



Report to the INTOSAI Governing Board by the INTOSAI PSC Financial Audit Guidelines Subcommittee

Based on decisions taken by the INCOSAI and the INTOSAI Governing Board the strategic objective of the INTOSAI PSC Financial Audit Guidelines Subcommittee (FAS) is to develop high quality guidelines that are globally accepted for the audit of financial statements in the public sector. To achieve this objective and ensure a strategic and cooperative partnership with the International Auditing and Assurance Standards Board (IAASB), the FAS shall make use of the best resources made available by INTOSAI members and by leverage the expertise and resources of the IAASB. The FAS shall incorporate public sector considerations in the International Standards of Auditing (ISA) by participating as members in IAASB Task Forces where audit standards on current and future ISAs are developed. Furthermore, the FAS shall comment on exposure drafts of ISAs and provide guidance above and beyond what is provided in the ISAs for public sector audits. The FAS shall develop Practice Notes to all ISAs. Activities and achievements are summarized in FAS' Quarterly Performance Reports.

The development of guidelines and the co-operation with the IAASB are long term commitments. The work involves financial audit expertise from a large number of Supreme Audit Institutions. The subcommittee itself consists of eleven members and approximately 70 SAIs have nominated 150 experts for participation in the FAS work. At present 33 SAI auditors are involved in ongoing projects as experts and back-office experts. This is one of the most extensive and complex projects of the INTOSAI. The project is supported, financially and in other ways, by the participating SAIs, the World Bank, the Asian Development Bank and the International Federation of Chartered Accountants (IFAC). The Swedish National Audit Office (SNAO) is facilitating the work by providing the Project Secretariat.

In the first two years of the project, resources were allocated to develop and put efficient working and decision-making procedures in place and to ensure the availability of INTOSAI experts from different SAI systems and geographical regions. These mechanisms are now in

place and the Project Secretariat's role to assist the subcommittee has in the last year primarily focused on the development of the guidelines.

Summary of achievements

- The subcommittee has developed comprehensive internal work procedures and principles for the work by experts and procedures for co-operation with external stakeholders, strategic plans and work plans.
- The subcommittee approved its first Practice Note in September 2006. The Practice Note will be brought up for approval at the INTOSAI Governing Board meeting in November 2006. The subcommittee is aiming at presenting 13 Practice Notes for endorsement at the 2007 INCOSAI.
- The co-operation with the IAASB is highly efficient and constructive. The input by INTOSAI experts to IAASB Task Forces has been recognized and deemed as being of great value by the IAASB. The process to appoint experts to different IAASB Task Forces is developing according to plan.
- Practice Note Task Forces have been created and experts have been appointed to two of the Task Forces by the end of September 2006.
- The subcommittee has developed and documented work processes and terms of references for all groups and expert positions within the FAS. A special Court of Audit Experts Group has been established and contributes to the FAS activities on a valuable level.
- Currently 44 positions of experts and back-office experts in different groups are actively contributing to the development work, and during 2007 the number of positions will increase to approximately 65.
- Participating SAIs make tremendous contributions to the work and the subcommittee members are very active and take a mutual responsibility for the outcome of FAS.

Intended outcome of subcommittee work

As formulated in the Memorandum of Understanding between INTOSAI and the IAASB, the Guidelines for Financial Audit will form in-depth guidance to the INTOSAI Auditing Standards. The Guidelines will constitute the fourth level in the existing hierarchy of standards in INTOSAI, which consists of the Lima Declaration, the Code of Ethics and the INTOSAI Auditing Standards.

A guideline will consist of an ISA, which – where applicable – may contain public sector considerations at a general level, and a Practice Note. A Practice Note will explain the application of an ISA to the public sector, the extent to which it is applicable, and what adjustments need to be made by a public sector auditor.

Where considered necessary, a Practice Note may contain detailed guidance on the application of an ISA in the public sector. Guidelines will also be developed by the subcommittee in areas of specific interest to the public sector auditor that are not relevant to the private sector.

Development of the Financial Audit Guidelines

The subcommittee formulated a strategic objective for the project and defined actions to achieve the objective in March 2005.

Participating as members in IAASB Task Forces to write audit standards on current and future projects

The Memorandum of Understanding between INTOSAI and the IAASB was agreed in the beginning of 2004 and revised in 2006. The first appointment of an INTOSAI expert to the IAASB Task Force work was made in March, 2004.

In total INTOSAI has appointed experts to the following Task Forces:

- **ISA 230 – Documentation.** Expert Ms. Kelly Ånerud, Norway and B-O experts Ms. Gail Vallieres, USA and Mr. Inge Danielsson, Sweden.
- **ISA 260 – Communications with those charged with Governance.** Expert Ms. Tove Myklebust, Norway and B-O experts Mr. Filip Cassel, Sweden and Ms. Gail Vallieres, USA.
- **ISA 800 (ISA 801 and 805) – Auditor’s report on special purpose audit engagements.** Expert Mr. Jonas Hällström, Sweden and B-O experts Mr. Martin Dees, the Netherlands and Mr. Robert Cox, New Zealand.
- **ISA 505 – External Confirmations.** Expert Mr. John O’Brian, Canada and B-O expert Ms. Birgit Bach-Nilesen, Denmark.
- **ISA 550 – Related Parties.** Expert: Mr. John Thorpe, United Kingdom and B-O experts: Ms. Zainun Taib, Malaysia and Mr. Uwe Schreiner, Germany.
- **ISA 580 – Management Representation.** Expert position is presently vacant, B-O experts are Mr. Martin Garrido, Chile and Mr. Ennio Colasanti, Italy.

- **ISA 620 – Using the Work of an Expert.** Expert Mr. Claudio Branco, Brazil and B-O experts Mr. András Morvay, Hungary and Ms. Monica Besetsa, Lesotho.
- **ISA – Material Weaknesses in Internal Controls.** Expert Mr. Mohammad F Bajhatt, Saudi Arabia and B-O experts Mr. Robert Cox, New Zealand and Mr. Filip Cassel, Sweden.

The subcommittee has appointed experts to all IAASB Task Forces created since the first Memorandum of Understanding was signed with IAASB.

All Task Forces are still active, except for the Task Force on ISA 230, which has been approved by the IAASB. The INTOSAI expert will stay on as a corresponding member to the ISA 230 Clarity Task Force.

The participation in IAASB Task Forces is a long term commitment, each Task Force works for two to three years revising an ISA. It should be mentioned that the IAASB recently decided to undertake a large project to clarify the ISAs (the “Clarity Project”). This IAASB project will extend the working period for the Task Forces with one to two years each. This, unfortunately, has a severe impact on the pace for producing INTOSAI Practice Notes and will cause some delay in developing Practice Notes for the period proceeding INCOSAI 2007. Still, the Clarity Project is most important and valuable also for the INTOSAI community.

In addition to the participation in IAASB Task Forces the INTOSAI has appointed an expert to represent the INTOSAI on the IAASB Consultative Advisory Group (CAG).

Experts impact on ISA Task Force work

Due to the extensive time frame for an IAASB Task Force to revise an ISA, only one ISA with the participation of an INTOSAI expert has been approved at this stage. It is therefore not possible to draw a final conclusion concerning the impact of INTOSAI experts on the development of the ISAs. Based on approved and exposed drafts of ISAs it is our opinion that the experts have contributed in the following way:

- Provided public sector guidance within the ISA with implicit reference to the public sector,
- Provided input to reformulate issues within the ISA to reflect guidance acceptable for both private and public sector (without direct reference to public sector).

The participation of INTOSAI experts in the IAASB work has been highly accepted by the IAASB. There is an increased awareness of public sector issues and several issues have been

raised in the board meetings of the IAASB. The FAS has received appreciation from IAASB for competent and valuable contributions by INTOSAI experts in IAASB Task Forces.

It is crucial that the approach of INTOSAI experts is consistent in order to have the ISAs accepted for financial audit work in the public sector. In order to reach a common understanding among the INTOSAI experts, the Project Secretariat has annually arranged Reference Panel meetings at the Swedish National Audit Office in Stockholm. On these occasions both active and newly nominated SAI experts get the chance to meet in person to discuss matters arising in their work as experts, as well as get general information on the progress of the project. The invited experts also contribute on issues as the development of the scope of the guidelines, format of the Practice Notes, etc. These meetings have supported the communicative and co-operative ambitions of this project and have served as a leverage of the sense of mutual responsibility amongst the experts.

Writing comment letters on exposure drafts of ISAs where there was no INTOSAI input on the IAASB Task Force

The subcommittee has commented on several ISA Exposure Drafts in line with the procedures for the subcommittee as decided in 2005.

In addition to the subcommittee responses on the draft ISAs the FAS Focus Group has issued responses to the IAASB on both project proposals and, in relation to the Clarity Project, the treatment of existing Public Sector Perspectives, PSPs.

The comments provided by the subcommittee and by the FAS Focus Group have been accepted by the IAASB and noted in the IAASB Task Forces summaries of significant comments. In 2006, the FAS has provided comments on the exposure drafts to ISA 240, 315, 330 (all redrafted), ISA 550 and ISA 600.

Drafting Practice Notes for all ISAs in order to provide special considerations for the public sector

In late 2005, two Practice Notes were issued as drafts, Practice Note to ISA 230 and Practice Note to ISA 240. These Practice Notes were subject to comments from the INTOSAI members due on March 31, 2006. Based on comments received adjustments were made and the Practice Note to ISA 230 was approved by the subcommittee in September 2006 as the first Practice Note ever. The Practice Note to ISA 240 will be approved in December this year. All Practice Note drafts will be exposed on the FAS website.

Several ISAs were revised by the IAASB before the original Memorandum of Understanding between the IAASB and INTOSAI came in force, and in order to develop

Practice Notes to these ISAs within reasonable time, it was decided to create the FAS Practice Note Task Forces (PN TF). Each PN TF consist of two INTOSAI experts and two or three INTOSAI back-office experts. Each PN TF is given the task to develop Practice Notes for up to five ISAs. The ISAs have been grouped together based on relation to other ISAs. The Project Secretariat has ensured the assistance of the IAASB technical staff to each PN TF.

The two first PN TFs were set up in early 2006 (PN TF 1 and PN TF 2). During the autumn of 2006 two more PN TFs will be set up, and in 2007 yet another 2-3 PN TFs.

- PN TF 1

- ISQC 1 – Quality Control for Firms that perform Audits and Reviews of Historical Financial Information, and other assurance and related services engagements**

- ISA 220 – Quality Control for Audits of Historical Financial Information**

- Experts: Mr. Mike Suffield, UK and Mr. Robert Tjon Tsoe Jin, the Netherlands

- Back-office experts: Mr. Roy Glass, New Zealand and Mr. Mohammad Heissat, Jordan

- PN TF 2

- ISA 300 – Planning an Audit of Financial Statements**

- ISA 315 – Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatements**

- ISA 330 – The Auditor’s Procedures in Response to Assessed Risks**

- Experts: Ms. Marcia Buchanan, US and one expert position is vacant

- Back-office experts: Mr. Ömer Kose, Turkey and Mr. Russel Frith, Scotland

According to a recent decision made by the subcommittee, the PN TF 2 will be reorganized and different working procedures will be adopted in order to, as far as possible, reduce the risk of delays caused by the Clarity Project and other factors. The number of ISAs to be developed by PN TF 2 will be extended to include **ISA 320 – Materiality in Planning and Performing an Audit and Evaluation of Misstatements Identified during the Audit** and **ISA 540 – Auditing Accounting Estimates and Related Disclosures (Other than Those Involving Fair Value Measurements and Disclosures)**. PN TF 2 will then have a specific responsibility for corner-stones of the ISAs. The FAS is presently making arrangements for coherent and concentrated working sessions by PN TF 2.

Drafting additional guidance to deal with the special needs of the public sector which together with ISAs and Practice Notes will form the INTOSAI Financial Audit Guidelines

In order to identify the need of guidance beyond the ISAs, the subcommittee undertook a gap-analysis of the differences between the INTOSAI Auditing Standards and the ISAs in the beginning of 2005. The result of the analysis has been formulated in the work plan outlining five additional areas where a need for public sector guidance beyond the ISAs has been identified. The most significant area is related to SAI's responsibilities on compliance audit issues. The task of developing guidelines on compliance issues have been given to the PSC Compliance Audit Subcommittee (CAS). The FAS and CAS have agreed on co-operation in development of financial audit related compliance guidelines, which will form part of the Financial Audit Guidelines. The FAS has upon request from the CAS created a compliance audit expert group to assist the CAS in their developing work.

Other areas identified in the gap-analysis will be attended to after the INCOSAI in 2007.

Current challenges

The subcommittee has identified a number of issues that has had impact on the chances to achieve the goals and that will continue to affect the work of developing guidance in the desired time frame:

- The Clarity Project within the IAASB will, as mentioned, cause a delay seen in relation to FAS' timeline for developing Practice Notes. The subcommittee has discussed actions to reduce this impact, but it will cause delays.
- The work in an IAASB Task Force is a long term commitment for the INTOSAI. The subcommittee has faced situations when INTOSAI experts have been given other responsibilities within their respective SAI, and therefore not been able to fulfill their commitment to the FAS. To replace an expert within an IAASB Task Force without causing too much inconvenience for the Task Force is a challenge for the subcommittee. The Project Secretariat will approach all SAIs to make clear what a serious set-back a broken commitment of an expert creates to our mutual cause.
- The work to identify and appoint suitable experts and back-office experts from the Reference Panel is often time consuming. The Reference Panel is extending and currently comprise of more than 150 experts nominated from different SAIs. There is still a problem to identify experts with both relevant experience and the necessary level of knowledge in English. Experts need to have excellent knowledge in English to be able

to contribute and make sure that the relevant public sector guidance is included in the ISA and Practice Note. The combination of relevant experience and excellent knowledge in English is still scarce.

Taken the impact of the Clarity Project into consideration, the FAS has set up final goals to achieve until INCOSAI 2007. The goal is now set at presenting 13 Practice Notes to the INCOSAI for endorsement in 2007. The previous goal was set at 22 Practice Notes. The total number of Practice Notes endorsed after INCOSAI in 2010 remains. The subcommittee is working actively to reduce the risk of further delays in the development work and to counteract impact of external factors beyond our control.

It should also be mentioned that the subcommittee has developed and adopted working procedures in order to include audit expertise from a large number of SAIs, and to allow for input and comments from SAIs representing different SAI systems. As a consequence of this intentional solution for the development of the guidelines, the time frame for the development of the guidelines and the Practice Notes is extensive. However, making the choice between ensuring the wide acceptability for the guidance using procedures seen below, or having the guidelines developed in a quicker way, the subcommittee considered the acceptability of the guidelines to be of more importance than the actual time for the development. These procedures include:

- Nomination of experts and back-office experts
- Selection and appointment of experts and back-office experts
- Sufficient time for development of the Practice Notes
- Reasonable time for public exposure of the Practice Notes
- Sufficient time for experts to make alterations based on comments to exposure drafts
- Time for the subcommittee to approve the Practice Notes
- Time for making conforming changes in other Practice Notes
- Reasonable time for making translations of the Practice Notes
- Final arrangements for the approval and endorsement procedures within the INTOSAI

Each of these sub-processes needs to be considered when evaluating the time needed to develop a Practice Note. For Practice Notes developed as part of the experts participation in an IAASB Task Force an additional period is needed for the Task Force work (two to three years). The timeframe also has to allow the possibility of re-exposure of a Practice Note for comments, the need to exchange experts and the schedules of INTOSAI committees and subcommittees meetings.

Organizational changes within FAS

The subcommittee has decided to set up expert groups for different issues. The following groups have been created:

- The Focus Group (FG) was set up with a special responsibility for responding to invitations to comment on IAASB project proposals. The FG thus provides public sector input even before an IAASB Task Force is established. The responsibilities of the FG also include to provide the experts in INTOSAI Practice Note Task Forces with comments on their proposals, and to provide input to the IAASB on other public sector issues upon request. The FG, when fully staffed, will have six members. Currently there are four members of the FG.
- The Court of Accounts Expert Group (CEG) was established in 2005 consisting of experts representing Supreme Audit Institutions with the court of accounts model. The CEG works with the development of Practice Notes and identifies the need for specific issues of the court of accounts system to be reflected in the guidance. Experts from Brazil, Turkey, Tunisia and Greece (chair) constitute the CEG.
- The Compliance Audit Reference Expert Group (CAREG) was created in 2006 with the purpose of ensuring consistency between the FAS and the Compliance Audit Guidelines Subcommittee (CAS) within the PSC structure for developing standards and guidance. The CAREG shall assist the CAS and the FAS in providing guidance to the CAS on already existing best practices, standards or guidance used or developed in the respective expert's SAI, comments on drafted guidelines or documents to the CAS to ensure a high quality on all aspects of compliance audit relevant for the guidelines on compliance audit and to ensure the consistency between the Compliance Audit Guidelines and the audit scope decided by the FAS. The CAREG consists of four members of which one member is appointed chair.
- The INTOSAI Clarity Reference Group was recently created with the objective to assist the IAASB in providing suggestions for treatment of existing Public Sector Perspectives in redrafted clarity versions of ISAs. The group will have three members when fully staffed.

Other achievements

Project structure

In order to have the project running in a consistent way and all experts made aware of the expectations, the Project Secretariat has developed draft Terms of Reference and description

of the work processes for all significant groups and processes. These documents have been approved by the subcommittee.

In 2006 all Terms of References have been re-approved to reflect changes in the project. The existing work processes have been updated and re-approved and policy documents on Authority and Scope of the Financial Audit Guidelines as well as Format and Structure of Practice Notes have been issued and approved.

The Terms of Reference for the new Compliance Audit Guidelines Reference Expert Group has been approved by the subcommittee.

Reference Panel nominations

On a yearly basis the Project Secretariat has, on behalf of the subcommittee, asked all SAIs to participate in the development work by nominating their most experienced experts in the areas of standard setting.

Up to the end of September 2006, 44 positions of experts and back-office experts are actively participating in different groups or task forces. In November an additional eight positions will be appointed, and vacancies for four positions be reinstated. In the beginning of next year an additional eight experts will be appointed and at the end of the first half of 2007, approximately 65 positions of experts and back-office experts will have been appointed.

Reference Panel meetings have been held every year since 2004. The last meetings were held in September 2006, when two groups of approximately 20 experts were invited to attend a two days meeting in Stockholm. One of the meetings was for all active experts and back-office experts to discuss issues related to the work. The other meeting was aimed for newly nominated experts. The purpose is to inform them about the work as well as to identify possible future appointments. The Reference Panel meetings have been very useful for the development work.

Funding issues

The project receives funding from the World Bank and the Asian Development Bank. Additional sources of funding are actively searched for by the Project Secretariat. The total project cost for the period 2004-2007 is approximately 11 million USD. The major part of these costs is taken by the respective SAI, in form of expert salaries. The IAASB contributes by expertise and by reimbursing the cost for travel and accommodation for INTOSAI experts when participating in an IAASB Task Force.

The external funding from the World Bank and the Development Bank is primarily used for Reference Panel meetings, subcommittee meetings, translations, printing and to cover some of the cost for the Project Secretariat. Still there is a lack of external funding, currently covered by the Swedish National Audit Office.

Information and communication

To ensure transparency, awareness and interest of this work within the INTOSAI community, the subcommittee has decided to communicate to the SAIs in the following way:

- Updates on on-going activities to all members of the reference panel on a periodical basis, so far eight updates have been issued. From the second quarter of this year the updates have been renamed QPR (Quarterly Performance Reports) and written in a way that they will serve as information to all stakeholders.
- Update on activities issued in each number of INTOSAI Journal (every fourth month), so far a report has been issued to all issues of the journal during 2004, 2005 and 2006.
- Request for nominations of experts on a yearly basis, the third nomination letter was sent in November 2005.
- Printing of a brochure describing the development work (version 2 issued 2005)
- E-mail to all SAIs when a new Practice Note exposure draft is issued on the website for comments, which has been done in November 2005 to address the exposure of Practice Note 230 and Practice Note 240.
- A website with all relevant information presented in a transparent way, the website was launched in November 2005. The website (on the website of the Professional Standards Committee) will be the main instrument to communicate with all stakeholders.

Translation issues

Following a decision by the Professional Standards Committee in June 2006, the subcommittee has decided to translate the guidance in the following way;

- Practice Notes and other developed guidance will be translated into all official languages of INTOSAI before approval by the INTOSAI Governing Board
- Exposure drafts will be exposed in the FAS working language, i.e. English.
- Comments will be accepted in all official INTOSAI languages, although English is preferred.

- International Standards of Auditing will be included in English, and not subject to any translations by the FAS.
- The Project Secretariat will arrange for translations of guidance using the most efficient resources.
- The subcommittee will take on the role to ensure the quality of translated guidance.