

IV. Accounting and Auditing Standards

This chapter describes the accounting and auditing standards that govern the preparation of external financial reports and their audit. It comprises 13 sections as follows:

Part One: Accounting Standards

- 1 – Introduction – reviews the historical development of Sri Lankan accounting standards.
- 2 – Accounting Standards Committee (ASC) – outlines the role, composition and activities of ASC, the primary accounting standard-setting body.
- 3 – Accounting Standard Setting Process – describes the accounting standard-setting process.
- 4 – Sri Lankan Accounting Standards – describes Sri Lankan accounting standards.
- 5 – Conformity with International Accounting Standards (IAS) – examines differences between Sri Lankan accounting standards and IASs.
- 6 – Public Sector Accounting Standards – describes the standards that govern public sector reporting.
- 7 – Taxation Reporting Requirements – reviews the relationship between financial reporting and taxation reporting practices.

Part Two: Auditing Standards

- 8 – Introduction – describes the historical development of Sri Lankan auditing standards.
- 9 – Auditing Standards Committee (AuSC) – outlines the role, composition and activities of the AuSC, which is the auditing standard-setting body.
- 10 – Auditing Standard Setting Process – discusses the audit standard-setting process.
- 11 – Sri Lankan Auditing Standards – describes Sri Lankan auditing standards.
- 12 – Comparison with International Standards on Auditing (ISA) – examines differences between Sri Lankan auditing standards and ISAs.
- 13 – Issue Synopsis: Accounting and Auditing Standards – summarizes the issues identified in this chapter.

Part One. Accounting Standards

1. Introduction

Before 1970, Sri Lankan financial reporting requirements were based upon the prescriptions of the *Companies' Ordinance of Ceylon*, contemporary UK legislation and the recommendations of ICAEW. On 1 April 1970, ICASL issued the first SLAS, SLAS I: *The treatment of dividends duly grossed in the balance sheets and appropriation statements of companies*.⁷⁷ However, the use of SLASs was not legally mandated, other than for publicly quoted companies, financial institutions and insurance companies.⁷⁸

A number of Sri Lankan finance companies collapsed in the late 1980s and early 1990s. Many small depositors lost their savings and significant fiscal costs were incurred in bailouts. In response, the Government established the *Presidential Commission on Finance and Banking* to investigate and strengthen financial sector arrangements. Among other things, the *Commission* recommended that international accounting and auditing standards be adopted to improve financial disclosure.⁷⁹

To this end, the *Sri Lanka Accounting and Auditing Standards Act (No. 15) 1995* was developed by government officials, the accountancy profession, and representatives from the commercial and financial sectors. Together with subsidiary regulations, the Act defines certain enterprises as SBEs and governs the preparation, presentation and audit of financial statements of SBEs for periods commencing on or after 1 January 1999.

The Act requires all SBEs to prepare and present financial statements in accordance with SLASs. It also empowers ICASL to adopt suitable accounting standards from time to time. These standards have legal effect once they have been published in the *Gazette*. SLASs relating to banks must have the concurrence of the Banking Supervision Department of the Central Bank. The ASC, an ICASL committee, was established to undertake the accounting-standard-setting process. The Act also established the independent SLAASMB to monitor SBE compliance with SLASs.

The Sri Lankan regime for promulgating accounting standards, and monitoring compliance with these standards, is a world leader. It is particularly appropriate for application in developing and transitional

⁷⁷ Wickramarachchi, M. W. 1978. *Accounting Research Study No. 6: An Examination of Selected Financial Reporting Practices of Public Companies in Sri Lanka*. University of New England, Armidale: Department of Accounting and Financial Management. p. 4.

⁷⁸ US State Department. 1999. *Country Commercial Guides for FY 2000: Sri Lanka*.

⁷⁹ World Bank. 1998, July 31. *Sri Lanka: Financial Sector Reforms*. p. 3.

markets, which tend to lack effective investor monitoring. In this respect, other developing and transitional countries should be encouraged to examine the Sri Lankan model with a view to strengthening their financial reporting and disclosure practices.

2. Accounting Standards Committee (ASC)

ICASL established the ASC in accordance with the *Sri Lanka Accounting and Auditing Standards Act (No. 15) 1995*. This Committee is responsible for making recommendations and assisting the Institute to develop and promulgate SLASs.

The ICASL promulgates SLASs in accordance with Sections 2(1) and 8(1) of the Act. In keeping with the recommendations of the *Presidential Commission on Finance and Banking*, SLASs are directly based on the IASs promulgated by the IASB. It is a condition of ICASL's IFAC membership that the Institute works towards implementation of IASs.

The first Committee under the Act was established in June 1996. Within six months it had reviewed the IAS Framework and all IASs (up to IAS 27), and published a book of Sri Lankan Accounting Standards.⁸⁰

The ASC comprises 12 members, who are drawn from professional accountancy bodies, regulatory bodies, and user groups (see Table 11). Members are appointed for four-year terms under Section 10(2) of the *Sri Lanka Accounting and Auditing Standards Act (No. 15) 1995*. In 1995, the *Presidential Commission on Finance and Banking* recommended that resources be appropriated to ICASL to support ASC's activities, however no action was taken and the ASC's activities are funded entirely by ICASL (In contrast to the SLAASMB).

Table 11. Membership of the Accounting Standards Committee⁸¹

Organization	Members	Nomination and Appointment
ICASL	1	President.
	5	Five other members nominated by the Institute's Council.
CIMASL	1	Nominated by CIMASL.
Registrar of Companies.	1	Registrar of Companies.

⁸⁰ ICASL. 1999. *Sri Lanka Accounting Standards 1999*. President's Message to 1999 Edition. Colombo: ICASL.

⁸¹ Ratnayake, Ajith S. (Director-General, SLAASMB). 2000. *Scope and Functions of the Accounting and Auditing Standards Monitoring Board*. www.sec.gov.lk

Table 11. Membership of the Accounting Standards Committee *(continued)*

Organization	Members	Nomination and Appointment
Central Bank of Sri Lanka	1	Nominated by the Governor of the Central Bank.
SEC	1	SEC Director-General.
Ceylon Chamber of Commerce.	1	Company director or other person with extensive senior management experience in a specified business enterprise, nominated by the Ceylon Chamber of Commerce.
Federation of Chambers of Commerce and Industry of Sri Lanka	1	Company director or other person with extensive senior management experience in a specified business enterprise, nominated by the Federation of Chambers of Commerce and Industry of Sri Lanka.

3. Accounting Standard Setting Process⁸²

The ASC's standard-setting process is broadly similar to that of the IASB and the US Financial Accounting Standards Board (FASB), except that the process focuses on reviewing IASs for adoption in Sri Lanka. Although the Committee aims to achieve complete consistency between SLAs and IASs, modifications are sometimes made to reflect country-specific factors. The ASC's standard-setting process is as follows:

- The ASC invites interested parties to comment on the targeted IAS.
- The ASC appoints a subcommittee, chaired by an ASC member, to study the IAS.
- The subcommittee studies the IAS, taking into consideration any comments from interested parties.
- The subcommittee prepares a draft SLAS, modified as necessary, and presents it to the ASC.
- The ASC conducts a public seminar, to explain the proposed SLAS, and to obtain further public comments.
- The subcommittee reviews the draft SLAS, taking into consideration any further public comments, and recommends the SLAS for adoption to the ASC.
- The ASC discusses the proposed standard with the subcommittee Chair and determines the nature and contents of the final standard

⁸² Primary Source: Ratnayake, Ajith S. (Director-General, SLAASMB). 2000. *Scope and Functions of the Accounting and Auditing Standards Monitoring Board*. www.sec.gov.lk

that it will recommend to the ICASL Council for adoption. Under ASC rules, at least three-quarters of members must support a standard, before it is recommended to the ICASL Council for adoption.

- The ICASL Council then adopts the SLAS in accordance with Section 2 of the *Sri Lanka Accounting and Auditing Standards Act (No.15) 1995*.
- The adopted SLAS must be published in the *Gazette*. It becomes effective from the date of publication, or from a later date as specified in the SLAS.
- In order to be gazetted, the SLAS must be translated into Sinhala and Tamil. The first batch of 28 SLASs was translated with ADB assistance under the Financial Management Training Project.

The first set of SLASs promulgated through this process was published in *Gazette Extraordinary No.1056/19* (2 December 1998). These standards applied to financial reporting on financial periods commencing on, or after, 1 January 1999.

4. Sri Lankan Accounting Standards (SLASs)

Twenty-eight SLASs were effective as of 30 June 2001. Table 12 lists the effective SLASs and identifies divergences with IASs. Differences between SLASs and IASs are examined more closely in the following section.

Table 12. Sri Lankan SLASs as at 30 June 2001⁸³

No. Title	Parentage	Effective
... Framework for the Preparation and Presentation of Financial Statements	IAS Framework	
3 Presentation of Financial Statements	IAS 1	Apr 2000
5 Inventories	IAS 2	Jan 1996
8 Depreciation Accounting	IAS 4	Apr 1986
9 Cash Flow Statements	IAS 7	Jan 1996
10 Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies	IAS 8	Jan 1996
11 Research and Development Costs	IAS 9 (superseded by IAS 38)	Jan 1996
12 Contingencies and Events Occurring After the Balance Sheet Date	IAS 10 (superseded by revised IAS 10 and IAS 37)	Jan 1980

⁸³ Sources:

- ICASL. 1999. *Sri Lanka Accounting Standards 1999*. Colombo: ICASL.
- SLAAMSB. 2001. *Status of Sri Lankan Accounting Standards in Relation to International Standards*. www.slaasmb.org

Table 12. Sri Lankan SLASs as at 30 June 2001 (continued)

No.	Title	Parentage	Effective
13	Construction Contracts	IAS 11	Jan 1996
14	Accounting for Taxes on Income	IAS 12 (superseded by revised IAS 12)	Jan 1984
16	Retirement Benefits Costs	IAS 19 (superseded by revised IAS 19)	Jan 1996
18	Property, Plant and Equipment	IAS 16 (superseded by revised IAS 1, 22, 26 and 37)	Jan 1996
19	Accounting for Leases	IAS 17	Jan 2001
20	Borrowing Costs	IAS 23	Jan 1996
21	The Effects of Changes in Foreign Exchange Rates	IAS 21	Jan 1996
22	Accounting for Investments	IAS 25	Apr 1991
23	Revenue Recognition and Disclosures in the Financial Statements of Banks	IAS 30	Jan 1992
24	Accounting for Government Grants and Disclosure of Government Assistance	IAS 20	Apr 1991
25	Business Combinations	IAS 22 (superseded by revised IAS 12, 36, 37 & 38)	Jan 1996
26	Consolidated Financial Statements and Accounting for Investments in Subsidiaries	IAS 27	Jan 1992
27	Accounting for Investments in Associates	IAS 28 (superseded by revised IAS 36)	Jan 1992
28	Segment Reporting	IAS 14	Apr 2000
29	Revenue	IAS 18	Jan 1996
30	Related Party Disclosures	IAS 24	Apr 1992
31	Financial Reporting of Interests in Joint Ventures	IAS 31 (superseded by revised IAS 36)	Jan 1993
32	Plantations	IAS 41 (Agriculture) subsequently issued in 2000	Jan 1994
33	Revenue Recognition and Disclosures in the Financial Statements of Finance Companies	IAS 30	Apr 1995
34	Earnings per Share	IAS 33	Apr 2000

Five issues warrant attention in relation to SLASs. First, the IASB holds exclusive copyright over IASs. In this respect, the ICASL has obtained permission from the IASB to use its materials, including IASs. Other DMCs should be encouraged to follow Sri Lanka's approach.

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Second, IAS and IAS-related materials are highly priced—a copy of IAS 1 is available from the IASB for \$48—this is cheap compared to IAS 39 at \$71. To effectively adopt IAS-compliant accounting standards, developing countries must have affordable access to IAS explanatory and training materials—every accountancy teacher and accountant should have copies of these materials. IASB’s pricing policy is inconsistent with its objectives. Moreover, it fails to recognize that the international community has funded the development of these materials (IASB’s activities are financed by professional accountancy bodies and other organizations on its Board, by IFAC, and by contributions from companies, financial institutions, accounting firms, and other organizations).

Third, SLASs include a section that compares the SLAS to the equivalent IAS. Once again, other DMCs should be encouraged to follow Sri Lanka’s approach.

SLAS 5 *Inventories*: Compliance with IAS⁸⁵

Compliance with this SLAS ensures compliance in all material respects with International Accounting Standard IAS 2, *Inventories*.

⁸⁴ Source: www.iasc.org.uk

⁸⁵ ICASL. 1999. *Sri Lanka Accounting Standards 1999*. Colombo: ICASL. p. 112.

Fourth, the IASB came into being in April 2001 and intends to undertake an *Improvements Project* (see Appendix 7) focusing on: (i) eliminating explicit or implicit choices; (ii) eliminating conceptual inconsistencies between IASs; (iii) providing additional guidance; (iv) identifying additional disclosures; (v) making drafting improvements; and (vi) improving the structure of standards. The *Improvements Project* is additional to the issuance of further EDs and standards. Consequently, as there will be many changes to IASs in the next five years, it will be difficult for Sri Lankan SLASs to keep abreast of these changes. In this respect, SLASs are already slightly out-of-step with certain IASs that have been recently revised or issued (see, for instance, IAS 16 and IAS 36).

Fifth, IASs are particularly intended for financial reporting by publicly listed companies. Small and medium-sized enterprises generally do not have the capacity to correctly apply the provisions of certain standards, such as IAS 39 *Financial Instruments, recognition and measurement* and IAS 19 *Employee Benefits* (see Box 3).

**Box 3. Practical Problems Meeting the Requirements of IAS 19
*Employee Benefits***

Sri Lankan organizations must provide employee retirement benefits at a rate of one-half month's salary for every year of completed service. SLAS 16 *Retirement Benefits Costs* (largely equivalent to IAS 19 *Employee Benefits*) effectively requires an actuarial valuation to calculate the value of such benefits for financial disclosure purposes.

Given the dearth of Sri Lankan actuaries—and the potential costs for SMEs—ASC opted to suspend the actuarial valuation requirement for a period of three years commencing 1 January 1999 (Gazette Extraordinary No.1103/18 of 28 October 1999). Instead, Sri Lankan companies are required to calculate the liability at its undiscounted face value. Although significantly overstating employee benefit liabilities—in comparison to the IAS 19 treatment—the calculation is simple to apply and audit.

In April 1998, a project to examine the reporting requirements for SMEs was added to the IASB agenda—however no progress has been made to date and further activity has yet to be determined by IASB. Possible issues that relate to this, include: (i) whether IASB should develop a basic accounting system for developing countries, comprising procedural standards and guidelines similar to the French *Plan Comptable*; (ii) whether there should be different accounting standards or different disclosure standards for enterprises in developing countries and economies in transition; and (iii) whether there are special problems with applying existing IASs in developing or transition countries.

In July 2000, IASB staff attended the most recent session of the UN Intergovernmental Working Group of Experts on International Standards

of Accounting and Reporting (ISAR), which discussed SME accounting and reporting, and suggested that a 'progressive' system of reporting formats be developed. At the session, ISAR specified that the proposed framework should: (i) be simple, understandable and user-friendly; (ii) produce useful management information; (iii) be as standardized as possible; (iv) be flexible enough to accommodate the business growth and increase the potential of some SMEs as they expand to use IASs; (v) be easily reconcilable for tax purposes; and (vi) recognize the environment in which SMEs operate

ISAR mandated an *ad hoc* working party to prepare a set of voluntary guidelines as to how those countries that wished to review their accounting regulatory structure might install a system that was both coherent throughout, adapted to the needs of SMEs at the entry level and permitted a logical progression in line with company growth.

IASB staff attended an ISAR working party meeting in May 2001 to discuss the proposals that were later put before the annual ISAR conference in September 2001. The proposals aimed to provide a model framework for national accounting regulators that will cover the whole range of accounting entities from the one-person business through to the listed company.⁸⁶

At the September 2001 meeting, ISAR agreed a categorization methodology for entities and requested that the *ad hoc* working party further refine the proposals for SME reporting.

However, although the use of IAS-compliant accounting policies by Sri Lankan organizations currently creates difficulties in the absence of a differential reporting regime, the ICASL has initiated a project to develop an SME reporting standard on the lines taken by the United Kingdom.

5. Conformity with International Accounting Standards (IAS)

As a consequence of the ASC's decision to make SLASs IAS-compliant, there are few material differences, except for the following variances that this study identified.

IASs not adopted (yet) by Sri Lanka:

IAS 15	Information reflecting the effects of changing prices (SLAS17 was withdrawn).
IAS 26	Accounting and reporting by retirement benefit plans.
IAS 29	Accounting and reporting in hyperinflationary economies.

⁸⁶ Source: www.iasc.org.uk

IAS 32	Financial instruments, disclosure and presentation.
IAS 35	Discontinued operations (partly dealt with in SLAS 10).
IAS 36	Impairment of assets.
IAS 38	Intangible assets (partly dealt with in SLAS 25).
IAS 39	Financial instruments, recognition and measurement.
IAS 40	Investment property.
IAS 41	Agriculture.

SLASs which have been drafted or adopted, but have not been issued:

SLAS 12	Events after the balance sheet date (draft standard based on IAS 10).
SLAS 35	Interim financial reporting (draft standard based on IAS 34).
SLAS 36	Provisions and contingent assets and liabilities (Adopted but not yet issued, based on IAS 37).

Sri Lankan standards based upon *IASs that have been withdrawn:*

SLAS 8	Depreciation accounting IAS 4 (superseded by IAS 16, 22 and 38).
SLAS 11	Research and development costs IAS 9 (superseded by IAS 38 Intangible Assets).
SLAS 15	Presentation of current assets and current liabilities.
SLAS 22	Accounting for investments IAS 25 (superseded by IAS 39 & 40).

***Country-specific national standards* that have been developed:**

SLAS 32	Plantations.
SLAS 33	Revenue recognition and disclosure in the financial statements of financial companies.

***Non-comparable SLASs* (due to significant differences):**

IAS 12	Income taxes (SLAS 14 Accounting for taxes on income).
IAS 19	Employee benefits (SLAS 16 Defined contribution plans).

There are the following ***content differences with IASs:***

IAS		Differences
16	Property, plant and equipment	The SLAS is completely consistent with the pre-1998 IAS 16. However, IAS 16 was revised in 1998 and, as part of the revision process, IAS 36 (Impairment losses) was issued. SLASs have not been updated to reflect these revisions.
31	Financial reporting of interest in joint ventures	Revisions made to the IAS regarding Impairment Losses have not been adopted. Instead, declines other than temporary in the carrying value of long-term assets should be recognized.

6. Public Sector Accounting Standards

Sri Lankan government organizations can be categorized into: (i) ministries, departments and constitutional bodies, such as the Auditor-General's Office; (ii) nonrevenue-earning statutory bodies and public enterprises; and (iii) revenue-earning statutory bodies and public enterprises. The *Sri Lankan Accounting and Auditing Standards Act (No. 15) 1995* requires that the latter group report in accordance with SLASs.

Groups (i) and (ii) are required to report in accordance with the *Financial Regulations 1992* issued by MOFP's Public Finance Department Planning.⁸⁷ These groups prepare cash-based budgets and financial reports. The *Financial Regulations* do not prescribe accounting standards in this respect. The Government is considering introducing accrual budgeting and accounting as part of the Public Expenditure Management Reform Program.

In 1996, the Public Sector Committee (PSC) of IFAC initiated a project to prepare a set of International Public Sector Accounting Standards (IPSASs). The benefits of improved governmental financial reporting and the corresponding improvement in transparency were recognized by international and regional organizations, including ADB, the World Bank, the IMF and the United Nations Development Programme (UNDP), all of which provided funding for the public sector accounting standards project.

On 24 May 2000, IFAC formally released the first IPSASs (see Appendix 6). They are the first set of accounting standards applicable to public sector reporting and are intended to meet the needs of governments, ministers, taxpayers and credit-rating agencies. The standards apply to all levels of government and will provide governments with a platform on which to base improvements in their financial management and reporting practices. Further IPSASs are currently being developed.

The PSC recognizes that many governments may not yet be in a position to adopt the accrual-based IPSASs. To assist these governments, the PSC has also developed ED-9 *Financial Reporting under the Cash Basis of Accounting*. ED-9 sets out the requirements for the presentation of the primary financial statement under the cash basis of accounting, as well as the statement's structure and minimum content requirements. The requirements that are likely to emerge in this standard should lead to transparency where governments remain on the cash basis of reporting.

⁸⁷ Government of Sri Lanka. 1992. *Financial Regulations of the Government of the Democratic Socialist Republic of Sri Lanka*. Department of Government Printing: Colombo.

Although public corporations report largely in accordance with SLASs, there are no accounting standards for Sri Lankan public sector budgeting and reporting. Although the Government has stated its intention to adopt the accrual-based IPSASs as the basis for government budgeting and accounting, this is likely to take some years to achieve. In the interim, the requirements of ED-9, which calls for preparation of a standard cash flow statement (i.e., where flows are categorized into cash flows from operating, investing and financing) could be met by the existing Computerized Integrated Government Accounting System (CIGAS), with few modifications.

7. Taxation Reporting Requirements

All Sri Lankan companies must prepare SLAS-compliant financial reports. Adjustments are then applied to these financial reports to derive corporate income for taxation purposes.

Part Two. Auditing Standards

8. Introduction

As already described (see page 54), the findings and recommendations of the *Presidential Commission on Finance and Banking* foreshadowed the passage of the *Sri Lanka Accounting and Auditing Standards Act (No. 15) 1995*. The Act empowers the ICASL to adopt from time to time, appropriate SLAuSs.

To assist the Institute in promulgating SLAuSs, the Act provides for the AuSC, which was established in June 1996. The AuSC promulgates SLAuSs, which are based directly upon IAASB pronouncements. The ICASL is obliged, as a member of IFAC, to work towards implementation of ISAs. The AuSC issued a new set of SLAuSs in May 1997. These replaced the auditing standards that had been issued in the mid-1970s and had only been subjected to minor modifications in the interim.⁸⁸

The Act stipulates that only a professionally qualified auditor, who is an ICASL member holding a Certificate to Practice, may audit SBE accounts. The Act makes the SLAASMB responsible for monitoring the application of SLAuSs in the conduct of SBE audits.

⁸⁸ ICASL. 1997. *Sri Lanka Auditing Standards 1997*. President's Foreword. Colombo: ICASL.

9. Auditing Standards Committee (AuSC)

The Committee comprises eight members are appointed under Section 9(1) of the *Sri Lanka Accounting and Auditing Standards Act (No. 15) 1995*. Four Committee members must also be ASC members. As with the ASC, and in contrast to the SLAASMB, the AuSC's activities are funded entirely by the ICASL.

10. Auditing Standard Setting Process

The promulgation process for SLAuSs is similar to that for SLASs (see page 56). SLAuSs are based on the ISAs published by the IAASB.

The first 28 new SLAuSs were published in all three languages in the Gazette Extraordinary No. 1056/19 of 2 December 1998. ADB supported the translation process under the Financial Management Training Project.⁸⁹

11. Sri Lankan Auditing Standards

Twenty-eight SLAuSs were effective as of 30 June 2001 (Table 13 refers).

Table 13. Sri Lankan SLAuSs as at 30 June 2001⁹⁰

No.	Title	Parentage	Effective
...	Framework of SLAuSs	ISA 120	
Responsibilities:			
1	Objective and General Principles Governing an Audit of Financial Statements	ISA 200	Jan 1998
2	Terms of Audit Engagements	ISA 210	Jan 1998
3	Quality Control for Audit Work	ISA 220	Jan 1998
4	Documentation	ISA 230	Jan 1998
5	Fraud and Error	ISA 240	Jan 1998
6	Consideration of Laws and Regulations in an Audit of Financial Statements	ISA 250	Jan 1998
Planning:			
7	Planning	ISA 300	Jan 1998
8	Knowledge of the Business	ISA 310	Jan 1998
9	Audit Materiality	ISA 320	Jan 1998

⁸⁹ ICASL. 2000. *Institute of Chartered Accountants of Sri Lanka 1999 Annual Report*. p. 18.

⁹⁰ ICASL. 1997. *Sri Lanka Auditing Standards 1997*. Colombo: ICASL.

Table 13. Sri Lankan SLAuSs as at 30 June 2001 (continued)

No. Title	Parentage	Effective
Internal Control:		
10 Risk Assessment and Internal Control	ISA 400	Jan 1998
11 Auditing in a Computer Information System (CIS) Environment	ISA 401	Jan 1998
12 Audit Considerations Relating to Entities Using Service Organizations	ISA 402	Jan 1998
Audit Evidence:		
13 Audit Evidence	ISA 500	Jan 1998
14 Audit Evidence: additional considerations for specific items	ISA 501	Jan 1998
15 Initial Engagements - Opening Balances	ISA 510	Jan 1998
16 Analytical Procedures	ISA 520	Jan 1998
17 Audit Sampling	ISA 530	Jan 1998
18 Audit of Accounting Estimates	ISA 540	Jan 1998
19 Related Parties	ISA 550	Jan 1998
20 Subsequent Events	ISA 560	Jan 1998
21 Going Concerns	ISA 570	Jan 1998
22 Management Representations	ISA 580	Jan 1998
Using the Work of Others:		
23 Using the Work of Another Auditor	ISA 600	Jan 1998
24 Considering the Work of Internal Auditing	ISA 610	Jan 1998
25 Using the Work of an Expert	ISA 620	Jan 1998
Audit Conclusions and Reporting:		
26 The Auditor's Report on Financial Statements	ISA 700	Jan 1998
27 Corresponding Figures	ISA 710	Jan 1998
28 Other Information in Documents Containing Audited Financial Statements	ISA 720	Jan 1998

Four issues deserve attention in relation to SLAuSs. First, the IFAC holds exclusive copyright over ISAs. In this respect, the ICASL has obtained permission from IFAC to use its materials, including ISAs. Other DMCs should be encouraged to follow Sri Lanka's approach. Second, ISAs and ISA-related materials are much more reasonably priced than IASs. They are also available via the Internet (www.ifac.org). Third, SLAuSs include a section that compares the SLAuS to the equivalent ISA. Once again, other DMCs should be encouraged to follow Sri Lanka's approach.

SLAuS 13 *Audit Evidence: Compliance with ISAs*⁹¹

Compliance with this SLAuS ensures compliance in all material respects with International Standard on Auditing ISA 500.

⁹¹ ICASL. 1997. *Sri Lanka Auditing Standards 1997*. ICASL: Colombo. p. 119.

Fourth, in keeping with ISAs, SLAuSs include a section that provides a public sector perspective on the standard. Once again, other DMCs should be encouraged to follow Sri Lanka's approach.

SLAuS 2 *Terms of Audit Engagements*: Public Sector Perspective⁹²

The purpose of the engagement letter is to inform the auditee of the nature of the engagement and to clarify the responsibilities of the parties involved. The legislation and regulations governing the operations of public sector audits generally mandate the appointment of a public sector auditor and the use of audit engagement letters may not be a widespread practice. Nevertheless, a letter setting out the nature of the engagement may be useful to both parties. Public sector auditors have to give serious consideration to issuing audit engagement letters when undertaking an audit.

12. Comparison with International Standards on Auditing (ISA)

The IAASB works to improve the uniformity of auditing practices by issuing pronouncements on auditing issues and promoting their acceptance. Its key pronouncements are ISAs and International Auditing Practice Statements (IAPs). The list of ISAs and IAPs that were effective at 30 June 2001 is provided as Appendix 5.

National standards on auditing and related services that have been published in many countries differ in form and content. The IAASB recognizes these documents and differences and, in the light of this knowledge, issues ISAs that are intended for international acceptance. ISAs are to be applied in the audit of financial statements. ISAs are also to be applied, adapted as necessary, to the audit of other information and to related services. These standards outline basic responsibilities for auditors, help them cope with increased and changing demands for financial statement information, and provide guidance in specialized areas, such as auditing computerized information systems. They are codified and available in a bound volume or through an electronic subscription service. IAPs provide practical assistance to auditors in implementing the standards or on related subjects and promote good practice. These statements are not intended to have the authority of standards.

As a consequence of the AuSC's decision to make SLAuSs ISA-compliant, there are few material differences, except for the following variances that this study identified.

⁹² *Ibid.* p. 26.

ISAs not adopted by Sri Lanka:

ISA 505 External confirmations

ISAs adopted as Sri Lankan Auditing Practice Statements:

ISA 800 The auditors report on special purpose audit engagements.

ISA 810 The examination of prospective financial information.

ISA 910 Engagements to review financial statements.

ISA 920 Engagements to perform agreed upon procedures regarding financial information.

ISA 930 Engagements to compile financial information.

IAPs not adopted by Sri Lanka:

IAPS 1000* Inter-bank confirmation procedures.

IAPS 1001* Computer Information System (CIS) environments: standalone microcomputers.

IAPS 1002* CIS environments: online computer systems.

IAPS 1003* CIS environments: database systems.

IAPS 1004* The relationship between bank supervisors and external auditors.

IAPS 1005 Particular considerations in the audit of small business.

IAPS 1006 The audit of international commercial banks.

IAPS 1007* Communications with management.

IAPS 1008 Risk assessments and internal control: CIS characteristics and considerations.

IAPS 1009* Computer assisted techniques.

IAPS 1010 The consideration of environmental matters in the audit of financial statements.

IAPS 1012 Auditing Derivative Financial Instruments

IAPS 1013 Electronic Commerce: Effect on the Audit of Financial Statements

* under consideration for adoption as of March 2002.

There are *no content differences with ISAs*. However, in addition to the provisions of ISA 700 (The Auditor's Reports on Financial Statements), a Sri Lankan audit report must also cover whether: (i) the books of account agree with the financial statements; (ii) the company maintained proper books of account; (iii) the financial statements were prepared according to accounting standards; (iv) the financial statements provide information required by the Companies Act; and (v) any directors' interests in contracts have been disclosed.

13. Issue Synopsis: Accounting and Auditing Standards

Other countries should consider the following aspects of Sri Lanka's arrangements regarding accounting and auditing standards. First, the ICASL has obtained permission from the IASB to use its materials, including IASs. Second, SLASs include a section that compares the

SLAS to the equivalent IAS. Third, the ICASL has obtained permission from IFAC to use its materials, including ISAs. Fourth, SLAuSs include a section that compares the SLAuS to the equivalent ISA. Fifth, SLAuSs include a section that provides a public sector perspective on the standard.

Chapter VIII – *Issues and Recommendations* – identifies and describes constraints and proposes corrective actions. These include the following issues regarding Sri Lankan accounting and auditing standards:

- In contrast to SLAASMB activities, the standing-setting activities of the ASC and the AuSC are entirely reliant on voluntary efforts. This potentially constrains Sri Lanka’s ability to maintain country standards in line with international standards.
- IASs are particularly intended for financial reporting by publicly listed companies. SMEs generally do not have the capacity to correctly apply the provisions of certain standards, such as IAS 39 (Financial instruments, recognition, and measurement) and IAS 19 (Employee benefits). In this respect, the application of IAS-compliant accounting policies by Sri Lankan organizations creates difficulties in the absence of a differential reporting regime.
- A gap has emerged between SLASs and IASs. In the absence of corrective actions or arrangements, this gap will widen as the IASB reviews existing IASs and issues new standards.