needs.
- ICAI to model the operating procedure of AASB more on lines of IAASB to make it transparent and more conducive to greater accountability.
- Indian companies, require independent regulatory oversight body supervising the accounting profession to avoid potential conflicts of law.



Thank You

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