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PIN-PA-1: Introduction to Audits Performed under International Standards

INTRODUCTION

In an increasingly global economy, auditors must be able to address the needs of clients with international reach. That may translate into auditing international affiliates of their local clients or, conversely, local affiliates of entities based abroad. Those scenarios require an expanded set of skills for American audit firms, as many other jurisdictions mandate that financial statements be prepared using International Financial Reporting Standards (IFRS) and that the audits of those financial statements be conducted in accordance with International Standards on Auditing (ISAs).

PPC's Practice Aids for Audits Performed under International Standards provide a streamlined, technically sound audit approach for nonlisted commercial entities, located in the United States or abroad, that follow IFRS. These *Practice Aids* provide auditors a flexible, adaptable audit process that is thorough, yet practical; effective, yet efficient. PPC customers will find the audit approach presented in the *Practice Aids* to be consistent with that of other PPC U.S. audit products, making it easily integrated into existing firm practices and quality control procedures. The audit approach in these *Practice Aids* further enhances audit quality for international engagements by ensuring compliance with ISAs.

THE SCOPE OF *PPC's PRACTICE AIDS FOR AUDITS PERFORMED UNDER INTERNATIONAL STANDARDS*

PPC's Practice Aids for Audits Performed under International Standards are intended for use by practitioners in the United States of America who are conducting audits in accordance with the ISAs. They are designed to address audits of nonlisted commercial entities, located in the United States or abroad, that are not public interest entities and that follow IFRS.

These *Practice Aids* include—

- Audit programs that can be easily tailored to address the risks associated with your individual audit engagements.
- A complete, up-to-date set of easy-to-use practice aids.
- Examples of the most commonly used ISA auditor's reports.

PPC's Practice Aids for Audits Performed under International Standards do not address engagements where the auditor is performing an examination of the design and operating effectiveness of internal control over financial reporting that is integrated with the audit of the financial statements. They also do not address the additional regulatory requirements associated with an audit of a listed entity.

International Financial Reporting Standards

IFRS are a single set of accounting and financial reporting standards developed by the International Accounting Standards Board (IASB). They are intended for use globally, for all types of economies, from developing countries to emerging markets, to well-established industrialized nations. The purpose of IFRS is to provide financial statement users with consistent and comparable information across borders. According to the IFRS Foundation, the standards are currently legally approved for use in over 100 countries, including the European Union and more than two-thirds of the G20 nations.

The standard-setting body behind IFRS, the IASB, is part of the IFRS Foundation, an international public-interest organization based in London. The 14-member Board is appointed and overseen by 22 Trustees. The Trustees answer to IFRS Foundation Monitoring Board of public authorities, which includes representatives of the Board and members of the Growth and Emerging Markets Committee of the International Organization of Securities Commissions (IOSCO), the European Commission (EC), the Financial Services Agency of Japan (JFSA), the U.S. Securities and Exchange Commission (SEC), the Brazilian Securities Commission (CVM), and the Financial Services Commission of Korea (FSC).

International Standards on Auditing

ISAs are established by the International Auditing and Assurance Standards Board (IAASB). The IAASB is an independent standard-setting board overseen and supported by the International Federation of Accountants (IFAC), a global organization with 175 member entities and associates representing 130 nations and jurisdictions.

The ISAs are codified in a manner American auditors will recognize, as the AICPA used the IAASB's model for the clarification and convergence of the U.S. Auditing Standards (AU-Cs). U.S. and International auditing standards are similar; however, there are a number of important differences, which are highlighted as Practical Considerations throughout these *Practice Aids*.

Ethical Requirements

In addition to the IAASB, the IFAC oversees the International Ethics Standards Board for Accountants (IESBA). The IESBA issues the *Code of Ethics for Professional Accountants* (Code of Ethics), which includes standards relevant ethical requirements, including independence. American CPAs need to be mindful of both AICPA and IESBA ethical standards when reporting on ISA engagements. These *Practice Aids* primarily address AICPA independence and other ethical requirements, as they are intended for use by practitioners in the United States. If used outside the United States, practitioners should refer to and comply with the IESBA *Code of Ethics*.

SPECIAL CONSIDERATIONS FOR INTERNATIONAL AUDITS

One area of special consideration for auditors on an international engagement is group audit implications. As previously noted, U.S. and International auditing standards are quite similar; there are differences, however, and some of these variances occur in this area. For example, ISA 600 does not allow the auditor's report on group financial statements to make reference to a component auditor unless required by law or regulation do so. If the entity is an affiliate or has international affiliates, failure to comply with ISA requirements for group audits could result in an audit failure. The audit programs in these *Practice Aids* have been designed with planning procedures and practical considerations for group audits. In addition, the *Practice Aids* include template forms for drafting group and component auditor communications, a worksheet for use determining component materiality, and other items of consideration when performing a group audit.

While U.S. and International auditing standards are largely converged, the same cannot be said for U.S. GAAP and IFRS. While the FASB and IASB have participated in convergence projects and collaborated in some areas, there are many differences in the two sets of accounting standards. Practitioners need to be familiar with relevant accounting standards when conducting an audit of an entity with financial statements prepared in accordance with IFRS.

One of the fundamental areas of divergence between the two sets of accounting standards is the increased focus on fair value measurement in IFRS. Therefore, more time and resources will be spent by auditors in testing fair value measurements than is customary in audits of U.S. GAAP financial statements. Due to its subjective nature, auditors will need to be prepared to apply professional skepticism when evaluating management's inputs and assumptions. The audit programs in these *Practice Aids* have been fully incorporated to include audit procedures and Practical Considerations addressing fair value considerations in the relevant audit areas.

Similarly, impairment testing is more pervasive under IFRS than U.S. GAAP. Annual impairment testing requirements apply not only to indefinite-lived assets and goodwill, but also to all fixed assets, intangible assets and other assets; equity method investments in associates and joint ventures; consolidated subsidiaries; and held-to-maturity investments. In addition, unlike U.S. GAAP, in many cases an impairment loss may be reversed in a future period if evidence supports the change in value. As with fair value measurements, these are very subjective areas, requiring a high degree of judgment and professional skepticism on the part of the auditor. The audit programs in these *Practice Aids* have been designed with impairment testing and impairment loss reversal procedures and practical considerations in the relevant audit areas.