



International Federation of Accountants

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Agenda Item

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Committee: IAASB Consultative Advisory Group

Meeting Location: Washington

Meeting Date: September 9–11, 2009

Reviews, Compilations and Alternatives to the Audit— Report Back and Key Issues

Objective of Agenda Item

1. The Objectives of this Agenda Item are:
 - (a) To obtain the Representatives' views on a number of key issues relating to this project, and
 - (b) To provide a report back on proposals of Representatives on the project proposal for the project to revise the standards for reviews and compilations, discussed at the March 9-10, 2009 CAG meeting.
2. The current focus of this project is to revise the standards for review and compilation engagements, which the Task Force is progressing in tandem. Accordingly, the Issues Paper that the Task Force is presenting to the September 2009 IAASB meeting (Agenda Item 6 of the September 2009 IAASB meeting material) focuses on reviews of financial statements only (provided as a CAG Reference Paper for this Agenda Item). The Task Force will develop an Issues Paper for revision of the standard on compilation engagements to be presented at the December 2009 IAASB meeting.

Background

3. As noted in the project proposal the IAASB approved at its March 2009 meeting, the IAASB acknowledges this project's overall importance to addressing the needs of small and medium-sized entities (SMEs) and small and medium practices (SMPs) for assurance and related services, in settings where the audit services may often exceed what users want in terms of both services and cost and where there is no mandatory audit requirement. A key consideration in this project is to address SME client's needs through alternative services that give them viable choice to select from different services, or combinations of services, that meet their needs in an appropriate and cost-effective manner.
4. The IFAC Small and Medium Practices Committee represents the interests of professional accountants operating in SMPs and other professional accountants who provide services to SMEs to international standard setters, IFAC boards and committees, and other international organizations. The SMP Committee has contributed its views and feedback on the project proposal, and on the initial Issues Paper the Task Force presented at the June 2009 IAASB meeting (the SMP Committee's comments on that Issues Paper are provided as a CAG Reference Paper for this Agenda Item).

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5. An important consideration for noting is that for review engagements the focus of the project is on reviews of financial statements that are addressed in extant ISRE 2400¹, not reviews of interim financial statements which are addressed in ISRE 2410² and are undertaken by the entity's auditor who also performs the audit of the entity's annual financial statements. The project to revise ISRE 2400 may identify matters relevant to a future revision of ISRE 2410, or that would require conforming changes to that standard. It is important to understand the respects in which these standards need to be consistent, and also those in which they need to be different.
6. At its June 2009 meeting the IAASB considered and agreed scope and directional matters in relation to this project, as set out in the Issues Paper presented by the Task Force (provided as a CAG Reference Paper for this Agenda Item).
7. The following points were among the key matters agreed by the IAASB at the June 2009 meeting:

- *Prioritization of Development of Revised Standards for Reviews and Compilations*

The first priority is to develop review and compilation engagement standards to replace ISRE 2400 and ISRS 4410³ respectively.

- *Assessing the Need for Other Alternatives to the Audit*

The Task Force looked at models that exist or are under development in some countries, and formed the view that these developments are seeking to address particular practice issues related to the existing review and compilation services. They are not *new* alternative services.⁴

The existing review and compilation services offer a relatively simple solution to address user needs for alternative assurance and non-assurance services respectively, albeit that it is acknowledged that revised standards are needed in each case. They are viewed as services that have continuing viability to respond to user needs in the current environment. They also have the advantage of already having achieved market acceptance in a number of countries. This view was also confirmed by the national standard setters group.

¹ ISRE 2400, "Engagements to Review Financial Statements."

² ISRE 2410, "Review of Interim Financial Information Performed By the Independent Auditor of the Entity."

³ ISRS 4410, "Engagements to Compile Financial Statements."

⁴ Among the models that the Task Force has looked at are: a model under development in Germany which combines compilations with direct reporting; also two other models identifiable with the existing review engagement that are under development/under revision in the United Kingdom and the United States.

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The IAASB agreed that the question of whether there is need to consider development of further alternatives to the audit can best be clearly answered once revised standards for reviews and compilations are in place and being used.

- *Broad Principles that Guide this Project*

These are:

- (a) “An audit is an audit.”
- (b) Other services must be distinguished clearly from an audit and from each other. (Including, most importantly, that the ISRE 2400 review service needs to be clearly distinguished from the ISRE 2410 review service.)
- (c) Alternatives to the audit service must be:
 - meaningful, in the sense their value to users through having the practitioner’s involvement in the service is made clear, and
 - developed with cost-effectiveness in mind.
- (d) The concepts and principles contained in the IAASB’s International Framework for Assurance Engagements (the Framework) will inform this project.
- (e) The standards for reviews and compilations should guide practitioners, in performing these engagements, to meet the overall ethical obligation not to be associated with misleading information, or information that the practitioner ought reasonably to have known is misleading, or is likely to be misleading.
- (f) There should be a “stand-alone” package of standards for review engagements that practitioners can use without making reference to the ISAs. Some practitioners perform reviews exclusively, and therefore may not maintain familiarity with the auditing literature.
- (g) The standards for reviews and compilations should aim to increase understanding of these services as appropriate alternative services to the audit.
- (h) The aspects of performance of reviews and compilations of financial statements that are common to audits, reviews and compilations should be addressed on a consistent basis, as appropriate in the context of each type of service.

- *Ethical Considerations – Maintaining Independence in Review Engagements*

The IAASB agreed that the Task Force should explore certain independence considerations regarding practitioners undertaking review and compilation engagements (in particular, practitioner involvement in provision of other services relevant to preparation of financial statements in conjunction with performance of review and/or compilations).

The IAASB considered that if addressing independence considerations were viewed as a part of the possible set of responses that ought to be considered as part of meeting the

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objectives of this project, then there would be the need to reconcile possible avenues the Task Force may view as being worthy of further consideration with the relevant provisions of the IFAC *Code of Ethics for Professional Accountants* (IFAC Code), which would require dialogue with the International Ethics Standards Board for Accountants (IESBA).

- *Project Timetable*

The IAASB agreed the following revised project timetable for the project:

Project Stage	Timing
Confirmation of project scope and direction	June 2009
Issues Paper	September 2009
First read of exposure draft(s)	March 2010
Approve exposure draft(s)	December 2010
Full review of exposure draft comments and first read post-exposure	September 2011
Approve final standard(s)	December 2011

8. The Task Force has met on three occasions after the June IAASB meeting (and twice beforehand) to progress development of these issues as relevant to the revision of ISRE 2400 and ISRS 4410. It has further developed its views about various technical issues relevant to revising ISRE 2400. These are reflected in the Issues Paper for the revision of ISRE 2400 that the Task Force is presenting to the September 2009 IAASB meeting (Agenda Item 6 of the September 2009 IAASB meeting material).
9. In brief, the main technical issues the Task Force has considered concerning performance and reporting for reviews of financial statements are as follows:
 - Approach to performing reviews in practice.
 - The objective of a review of financial statements.
 - Extent of the understanding of the entity, the industry, and the environment that a practitioner must have to perform a review.
 - The approach to risk in a review.
 - Application of the concept of “limited assurance” in a review of financial statements.
 - How the practitioner goes about resolving observed material inconsistencies between the financial statements as presented and the practitioner’s understanding of the entity, its industry and its operating environment.
 - Wording of the practitioner’s conclusion for the review.

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- ISRE 2400 vs. ISRE 2410 reviews.
- Undertaking reviews of component entities in the context of an audit of group financial statements.
- Application of quality control standards in a review engagement.
- The premises upon which a review of financial statements is performed: application of the Framework concepts on engagement acceptance.
- Maintaining independence in a review engagement – provision of certain non-assurance services.

10. From these broad areas the Task Force has identified some questions which it would like Representatives to consider that are set out in the next section of this paper.

Matters for CAG Consideration

11. The Task Force welcomes Representatives' comments on any of the issues the Task Force has identified in Agenda Item 6 of the September 2009 IAASB meeting material.
12. The Task Force is particularly interested to obtain Representatives' feedback on the questions set out below. Information relevant to the Task Force's development of these issues, and its considerations and recommendations in these areas (where applicable) is set out in more detail in the Issues Paper included at Agenda Item 6-A of the September 2009 IAASB meeting material.

Objective of, and the Approach to, Performing a Review of Financial Statements

- 1) Do Representatives consider that the objective of an engagement to review financial statements (paragraph 13), and the statement of the practitioner's objective when performing the review (paragraph 15), in Agenda Item 6-A of the September 2009 IAASB meeting material are appropriate?

See paragraphs 13-15 of Agenda Item 6-A of the September 2009 IAASB meeting material.

- 2) Do Representatives agree that a practitioner performing a review of financial statements should be required to obtain "limited assurance" as the basis for expressing the conclusion on the financial statements (as opposed to "moderate assurance")?

See paragraphs 28-29 of Agenda Item 6-A of the September 2009 IAASB meeting material.

- 3) Do Representatives consider that the Task Force's view that the revised standard should follow the approach of establishing the minimum procedures and work effort that practitioners should undertake to perform the review, and to establish the limited assurance which provides the basis for expression of the review conclusion, is appropriate? Or do Representatives consider that the alternative approach of attempting to define the term

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“limited assurance” in the revised standard should be followed?

See paragraphs 30-33 of Agenda Item 6-A of the September 2009 IAASB meeting material.

- 4) Do Representatives consider that the approach to performing a review as described in paragraphs 7-9 in Agenda Item 6-A of the September 2009 IAASB meeting material is appropriate for achieving the objective of the review of financial statements, and the practitioner’s objective in performing a review? Is the suggested approach to understanding the risk of occurrence of material misstatements in the financial statements appropriate?

See paragraphs 6-9 and 26-27 of Agenda Item 6-A of the September 2009 IAASB meeting material.

- 5) What do Representatives consider is the requisite understanding the practitioner needs to have, or to obtain concerning the entity, its industry and its operating environment to properly plan and perform a review of financial statements effectively?

See paragraphs 16-25 of Agenda Item 6-A of the September 2009 IAASB meeting material.

- 6) Do Representatives consider the approach that the Task Force suggests a practitioner should follow to resolve observed material inconsistencies in the financial statements and to be able to form a conclusion about the financial statements, is appropriate?

See paragraphs 34-39 of Agenda Item 6-A of the September 2009 IAASB meeting material.

Reporting in Review Engagements

- 7) Do Representatives consider that a positively-worded conclusion in a review report (for example, as set out in paragraph 43 in Agenda Item 6-A of the September 2009 IAASB meeting material may better meet the overall objective of the review engagement as an assurance engagement, i.e., to enhance the intended users’ confidence concerning the financial statements?
- 8) Do Representatives consider that the suggested positively-worded conclusion would adequately communicate the review conclusion to users in clear terms, and effectively signal the limitations of the review to users (i.e., when read together with a preceding scope and basis for conclusions paragraph contained in the report)?
- 9) Do Representatives consider that the potential cost associated with the risk of using a positively-expressed conclusion (essentially that the review conclusion may not be sufficiently distinguishable from the audit opinion) would likely outweigh the potential benefit of using that form of expression of the review conclusion? Or do Representatives consider it is more likely that the benefits would outweigh the costs?

See paragraphs 40-44 of Agenda Item 6-A of the September 2009 IAASB meeting material.

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Other Issues Pertinent to Reviews of Financial Statements

Premises Upon Which a Review of Financial Statements is Performed: Application of the Framework Concepts on Engagement Acceptance

- 10) Do Representatives agree that clarification of the engagement acceptance concepts (contained in the Framework) is important for a review of financial statements? And specification of requirements and guidance about pre-conditions for undertaking a review of financial statements?

See paragraphs 50-60 of Agenda Item 6-A of the September 2009 IAASB meeting material.

Maintaining Independence in Review Engagements – Provision of Certain Non-Assurance Services

- 11) Do Representatives agree with the Task Force's consensus view that, in the context of the objective of this project, the current provisions of the IFAC Code regarding the practitioner's involvement with an assurance client's accounting records and financial statements are appropriate?
- 12) Do Representatives believe further dialogue with the IESBA may needed to understand the basis for the current provisions of the IFAC Code pertaining to:
- (i) Non-public interest entities for which practitioners undertake reviews?
 - (ii) Review engagements for which the report is restricted in use or distribution?
 - (iii) Any other issues or questions pertaining to application of the principle of Independence in relation to review engagements?

See paragraphs 67-76 of Agenda Item 6-A of the September 2009 IAASB meeting material.

March 9-10, 2009 CAG Proposals

13. Below is an extract from the draft minutes of the March 2009 CAG meeting⁵ and an indication of how the IAASB Task Force or the IAASB responded to the Representatives' comments.

Representatives' Comments	Task Force/IAASB Response
Mr. Johnson encouraged the IAASB to lead the effort in establishing a credible alternative service to the audit, as the increase in audit exemptions may lead to a proliferation of services provided. For example, in Europe the audit exemptions are	Point taken. The IAASB agreed the approach of prioritizing revision of the standards for review and compilation engagements in the first instance, after which it considers the question of whether further alternative

⁵ The minutes will be approved at the September 2009 IAASB CAG meeting.

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Representatives' Comments	Task Force/IAASB Response
<p>leading to a large percentage of companies that are exempt from audit, with the needs of the marketplace driving the services being provided. There is a risk that there could be individual solutions in the member states leading to a fragmentation of different services. It will therefore be important for the IAASB to quickly decide what the output of the project will be.</p> <p>Mr. Peyret supported Mr. Johnson's views, noting it will be essential for the IAASB to determine the likely output as soon as possible.</p>	<p>services to the audit are needed to respond to user needs can be better answered.</p> <p>The Task Force based its recommendation of this approach to the IAASB on consideration of a variety of inputs and information, including the results of consultation with the IAASB National Auditing Standard Setters in April 2009, and information reported by the Fédération des Experts Comptables Européens (FEE) on the results of a survey of developments in European countries with regard to development of alternative services to the audit (July 2009).⁶</p>

Material Presented – FOR IAASB CAG REFERENCE PURPOSES ONLY

Agenda Item 6-A of the September 2009
IAASB Meeting – Engagements to Review
Financial Statements – Issues and IAASB
Task Force Proposals

<http://www.ifac.org/IAASB/Meeting-FileDL.php?FID=4931>

IFAC SMP Committee Comments on Issues
Paper presented to the IAASB at its June 2009
meeting

[Word File attached](#)

Agenda Item 8 of the June 2009 IAASB
Meeting – Reviews, Compilations and Other
Alternatives to the Audit – Issues and IAASB
Task Force Proposals

<http://www.ifac.org/IAASB/Meeting-FileDL.php?FID=4762>

⁶ FEE: "Survey on the Provision of Alternative Assurance and Related Services Across Europe"