Federation of European Accountants
Fédération des Experts comptables Européens

17 September 2009

Commissioner McCreevy
European Commission
DG Internal Market and Services
Auditing Unit-F4
SPA 2/JII – 01/112
B - 1049 Brussels

Cc Pierre Delsaux
Ulf Linder

E-mail: markt-consultation-isa@ec.europa.eu

Ref.: AUD/HvD/HB/SH

Dear Commissioner,
Dear Mr. Delsaux,
Dear Mr. Linder,

**Re: European Commission Consultation on the Adoption of International Standards on Auditing**

FEE is pleased to provide you below with its comments on the European Commission Consultation on the Adoption of International Standards on Auditing (ISAs) of June 2009 2008 (the Consultation Paper).

FEE is the Fédération des Experts comptables Européens (Federation of European Accountants). It represents 43 professional institutes of accountants and auditors from 32 European countries, including all of the 27 European Union (EU) Member States. In representing the European accountancy profession, FEE recognises the public interest. It has a combined membership of more than 500.000 professional accountants, working in different capacities in public practice, small and big firms, government and education, who all contribute to a more efficient, transparent and sustainable European economy.

FEE's objectives are:

- To promote and advance the interests of the European accountancy profession in the broadest sense recognising the public interest in the work of the profession;
- To work towards the enhancement, harmonisation and liberalisation of the practice and regulation of accountancy, statutory audit and financial reporting in Europe in both the public and private sector, taking account of developments at a worldwide level and, where necessary, promoting and defending specific European interests;

- To promote co-operation among the professional accountancy bodies in Europe in relation to issues of common interest in both the public and private sector;
- To identify developments that may have an impact on the practice of accountancy, statutory audit and financial reporting at an early stage, to advise Member Bodies of such developments and, in conjunction with Member Bodies, to seek to influence the outcome;
- To be the sole representative and consultative organisation of the European accountancy profession in relation to the EU institutions;
- To represent the European accountancy profession at the international level.

FEE's ID number on the European Commission's Register of Interest Representatives is 4713568401-18.

Our general remarks as well as the FEE position on the proposals including in the Consultation Paper are included below. Our responses to the questions included in the Consultation Paper are included in the Appendix to this letter and provide for more detailed comments backing-up the FEE position on the Consultation Paper.

## General remarks

FEE very much welcomes the European Commission (Commission or EC) Consultation on the Adoption of International Standards on Auditing as we are fully supportive of the adoption of ISAs for the statutory audit of all companies, including small companies for which an audit is required.

FEE started leading the debate on ISAs in Europe more than ten years ago with the issuance in June 1998 of a paper on "Setting The Standards – Statutory Audit in Europe"[1]. In 2001, FEE published a Discussion Paper entitled "Proposal on International Standards on Auditing in the EU"[2] in which FEE proposed that by 2005 national auditing standards in the European Union should require auditors of financial statements to comply with ISAs and report on financial statements in accordance with ISAs.

Therefore, in April 2006, FEE particularly welcomed the proposals in the Statutory Audit Directive requiring "statutory auditors and audit firms to carry out statutory audits in accordance with international auditing standards" to ensure consistent high quality statutory audits in Europe. This requirement supports the long standing belief that there is only one benchmark audit, whereby the level of assurance obtainable from an audit exceeds the level obtainable from other types of assurance engagements. If an auditor intends to issue a report under ISA, then compliance with all relevant ISAs is necessary. This concept is generally referred to as "an audit is an audit".

At the end of 2008, FEE developed proposals to support its member bodies with the implementation of ISAs over the next couple of years. FEE has started the execution of this work with a focus on sharing information to help smaller FEE Member Bodies and SMPs with the implementation of the clarified ISAs.

[1] See http://www.fee.be/publications/default.asp?library_ref=4&content_ref=1100
[2] See http://www.fee.be/publications/default.asp?library_ref=4&content_ref=113



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In April 2009, FEE issued a Policy Statement on ISAs[3] which focused especially on the implementation of ISAs for all statutory audits in the European Union (EU) and the implementation of ISAs for Small- and Medium-sized Entities (SMEs).

## FEE Position on the Proposals including in the Consultation Paper

*Adoption of ISAs in the EU*

FEE fully supports the adoption of ISAs for all statutory audits in the EU as the use of harmonized international auditing standards will serve to increase audit quality and enhance confidence in the reliability, comparability and consistency of financial statements in the EU as well as the acceptance of audit reports beyond their home jurisdictions whether within or outside the EU.

*Add-ons, carve-outs and audit report*

We very much welcome the mention in the Consultation Paper that the EC does not foresee circumstances in which modifications of the contents of the clarified ISAs would be necessary. In addition to EC add-ons and carve-outs not being acceptable, Member State add-ons that affect the ISA audit opinion and carve-outs are also not acceptable. Member State additions resulting from national legal and regulatory requirements should be reported in the second part of the audit report on matters that do not affect the ISA audit opinion and Member State additions should only be accepted after having passed the EC acceptance due process.

Therefore, in our view, the reference in the audit report should be to compliance with ISAs, not to ISAs as adopted in the EU. A harmonized layout of the audit report may be beneficial for users of financial statements, preferably applying ISA 700 on "Forming an Opinion and Reporting on Financial Statements".

*Legal instrument and Application and Explanatory Material*

As suggested in the Consultation Paper, we are fully supportive of an EU Regulation as the legally binding instrument to be used by the Commission to adopt ISAs for use in the EU.

We agree that the application material should be given a special status and be part of the adoption process as the entire text of an ISA is relevant to understand the objectives stated in an ISA and to properly apply the requirements of an ISA. However, we are of the opinion that the application material should not be acknowledged as "best practice" in the legal instrument adopting ISAs as it provides further explanation of the requirements of an ISA and guidance for carrying them out while in itself not imposing a requirement.

Therefore, it should be acknowledged as "Application and Other Explanatory Material" whereby it maintains its authority as stated in ISAs and whereby such authority is explained or defined in the introductory notes to the legal instrument adopting ISAs.

[3] See http://www.fee.be/publications/default.asp?library_ref=4&content_ref=1018



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*International Standard on Quality Control (ISQC 1)*

In line with the conclusion in the University of Duisburg-Essen study that the introduction of ISQC 1 would increase the benefits of ISA adoption at EU level, we recommend that ISQC 1 be part of the adoption process because ISAs and ISQC 1 are interrelated. The alternative as allowed by ISA 220 for audit firms to be subject to national requirements that are at least as demanding as ISQC 1 is acceptable but may not result in the harmonisation and other benefits expected from EC adoption of ISAs.

*Timing of adoption of ISAs in the EU*

Although it would make sense for the EC to adopt ISAs in the EU by the IAASB effective date for implementation of clarified ISAs for audits of financial statements for periods beginning on or after 15 December 2009, as also supported by the Forum of Firms of over 20 of the largest networks of accounting firms, it is in practice more appropriate for EU Member States that the EC adopts ISAs and ISQC 1 in the EU for audits of financial statements for periods beginning on or after 15 December 2010 at the earliest as this would provide additional time for the necessary changes to be implemented, especially in Member States where current national auditing standards are not based on extant ISAs. The European Commission should as soon as possible announce its timetable for the adoption and implementation of ISAs in EU Member States in order to ensure consistent adoption across Europe.

For further information on this letter, please contact Mrs. Hilde Blomme at +32 2 285.40.77 or via email at hilde.blomme@fee.be from the FEE Secretariat.

Yours sincerely,

Hans van Damme
FEE President



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## Appendix

### Question 1: Is international acceptance of the ISAs sufficiently demonstrated?

Yes. We believe that the international acceptance of the International Standards on Auditing (ISAs) as issued by the International Auditing and Assurance Standards Board (IAASB) is sufficiently demonstrated, as also indicated in the Consultation Paper.

(1) The audit profession globally has adopted ISAs:

(a) More than 100 jurisdictions around the world use ISAs directly or base their national standards on ISAs;
(b) The Forum of Firms (FOF), the association of over 20 of the largest networks of audit firms, has publicly announced that its members are encouraged to implement the clarified ISAs on a timely basis and that they will use clarified ISAs from the IAASB due date;
(c) The University of Duisburg-Essen study estimates that 56% of Member States currently have standards based on the extant ISAs (or have moved or will move to the clarified ISAs).

(2) Public authorities and regulators in different jurisdictions have adopted ISAs and are involved in the due process:

(a) As the Consultation Paper mentions, "*Many public authorities, including audit regulators have adopted ISA or made public their decision to converge their standards towards the ISA including Australia, Canada, China, the Netherlands, South Africa and the United Kingdom/Ireland*";
(b) Based on an informal survey held in May 2009 by FEE, 9 European Union Member States and Norway intend to adopt the clarified ISAs for audits of financial statements for periods beginning on or after 15 December 2009;
(c) As the Consultation Paper also mentions, the Financial Stability Board has effectively identified ISA as one of the 12 key sets of standards for sound financial systems[4];
(d) As the Consultation Paper also refers to, the World Federation of Exchanges (WFE) recognises the importance of ISAs;
(e) There is already active involvement of representatives of the public interest, including audit regulators, in the standard setting of the IAASB. This results from the rigorous due process and governance of the IAASB itself[5]:

(i) The IAASB has public members who must be individuals who are, and will be seen to be, capable of representing the broad public interest;
(ii) Half of the members of the IAASB are non-practitioners;
(iii) Observers, including the EC, have a right to speak at IAASB meetings and more generally to raise issues and present arguments during all stages of the standard setting process;

[4] See http://www.financialstabilityboard.org/cos/key_standards.htm.
[5] See http://www.ifac.org/Members/DownLoads/international-standard-setting-in-the-public-interest.pdf



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(iv) Involvement of the IAASB Consultative Advisory Group (CAG) whose members represent a balance of geographical representation and regulators, international organizations (including the EC), users and preparers;

(v) Public oversight by the Public Interest Oversight Board (PIOB) (made up of 10 members, including 2 members nominated by the European Commission, 4 members nominated by IOSCO and others by the Basel Committee on Banking Supervision, the International Association of Insurance Supervisors and the World Bank) which has its mandate from the Monitoring Group;

(f) As the Consultation Paper mentions, on 11 June 2009, IOSCO publicly encouraged the acceptance of audits performed in accordance with clarified ISAs for cross-border listings and the consideration of the clarified ISAs when setting auditing standards for national purposes;

(g) In the United States, the Auditing Standards Board of the AICPA, which sets standards for unlisted companies in the United States, has resolved to bring its standards (US GAAS) in line with ISAs (after verification they do not depart too much from the Public Company Accounting Oversight Board (PCAOB) standards);

(h) Recently, the PCAOB has started to move towards ISAs, especially in the area of risk assessment and responding to risk. The current differences in this area will be reduced when the PCAOB issues its current proposed standards on the topic;

(i) This explicit move to ISAs by the PCAOB is also acknowledged in the Maastricht Accounting, Audit and Information Management Research Center (MARC) study on the evaluation of the differences between ISAs and PCAOB auditing standards of 20 July 2009[6].

## Question 2: What degree of importance do you attach to the fact that the Commission may amend the standards?

(1) As Article 26 of the Statutory Audit Directive states that the European Commission may adopt international auditing standards the European Commission which are generally accepted internationally, this implies that the Commission should not seek to unilaterally modify such standards for Europe. This is confirmed by the Consultation Paper which states that the Commission services "currently do not foresee the circumstances in which modifications of the contents of the clarified ISAs would be necessary" (page 6).

(2) Additionally, the University of Duisburg-Essen study concluded that: "adoption of the clarified ISA through the European Union (EU) would contribute to the credibility and quality of financial statements and to audit quality in the EU, and to a greater acceptance of audit reports outside of their home jurisdictions within and outside of the EU"[7]. These effects would be diminished to the extent the Commission would modify clarified ISAs after adoption.

(3) We support early and active involvement of the Commission, in cooperation with the Member States, in the existing IAASB due process directly involving stakeholders,

[6] http://ec.europa.eu/internal_market/auditing/docs/ias/evalstudy2009/summary_en.pdf, p, 7-8.

[7] 'Evaluation of the possible adoption of International Standards of Auditings (ISAs) in the EU – Executive Summary', University of Duisburg-Essen, page 9, point 3.7, see http://ec.europa.eu/internal_market/auditing/docs/ias/study2009/summary_en.pdf).



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used to create and modify ISAs, to ensure that ISAs being developed meet the criterion of being conducive to the European public good. Such early intervention in the process should serve to avoid the need for any later amendments to ISAs.

(4) The circumstances under which the Commission, in cooperation with the Member States, would amend ISAs should be extremely limited. This should be a last resort solution, applicable only after the Commission has raised any objections it may have through the channels of the regular due process and based on the opinion of the European oversight authorities including the European Group of Auditor Oversight Bodies (EGAOB) ISA Subgroup.

## Question 3: To what extent are "add-ons" or "carve outs" by Member States acceptable?

(1) In our view Member State add-ons that affect the ISA audit opinion and carve-outs are not acceptable as they run counter to the goal of harmonized international auditing standards that will serve to increase audit quality and enhancing confidence in the reliability, comparability and consistency of financial statements in the EU. Any such add-ons or carve-outs would also not contribute to furthering the internal market for audit services. Only add-ons in relation to the scope of the audit relating to matters that do not affect the ISA audit opinion due to local corporate or business law would be acceptable because they will be dealt with in the second part of an ISA audit report. However, any such add-ons should be limited to those required to fulfil such legal requirements.

(2) More specifically, carve-outs will undermine the brand of "high quality audit" and should therefore be prohibited and add-ons affecting the ISA audit opinion would lead to regulatory competition with increasing standards without any benefits.

(3) Departure from a given standard may lead to additional costs (training, local re-design of EU-wide developed methodologies, etc.).

(4) The European Commission should develop a due process for the consideration and acceptance of specific national legal requirements relating to the scope of statutory audits in individual EU Member States following Article 26 of the Statutory Audit Directive for reporting purposes in the second part of the audit report on matters that do not affect the ISA audit opinion, but result only from legal and regulatory requirements. These additions should be kept to a minimum, as provided for in the Directive.

## Question 4: Do you have any comments on the overall cost/benefit analysis presented in the University of Duisburg-Essen study?

(1) We concur with the overall conclusion of the University of Duisburg-Essen study that "On balance, an adoption of the clarified ISAs through the EU would contribute to the credibility and quality of financial statements and to audit quality in the EC, and to a greater acceptance of audit reports outside of their home jurisdictions within and outside of the EU. There are significant net benefits expected from ISA adoption



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through the EU beyond any adoption through the Forum of Firms (FOF) or EU member states."

(2) The University of Duisburg-Essen study covered the costs by countries in aggregate and treated the costs that may occur if some Member States would not apply ISAs whilst others would do so anyway (with or without adoption by the Commission) as a benefit to be realized on ISA adoption (i.e. costs that would be saved or avoided if ISAs were adopted in Section 4.4.5.5.5).

(3) These "costs" should be taken into consideration by the European Commission as costs that will be incurred as opportunity costs of non-adoption, many in perpetuity, if ISAs were not adopted in all EU Member States and would be:

- (a) use of different (multiple) sets of standards by one and the same firm for statutory purposes (local standards) and for contributing to a group audit where the group audit is performed under other European Union Member States standards;
- (b) related amendments of methodologies, audit manuals, training, etc.;
- (c) costs incurred through any confusion of stakeholders as to what an audit entails under different Member State regimes.

We believe that if ISAs are adopted throughout the EU without any add-ons and carve-outs, these costs will be avoided but such costs should be taken into consideration to examine the cost of not adopting ISAs.

(4) We believe that the overall, main long-term benefit of the adoption of ISA would be at the level of audit quality throughout the EU. Over time Member State Oversight Bodies should be in a position to judge this effect.

## Question 5: Should the Application Material be part of the adoption process and acknowledged as "best practice"?

The Application and Explanatory Material should be part of the adoption process but not as "best practice".

(1) We agree that the application material contained in each ISA should also be adopted, for the understandability, coherence and quality of the standards.

(2) The publication/adoption method to be chosen should make it clear that although the application material is part of ISAs, it is guidance rather than a specific requirement or norm that has to be applied.

(3) We agree that the application material should be given a special status. However, we are of the opinion that the application material should not be acknowledged as "best practice" in the legal instrument adopting ISAs but as "Application and Other Explanatory Material" whereby it maintains its authority as stated in ISAs and whereby such authority is explained or defined in the introductory notes to the legal instrument adopting ISAs. In this respect, reference is made to ISA 200 on "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing" and more specifically to paragraphs A58 and A59. Paragraph A58 explains that the entire text of an ISA is relevant to an understanding of the



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objectives stated in an ISA and the proper application of the requirements of an ISA. Paragraph A59 clarifies that where necessary, the application and other explanatory material provides further explanation of the requirements of an ISA and guidance for carrying them out. [...] While such guidance does not in itself impose a requirement, it is relevant to the proper application of the requirements of an ISA. The application and other explanatory material may also provide background information on matters addressed in an ISA.

(4) As suggested in the Consultation Paper, we are fully supportive of a regulation as the legally binding instrument to be used by the Commission to adopt ISAs for use in the EU.

## Question 6: Should ISQC 1 on internal quality controls be part of the adoption process?

Yes, International Standard on Quality Control (ISQC) 1, Quality Controls for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements should be part of the adoption process. The alternative as allowed by ISA 220 for audit firms to be subject to national requirements that are at least as demanding as ISQC 1 is acceptable but may not result in the benefits as described below.

(1) As the Consultation Paper states, ISAs and ISQC 1 are interrelated, in particular as far as ISA 220 is concerned which requires the engagement partner of an audit to assess compliance with the audit firm's internal system of quality control, as required by ISQC 1.

(2) The University of Duisburg-Essen study also concluded that the introduction of ISQC 1 would increase the benefits of ISA adoption at EU level by enhancing the positive aspects attributable to the regulation effect of ISA adoption and that ISCQ1 would form the basis for the harmonization of the methodology for inspections or external quality reviews of audit firms[8].

(3) Adoption of ISQC 1 would also contribute to the harmonization of the audit offer in the EU and towards the development of an internal market for audit services.

(4) The adoption of ISQC 1 would provide the oversight bodies of EU Member States with a common standard against which to assess the quality control systems of audit firms.

## Question 7: In case of adoption of the ISAs at EU level, would a common reference to "ISAs as adopted in the EU" in all auditors' reports in the EU be sufficient? Or, is further harmonisation of audit reports necessary?

(1) In our view the reference in the audit report should be to compliance with ISAs, not to ISAs as adopted in the EU as this gives the impression that there will necessarily be an EU variation whereas we believe that the objective should be to adopt international auditing standards, without EU add-ons to the ISA audit opinion or carve-outs.

[8] Universty of Duisburg-Essen study, page 9.



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(2) Audit reports referring to 'ISAs as adopted in the EU' would also impair the worldwide reliability of consolidated financial statements of international groups.

(3) With full adoption of ISA and ISQC 1, there should be no need for (significant) differences in audit reports, at least not in the first part of the audit report that provides an opinion on the audited company's financial statements.

(4) A harmonized layout of the audit report (at least for the part of the auditors' reports on annual or consolidated accounts prepared using IFRS and under the Fourth and Seventh EU Directives) may be beneficial for users of financial statements and generally create efficiencies. It is however preferable that such harmonisation apply ISA 700 on "Forming an Opinion and Reporting on Financial Statements" on which standard the IAASB will perform further research in 2009-2010.

## Question 8: Do you support adoption of ISAs at EU level?

Yes. As suggested in the Consultation Paper, we are fully supportive of a regulation as the legally binding instrument to be used by the Commission to adopt ISAs for use in the EU.

## Question 9: If yes, which of the following options do you support:

*Option 1 – ISAs should be adopted for the audit of the consolidated accounts of the listed companies (IFRS accounts);*
*Option 2 – ISAs should be adopted for the statutory audit of all companies except for the audits of small companies where Member States would be free to choose which audit standards should be applied;*
*Option 3 – ISAs should be adopted for the statutory audit of all companies, including small companies for which an audit is required.*

(1) We are in favour of option 3 as we believe that this is the option that leads best to consistent audit quality throughout the EU and so enhances confidence in the reliability, comparability and credibility of financial reporting in the EU.

(2) In our opinion, it is also the only option which is in line with Article 26 of the Statutory Audit Directive.

(3) Options 1 and 2 would create first and second-class audits and auditors, which could lead to the following difficulties:

  (a) It could create confusion and misunderstanding in the minds of users of financial statements as to the significance of an audit and the nature and level of assurance provided in any given circumstance resulting in a decrease of confidence in the reliability of financial reporting;
  (b) Continuing to perform audits of smaller entities based on national auditing standards results in differences in the financial reporting chain throughout the EU and impairs harmonisation of EU financial reporting;
  (c) As the activities of smaller entities expand across national borders, taking advantage of the internal market, uniform standards arguably become just as



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relevant for them and the users of their financial statements as they do for large companies, particularly in accessing finance;

(d) A widening rather than a contraction of the "two tier" nature of the auditing profession, resulting in less rather than more choice for companies seeking an auditor;

(e) A person training with a smaller audit firms with little clients and expertise in larger auditing standards (ISAs) would find it more difficult than at present to move to a larger audit firm;

(f) An increase in costs for all audit firms that are present in both markets due to the need to create and maintain dual methodologies, tools, training, etc. (or an increase for the companies they audit, to the extent these costs are passed on);

(g) Complexity in the conduct of transnational audits incorporating different methodologies for different components;

(h) An increase in cost and/or complexity for auditor oversight bodies that would equally need to address two sets of standards in their inspections of audit firms.

(4) Specificities to audits of smaller entities are taken into account in the standards themselves as well as in the guidance to the standards:

(a) ISAs contain "Considerations Specific to Smaller Entities";

(b) FEE has issued a policy statement covering the implementation of ISAs for small and medium-sized companies, citing as an example that in the simple audit of a small or medium-sized company, up to one-third of the 36 ISAs may not be relevant so their requirements would not need to be met[9];

(c) The IFAC SMP Committee has issued a Guide to Using International Standards on Auditing in the Audit of Small- and Medium-Sized Entities in December 2007[10] and is in the process of updating this Guide for the clarified ISAs;

(d) The IAASB has recently issued a Staff Questions and Answers on "Applying ISAs Proportionately with the Size and Complexity of an Entity"[11] which demonstrates that ISAs can be proportionately applied with the nature, size, risks and complexity of the audited entity;

(e) The Auditing Practices Board in the UK issued "Guidance on Smaller Entity Audit Documentation"[12] and is in the process of updating this Practice Note based on the clarified ISAs by October 2009;

(f) The IAASB is currently examining the possible development of international standards for a limited assurance service (which would be clearly distinguished from an audit) in order to satisfy demand for such a service in those instances where a statutory audit is not required and such an audit is deemed to be too expensive compared to the needs of users in the particular circumstances. In July 2009, FEE issued a "Survey on the Provision of Alternative Assurance and Related Services Across Europe"[13] which lays out the urgent need for such standards for limited assurance services in the EU;

(g) FEE also supports the conclusions of the 28 May 2009 meeting of the High Level Group of Independent Stakeholders on Administrative Burden calling for all relevant stakeholders to reach a common understanding on this important aspect.

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[9] See http://www.fee.be/fileupload/upload/Auditing%20and%20Assurance%20PS%20I%20International%20Standards%20on%20Auditing%20%28ISAs%29%20I%2009043014520092314 9.pdf.

[10] See http://www.ifac.org/Members/DownLoads/ISA_Audit_Guide.pdf

[11] See http://www.ifac.org/Members/DownLoads/applying-isas-proportionate.pdf

[12] See http://www.frc.org.uk/images/uploaded/documents/PN26%20Web%20Sep%2020071.pdf.

[13] See http://www.fee.be/fileupload/upload/Assurance%20Survey%20color2472009251643.pdf

### Question 10: Do you have comments on the timing in case of an adoption of the ISAs?

(1) Since the Forum of Firms, covering over 20 of the largest networks of accounting firms, encourages its members to implement ISAs for audits of financial statements for periods beginning on or after 15 December 2009, the IAASB effective date for the implementation of clarified ISAs, it would make sense for the European Commission to also adopt ISAs in the EU by then. However, as the University of Duisburg-Essen study estimates that 56% of Member States currently have standards based on the extant ISAs, 44% of Member States have standards which are currently not based on extant ISAs, it is in practice more appropriate for the European Commission to adopt ISAs and ISQC 1 in the EU for audits of financial statements for periods beginning on or after 15 December 2010 at the earliest.

(2) The European Commission should as soon as possible after its analysis of the responses to this Consultation Paper announce its timetable for the adoption and implementation in EU Member States of ISAs for audits of financial statements in the EU.



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