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## **Agenda Item**

# **4**

**Board:** International Ethics Standards Board for Accountants

**Meeting Location:** Millennium Hotel, New York, USA

**Meeting Date:** April 27-28, 2009

### **Impact Assessments**

#### **Objective of Agenda Item**

1. The objectives of this agenda item are:
  - (a) To report on progress made in developing an impact assessment process for IFAC; and
  - (b) To obtain the views of the participants on a number of issues concerning the development of the impact assessment process.

#### **Background**

2. IFAC staff has commenced a project to develop an impact assessment process for IFAC. This is done in consultation with an International Auditing and Assurance Standards Board (IAASB) task force and IFAC staff group. The IFAC staff group includes representatives of the various IFAC boards and committees (including the IESBA), the Compliance Advisory Panel and the Communications department.
3. The impact assessment process proposed for IFAC will submit the development of a proposed new standard to a systematic and structured approach, and provide credible evidential bases for the proposals of a standard-setting board. It will require the board to:
  - (a) Set out in clear and simple language the nature of a problem, the objective(s) of the board in addressing the problem, the options that were considered in achieving the objective(s), and the information used to inform the analysis of the options, as well as the final decision(s) of the board in regard to the problem; and
  - (b) Document and communicate this process.
4. In developing the proposed impact assessment process, IFAC staff has been guided by the following criteria:
  - (a) Incorporating the impact assessment process into the due process and documenting the impact assessment, including the cost-benefit analysis (in the case of IFAC referred to as the “impact analysis”), in the explanatory memorandum that accompanies the exposure draft of a proposed new standard and in the basis for conclusions that accompanies the final standard.

- (b) The need to make the impact assessment scalable. In other words, its scope and depth depend on the nature of the problem being addressed.
- (c) The importance of developing an approach that is practical and can be applied by IFAC staff responsible for managing projects of their respective boards.

*Impact Assessment Process and Relationship to Due Process*

5. It is proposed that the impact assessment steps are considered at various stages during the due process. For this purpose, the following project stages have been identified based on the due process:
  - (a) Development of a project proposal.
  - (b) Development of an issues paper, after approval of the project based on the proposal. More than one issues paper may be developed during this stage. This stage may also include:
    - i. A public forum or roundtable, or the development of a consultation paper to solicit views on issues under consideration; or
    - ii. A field test of the application of the proposals.
  - (c) Development of an exposure draft of the proposed standard. This includes the development of an explanatory memorandum to accompany the exposure draft.
  - (d) Development of a summary of significant comments received on the exposure draft. The significant comments may be presented in more than one paper during this stage.
  - (e) Development of the final standard. This includes the development of a project summary, basis for conclusions and impact analysis document.
6. The impact assessment steps are as follows:<sup>1</sup>
  - (a) Determine the nature and magnitude of the problem and the need for action by the board (considered during the project proposal stage).
  - (b) Determine the objective(s) of the board in addressing the problem (considered during the project proposal stage).
  - (c) Identify the options to achieve the objective(s) (considered during the issues paper stage and when developing the proposed exposure draft for approval).

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<sup>1</sup> The impact assessment steps are adapted from those presented in *Hints & Tips for Writing a Regulatory Impact Statement/Business Compliance Cost Statement (RIS/BCCS)* developed by the Ministry of Economic Development, Wellington, New Zealand. They are also in line with those in the Mark/2007/15/F – Study on International Standards on Auditing, *Evaluation of the Possible Adoption of International Standards on Auditing (ISAs) in the EU – Interim Report* (21/08/2008). Paragraph 57 of this report notes that the impact assessment reporting format recommended by the European Commission depicts the following major (methodological) steps:

- (a) Procedural issues and consultation of interested parties;
- (b) Problem definition;
- (c) Objectives;
- (d) Policy options;
- (e) Analysis of impacts;
- (f) Comparing the options; and
- (g) Monitoring and evaluation.

- (d) Analyze the impact of the preferred option for each key issue and the overall impact of the proposed new standard (considered during the issues paper stage and when developing the proposed exposure draft for approval). (See paragraph 12.)
  - (e) Consult relevant stakeholders (considered throughout the process and, in particular during the exposure draft stage).
  - (f) Conduct an overall assessment and draw a conclusion (considered during the development of the issues paper and proposed exposure draft stages).
7. The proposed impact assessment process will not add or delete any stages of the existing due process. Many of the impact assessment steps are already considered in the existing due process stages. The results of the impact assessment steps are brought together and documented in the explanatory memorandum that accompanies the exposure draft. The explanatory memorandum will include an analysis of the overall impact of the proposed new standard and of the preferred option for each key issue addressed during the development of the proposed new standard. The impact assessment is further informed by consultation through the exposure draft process. The final impact assessment, including the impact analyses (see paragraph 12), is documented in the basis for conclusions.
8. It is proposed that the explanatory memorandum contain the following:
- (a) Statement of the nature and magnitude of the problem, and the need for action by the board.
  - (b) Statement of the objective(s) of the board in addressing the problem.
  - (c) Statement of the options that were considered in achieving the objective(s).
  - (d) Analyses of the impact of the preferred options and the overall impact of the proposed new standard (see paragraph 12).
  - (e) Statement of consultation to date.
  - (f) Overall assessment and conclusion.
9. The explanatory memorandum is particularly important for obtaining feedback from stakeholders on the board's analyses of the overall impact of the proposed new standard and of the preferred option for each key issue. At this stage, selected respondents may be requested to conduct a field test of the proposed new standard to assist in further informing the impact analyses.

#### *Proposed Impact Analysis*

10. It is proposed that the overall impact of the proposed new standard be analyzed. The template below has been developed for this purpose. In addition, it is proposed that the preferred option for each key issue addressed during the development of the proposed new standard be analyzed. The template may assist in this regard, but is not required.
11. The template is based on IFAC staff's research on various forms of cost-benefit analysis, and also takes account of the *Effect Analysis* of the International Accounting Standards Board (IASB). It identifies who will be affected by the preferred option / proposed standard, how

they will be affected, and to what extent they will be affected. It provides for an analysis of the primary impacts (for example, in the case of the IAASB, the impact on audit effectiveness and on work effort), and for other impacts, if any. The extent (size) of the impact is measured in qualitative (not quantitative) terms, using a simple 5-point directional scale. The scale takes account of the type (increase or decrease) and relative size of the impact (small or large).

12. The explanatory memorandum that accompanies the exposure draft, and the basis for conclusions, will contain the template analyzing the overall impact of the (proposed) new standard and, if used, the templates analyzing the impact of the preferred option for each key issue. To enhance the flow of the explanatory memorandum / basis for conclusions, it is proposed that brief descriptions of the analyses of the impact of the preferred options and the overall impact of the (proposed) new standard are included in the body of the document, and that the completed template(s) are presented in an appendix.

**Note:** Guidance on filling out the template is presented in italics and brackets.

<b>Subject</b> _____ <i>[Describe the subject being analyzed, which is either the Board's preferred option for dealing with a key issue or the overall impact of the proposal.]</i>			
<b>Primary Impacts</b>	<b>Size and Type of Impact</b>	<b>Applicability (Note 1)</b>	<b>One-off / recurring</b>
<i>[Describe who is affected]</i> <i>[Identify area of impact] increases/decreases because ... [i.e., describe how they are affected]</i>	<i>[Insert size and type: Large increase, Small increase, None, Small decrease, Large decrease]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>
<i>[Describe who is affected]</i> <i>[Identify area of impact] increases/decreases because ... [i.e., describe how they are affected]</i>	<i>[Insert size and type: Large increase, Small increase, None, Small decrease, Large decrease]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>
<b>Other Impacts</b>	<b>Size and Type of Impact</b>	<b>Applicability</b>	<b>One-off / recurring</b>
<i>[Describe who is affected]</i> <i>[Identify area of impact] increases/decreases because ... [i.e., describe how they are affected]</i>	<i>[Insert size and type: Large increase, Small increase, None, Small decrease, Large decrease]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>
<i>[Describe who is affected]</i> <i>[Identify area of impact] increases/decreases because ... [i.e., describe how they are affected]</i>	<i>[Insert size and type: Large increase, Small increase, None, Small decrease, Large decrease]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>

<i>affected]</i>			
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Note 1: Indicate whether the impact is for all entities or limited to specific industries, particular types of entity, or entities in particular jurisdictions. In particular, the difference between the impact on small and large firms should be considered.

Note 2: Additional rows should be added as considered necessary. It may be helpful to categorize the area of impact and show the overall impact per category. For example, in the case of the IAASB, different stakeholders may be affected by an increase / decrease in work effort as a result of a proposed new requirement. The impact on work effort per stakeholders is shown as one category, and the overall impact on work effort determined.

13. The appendix contains an example of the template developed by the IAASB task force for consideration by the IAASB in June.

### *Proposed Guidance*

14. IFAC staff is developing a proposed guide that provides background to the impact assessment process for IFAC, guidance on how to incorporate the impact assessment steps into the due process, and guidance on completing the impact analyses.

### **Consultation to Date and Planned Consultation**

15. The IFAC staff group is being consulted as the project progresses.
16. IFAC staff presented the principles of the proposed impact assessment process to the Consultative Advisory Group of the International Accounting Education Standards Board (IAESB) on February 6. IAASB task force chairman, John Fogarty, will present the proposed impact assessment process at the IAASB-National Standards Setters meeting on April 23-24. Presentations to the other boards and, where applicable, their consultative advisory groups, and committees are planned during 2009.
17. The IAASB task force will present the proposed impact assessment process at the IAASB meeting on June 15-19.

### **Testing the Process**

18. After the proposed impact assessment process is approved by the IAASB, the IAASB will be asked to pilot test it for a project to commence in the third quarter of 2009. It is proposed that this is followed by pilot tests on projects of the IESBA, the International Public Sector Accounting Standards Board and the IAESB.
19. The results of the field tests will be used to modify the proposed process. In addition, they will become examples to be appended to the proposed guide.

### **Action Requested**

20. Participants are asked for their views on the following:

- (a) The overall structure and complexity of the proposed impact assessment process (see paragraph 6), and its relationship with the due process (see paragraph 5).
  - (b) The impact analysis, as presented in paragraphs 10-13, and the proposed approach to qualitatively measuring the impact of the options.
  - (c) The application of the proposed impact assessment process. At present, the process is detailed and relevant to the development of a proposed new standard. It is therefore proposed that the process is scalable to the magnitude of the problem and the board's objective(s) in addressing the problem.
21. Participants are also asked to provide any other advice or ideas concerning the development of the proposed impact assessment process.

## Appendix: Impact Analysis Template Developed for the IAASB

**Note:** Guidance on filling out the template is presented in italics and brackets.

<b>Subject</b> _____ <i>[Describe the subject being analyzed, which is either the Board's preferred option for dealing with a key issue or the overall impact of the proposal.]</i>			
<b>Audit Effectiveness</b> <b>(Note 1)</b>	<b>Size and Type of Impact</b> <b>(Note 2)</b>	<b>Applicability</b> <b>(Note 3)</b>	<b>One-off /</b> <b>recurring</b>
Audit effectiveness increases/decreases because.... <i>[Narrative description of impact describing the reasons for the increase in audit effectiveness, including, where applicable, who is affected and how they are affected]</i>	<i>[Insert size and type: Large increase, Small increase, None, Small decrease, Large decrease]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>
<b>Work Effort</b>	<b>Size and Type of Impact</b> <b>(Note 4)</b>	<b>Applicability</b>	<b>One-off /</b> <b>recurring</b>
	<i>[Insert size and type of overall impact on work effort: Large increase, Small increase, None, Small decrease, Large decrease]</i>		
Auditors (Include consideration of any difference of the costs for small vs. medium vs. large firms) (Notes 5 and 6) Work effort increases/decreases because... <i>[Narrative description of impact describing who is affected and how they are affected]</i>	<i>[Insert size and type: Large increase, Small increase, None, Small decrease, Large decrease]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>
Management or, where appropriate, those charged with governance (Audit client) (Note 7) Work effort increases/decreases because... <i>[Narrative description of impact describing who is affected and how they are affected]</i>	<i>[Insert size and type]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>
Other stakeholders (such as audit oversight bodies) Work effort increases/decreases because... <i>[Narrative description of impact describing who is affected and how they are affected]</i>	<i>[Insert size and type]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>

<i>affected]</i>			
<b>Other Impacts</b>	<b>Size and Type of Impact (Note 8)</b>	<b>Applicability</b>	<b>One-off / recurring</b>
	<i>[Insert size and type of overall impact: Large increase, Small increase, None, Small decrease, Large decrease]</i>		
Auditors (Note 5) Other impact occurs because... <i>[Describe how they are affected]</i>	<i>[Insert size and type: Large increase, Small increase, None, Small decrease, Large decrease]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>
Management or, where appropriate, those charged with governance Other impact occurs because... <i>[Describe how they are affected]</i>	<i>[Insert size and type]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>
Investors (Note 9) Other impact occurs because... <i>[Describe how they are affected]</i>	<i>[Insert size and type]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>
Other stakeholders (such as audit oversight bodies) Other impact occurs because... <i>[Describe how they are affected]</i>	<i>[Insert size and type]</i>	<i>[If appropriate, describe applicability]</i>	<i>[Insert O or R]</i>

Note 1: Audit effectiveness is meant to encompass reviews, compilations, and any other assurance services.

Note 2: Present the size and type of the overall impact on the audit effectiveness.

Note 3: Indicate whether audit effectiveness, work effort, or other impact is affected for all entities or is limited to specific industries, particular types of entities, or entities in particular jurisdictions. In particular, the difference between the impact on small and large firms should be considered.

Note 4: Present the size and type of the impact on each stakeholder, as well as the size and type of the overall impact on work effort.

Note 5: The references to Auditors are assumed to include Supreme Audit Institutions.

Note 6: For example, in the case of the IAASB, the impact of a new requirement for audit planning may have a larger impact on small firms than large firms, while a new requirement relating to the work of internal auditors may have little or no impact on smaller firms.



- Note 7: For example, in the case of the IAASB, a new requirement for management to use an expert may create additional costs and effort for management to interact with the expert, and for management's expert to interact with the auditor's expert.
- Note 8: Present the size and type of the impact on each stakeholder, as well as the size and type of the overall other impacts.
- Note 9: Investors are considered to be a representative subset of users. The "Framework for the Preparation and Presentation of Financial Statements," adopted by the IASB in April 2001, indicates that, for a profit-oriented entity, as investors are providers of risk capital to the enterprise, the provision of financial statements that meet their needs will also meet most of the needs of other users that financial statements can satisfy.