



Convergence of Indian Auditing Standards with International Auditing Standards

Dr. Devesh Gupta¹, Dr. Geetika Shukla²

¹Assistant Professor, Pt. Deen Dayal Upadhyay Management College, Meerut

²Associate Professor, Dewan Institute of Management Studies, Meerut

ABSTRACT

The Institute of Chartered Accountants of India (ICAI) has issued a preface to the Standards on Quality Control, Auditing, Review, other Assurance and Related Services (effective from 1st April, 2008). As a result of issuing of this preface, the ICAI has re-classified the existing Auditing and Assurance Standards. The objective of re-classification is to converge our existing Auditing and Assurance Standards with International Standards on Auditing (ISAs) issued by the International Federation of Accountants (IFAC).

The ICAI is one of the founder members of the International Federation of Accountants (IFAC). It is one of the membership obligations of the Institute (IFAC) to actively propagate the pronouncements of the International Auditing and Assurance Standards Board (IAASB), to contribute towards global harmonization and acceptance of the Standards issued by the IAASB. Accordingly, while formulating Engagement and Quality Control Standards, the AASB (ICA) takes into consideration the corresponding Standards, if any issued by the IAASB (IFAC). In addition, the AASB also takes into consideration the applicable laws, customs, usages and business environment prevailing in India within the parameters of the July, 2006 Policy Paper 'A Guide for National Standard Setters that Adopt IAASB International Standards but find it necessary to make limited modifications,' issued by the IAASB.

Need for Convergence

Flowing from the objectives of the IFAC, there are certain obligations on its members which have been codified in the Statements on Membership Obligations (SMOs) issued by the IFAC. The SMO 3, International Standards, Related Practice Statements and Other Papers issued by the IAASB, requires "the members to use their best endeavours to: (a) To incorporate the International Standards issued by the IAASB into their National Standards or related other pronouncements, or where responsibility for the development of National Standards or related other pronouncements lies with third parties, to persuade those responsible to incorporate the International Standards into their National Standards or related other pronouncements; and (b) To assist with the implementation of International Standards or National Standards and related other pronouncements that incorporate International Standards. This includes promoting the use of related Practice Statements, or the development of national pronouncements that incorporate related Practice Statements or provide similar implementation guidance. Although the Constitution of IFAC and SMO 3 acknowledge National Standards, member bodies should, in implementing their obligations of membership, have as a central objective the convergence of National Standards or related other pronouncements with International Standards issued by the IAASB."

The Institute (ICAI), for the first time in 2002, was invited to attend the meeting of the National Auditing Standards Setter (NSSs) of the IAASB. The NSSs comprise of ten countries including India. Participation in the annual NSS meeting is a regular feature for the Institute since 2002. Being a part of the NSSs group is critical on account of the fact that only those Standard setters are invited which:

- Are significantly active in the development of National Auditing Standards, or by way of contributing to the development of International Standards on Auditing (ISAs);
- Have adopted or plan to adopt ISAs, or are demonstrably committed towards the achievement of convergence of International and National Standards;
- Are sufficiently resourced to participate actively in collaborative efforts identified through the activities of the liaison group; or
- Represent the world's largest economies.

International Acceptance of Auditing Standards issued by IAASB

The Standards issued by the IAASB are increasingly gaining acceptance world over. Whereas in some countries, these Standards have been adopted, in some others, they form the primary consideration in the development of National Standards. As per the

2007 Annual Report of the IAASB, “*more than 100 countries use auditing standards that are ISAs, either as written or adapted locally, or national standards that are compared to eliminate the differences.*”

The following provides a snapshot of the acceptance of ISAs in various parts of the world:

- The *Financial Reporting Council* in United Kingdom has already adopted ISAs, with effect from 1st January, 2004.
- The *European Commission* vide its Directive numbered 2006/43/EC of 17th May 2006, has decided to adopt the ISAs subject to the due process.
- The *Canadian Institute of Chartered Accountants* has also decided to adopt ISAs.
- The *Australian Auditing and Assurance Standards Board* as well as the *American Institute of Certified Public Accountants* also plans to revise their Standards based on the ISAs issued by IAASB.
- The *International Organisation of Securities Commission* is currently evaluating conditions on which it can endorse ISAs for use for cross border purposes and the form of such an endorsement.
- A survey by the *International Organisation of Supreme Audit Institutions (INTOSAI)* has revealed that ISAs are used by many national SAIs to develop their detailed Financial Audit Guidelines.
- Recognised by the *World Bank* as benchmark Standards for carrying out its study on Observance of Standards and Codes.
- The *World Federation of Exchanges* has endorsed the IAASB’s process for Standard setting and recognizes the importance of ISAs.

Problems in Convergence with International Auditing Standards

The Institute is committed to the goal of enabling the accountancy profession in India to provide services of high quality in the public interest and which are accepted worldwide. To further this goal, the Institute develops and promulgates technical Standards and other professional bodies and literature. Further, the Institute being one of the founder members of the International Federation of Accountants (IFAC), the Standards developed and promulgated by the AASB under the authority of the Council of the Institute are in conformity with the corresponding International Standards issued by the IAASB.

While developing auditing Standards that conform to the corresponding International Standards of the IAASB, the AASB, time and again, faces with a number of issues. Some of them are as follows:

Convergence *vis a vis* Adoption

Convergence may simply be defined as coming together from different directions to a common point of intersection. The issue of convergence *vis a vis* adoption has also been discussed in the 2004 Report of the IFAC, ‘*Challenges and Success in Implementing International Standards – Achieving Convergence to IFRSs and ISAs*’. The Report notes that a variety of terms have been coined to describe the extent of adoption, such as harmonized, largely harmonized, etc.

In July 2006, the IAASB came out with a policy on modifications to the Standards issued by the IAASB. The policy titled, ‘*A Guide for National Standard Setters that Adopt IAASB’s International Standards but find it Necessary to make Limited Modifications*’ sets out the policy of the IAASB on the question of what modifications may a National Standard Setter (NSS) that adopts International Standards (ISs) promulgated by the IAASB as its National Standards (NSs) make to the ISs.

Procedure of Convergence with International Auditing Standards

It is quite clear that the IAASB is revising and/ or redrafting the entire suite of its existing Standards pursuant to its clarity project. In addition, it is also bringing out a few new Standards. As a result, the IAASB frequently issues Exposure Drafts (EDs) of these revised and/ or redrafted or new Standards. The comment period for each such Exposure Draft is six months. Thereafter, the comments are considered by the IAASB and the proposed Standard, revised, if necessary, is sent to the Public Interest Oversight Board (PIOB) for final approval. The issuance of a final Standard therefore, normally, takes at least one year. This process of the AASB also requires about one year for a Standard to be finally issued. In this context, it may, however, also be noted that despite the fact that the IAASB is frequently issuing revised and/ or redrafted International Standards under its clarity project, these revised/ redrafted Standards would be effective only after December 15, 2009.

Implementation Guidance

It is important to note the fact that the IAASB's Standards are quite generic in nature, but with more than 157 member bodies spread out in 123 countries of IFAC to serve, it would not be possible for the IAASB to accommodate a country's specific legal and regulatory requirements and/ or cultural and trade practices and customs in the Standards formulated by it. The aim of IAASB while formulating ISAs is to propound principles of auditing which are fundamental to carrying out an effective audit of financial statements. The national standards setters can make the necessary modifications to the IAASB's Standards arising out of their legal/ statutory requirements and/ or trade/ cultural practices/ customs in the Application and Other

Explanatory Material section of the Standard in accordance with the requirements set out in the July 2006 IAASB policy paper. Alternatively, they can bring out implementation guides to help the auditors in their jurisdiction guiding them on implementing the requirements of the ISAs.

Having regard to exact requirements of the Standards being issued by the IAASB under its Clarity Project, the AASB decided to *bring out implementation guides* to assist the practitioners in understanding the Standards better and apply them in various practical situations. As stated earlier, the AASB has recently issued an *Implementation Guide on SQC 1* and a *Guide to Risk-based Audit of Financial Statements*. As a part of its future work plan, it intends to bring out implementation guide in all significant areas and update the existing implementation guides as and when new Standards are issued.

Enhancing Professional Skill Sets

Keeping in view the series of continuous developments in the field of audit, it is imminent for the Institute to organize training programmes, workshops and such other awareness programmes. Absorption of the requirements of new Standards and corresponding changes required to the audit methodology at the members' end would need time. The Institute would also need to make concerted efforts to help members understand the new Standards and resolve any implementation issues or other concerns that may arise there from. In this context, it is necessary that the focus of such learning activities is on providing knowledge about technology and risk assessment techniques including knowledge of macro-economic environment, industry-specific issues, etc.

Conclusion

Convergence of Indian Auditing Standards with the International Auditing Standards has been a conscious policy of the Institute. From the first Auditing Standard, which was issued in 1985, corresponding to the then International Auditing Guideline(s) to the most recent Standards on Auditing, the Institute has endeavoured to harmonise with the International Standards. In early 2007, the IAASB had issued thirty eight engagement Standards. As against these 38 Standards of the IAASB, the Institute was yet to issue Standards corresponding to the following some International Standards:

- ISA 545, *Auditing Fair Value Measurements and Disclosures*
- ISA 701, *Modifications to the Independent Auditor's Report*
- ISAE 3000, *Assurance Engagements other than Audits or Reviews of Historical Financial Information*

Though the IAASB embarked on its Clarity Project in 2004, a major landmark in the formulation of the International Standards came in 2003 when the IAASB issued two new Standards, ISA 315, '*Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*', and ISA 330, '*The Auditor's Procedures in Response to Assessed Risks*', and revised two of its existing Standards viz., ISA 200, '*Objectives and General Principles Governing an Audit of Financial Statements*', and ISA 500, '*Audit Evidence*'. These four Standards were collectively known as the *Audit Risk Standards*.

These Standards were effective in respect of the audit of financial statements for periods beginning on or after December 15, 2004. Issuance of these four Standards gave rise to conforming amendments/ revision to almost the entire suite of the International Standards on Auditing. Accordingly, revised International Standards on Auditing were issued by the IAASB during the period 2004 and were effective for all audits of financial statements for the periods beginning on or after December 15, 2004.

Since 2007, when the AASB initiated the process of issuing Standards corresponding to the International Standards on Auditing issued by the IAASB under the Clarity Project, it faces a daunting task of not only making amendments to the writing conventions for Standards but also of revising the almost entire suite of its Standards. The following paragraph provides a gist of the major differences in existing Auditing Standards of the Institute *vis a vis* the IAASB's International Standards and the progress achieved by the AASB to minimize such differences in conjunction with the Clarity Project.

"In addition, the Institute has already embarked on the revision of existing Code of Ethics to bring it in line with the Code of Ethics issued by IFAC, including ironing out the structural differences between the two Codes. The difference in the structuring of the two Codes of Ethics has been leading to difficulties while drawing corresponding reference from the IFAC Code of Ethics to the Institute's Code of Ethics. For example, paragraph 1 of the International Standard on Quality Control (ISQC) 1 draws a reference to Parts A and B of the IFAC Code. Since the Institute Code of Ethics does not contain such corresponding Parts A and B, while drafting the corresponding Standard on Quality Control (SQC) 1, the reference had to be drawn to the entire Code of Ethics of the Institute".

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