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Basis for Conclusions: Close Off Document—ISA 805 (Revised), Engagements to Report on Summary Financial Statements

Prepared by the Staff of the International Auditing and Assurance Standards Board



**International Federation
of Accountants**

BASIS FOR CONCLUSIONS

CLOSE OFF DOCUMENT – ISA 805 (REVISED), ENGAGEMENTS TO REPORT ON SUMMARY FINANCIAL STATEMENTS

This Basis for Conclusions has been prepared by staff of the International Auditing and Assurance Standards Board (IAASB). It relates to, but does not form part of, the close off document¹ of ISA 805 (Revised), “Engagements to Report on Summary Financial Statements,” which was approved by 17 of the 18 members of the IAASB in December 2006.

Introduction

1. In September 2006, the IAASB agreed the conventions that it would use in drafting future International Standards on Auditing (ISAs). These conventions are commonly referred to as the IAASB’s Clarity conventions.
2. The IAASB issued exposure drafts of certain proposed revised ISAs before it finalized these new conventions. In developing these ISAs for exposure and subsequently revising them as a result of responses received during the consultation, the IAASB applied its old drafting conventions. The revised ISAs, finalized but not issued, are described as the “close off” documents, and represent the final ISAs that the IAASB would have published had it not changed its drafting conventions as a result of the Clarity project. The Clarity conventions and any necessary redrafting are then applied to the close off documents to arrive at proposed redrafted ISAs that are next exposed for comment on the Clarity changes only (unless in any particular case there is a specific issue on which further consultation (in effect re-exposure) is deemed necessary).

Project to Revise Extant ISA 800

3. Extant ISA 800, “The Independent Auditor’s Report on Special Purpose Audit Engagements” (extant ISA 800) contains requirements and guidance for auditors’ reports on summary financial statements. Extant ISA 800 was last revised in March 1994. The IAASB agreed to revise extant ISA 800 when ISA 700, “The Independent Auditor’s Report on a Complete Set of General Purpose Financial Statements” and related conforming amendments were issued in December 2004.
4. The project to revise extant ISA 800 led to the issue of two exposure drafts, i.e., proposed ISA 701, “The Independent Auditor’s Report on Other Historical Financial Information” and proposed ISA 800, “The Independent Auditor’s Report on Summary Audited Financial Statements” (ED-ISA 800). The exposure drafts were issued in June 2005. They were presented in the IAASB’s old drafting conventions.
5. The comment period for the exposure drafts closed on October 31, 2005. Thirty-four comment letters were received from a variety of respondents, including regulators, IFAC member bodies, national standard setters, and firms. The IAASB revised the proposed ISAs as a result of these comments and approved the close off document of ISA 805

¹ Paragraph 2 describes the term “close off” document.

(Revised), “Engagements to Report on Summary Financial Statements”² under its old drafting conventions in December 2006. The Public Interest Oversight Board (PIOB) expressed satisfaction that the IAASB had duly followed its due process.

6. This Basis for Conclusions explains the more significant issues raised by respondents on ED-ISA 800, and how the IAASB has addressed them in finalizing the close off document of ISA 805 (Revised).
7. This Basis for Conclusions is issued to coincide with the release of the Clarity-redrafted exposure draft. The effects of the redrafting are explained in the separate explanatory memorandum accompanying that exposure draft.

A Separate ISA for Engagements to Report on Summary Financial Statements

8. Extant ISA 800, although having a primary focus on special purpose audit engagements, contains requirements and guidance for auditors’ reports on summary financial statements. The IAASB debated whether the nature of an engagement to report on summary financial statements is an audit, an other assurance engagement or a related services engagement, and where the related requirements and guidance should be placed.
9. The IAASB concluded that, because summary financial statements are derived from audited financial statements, and the auditor’s report on summary financial statements is closely linked to the auditor’s report on the financial statements from which they are derived, the requirements and guidance should form part of the ISAs. There are, however, significant differences between auditors’ reports on financial statements, and those on summary financial statements, and the underlying work to be carried out by the auditor. The IAASB therefore proposed that the requirements and guidance be placed in a separate ISA. The majority of respondents to the exposure draft supported this proposal.
10. Some respondents, however, were concerned that the form of opinion in ED-ISA 800 may conflict with law or regulation in some jurisdictions. As a result, they were of the view that the proposed requirements and guidance should not form part of the ISAs, as this may affect the adoption of ISAs by such jurisdictions. Although the separation of the requirements and guidance into their own ISA must alleviate any implications of this concern, the IAASB dealt with the substantive point by agreeing that alternative forms of opinion should be allowed. Paragraph 21 of the close off document of ISA 805 (Revised) explains that, in some jurisdictions, law or regulation governing reporting on summary financial statements may prescribe wording for the opinion that is different from that described in the ISA. Where this is the case, the auditor uses the prescribed wording; however, the auditor’s procedures required by the ISA remain the same, with the addition of any further procedures necessary to enable the auditor to express the prescribed opinion.

² See footnote 1.

Engagement Acceptance

11. In line with extant ISA 800, the requirements and guidance in the close off document of ISA 805 (Revised) apply when the auditor is engaged to report on a summary financial statements derived from financial statements *audited by that auditor*. Paragraph 4 of the close off document of ISA 805 (Revised) therefore permits the auditor to accept an engagement to report on summary financial statements in accordance with the ISA only when the summary financial statements are derived from financial statements on which the auditor has issued an auditor's report in accordance with the ISAs.
12. The audit of the financial statements from which the summary financial statements are derived provides the auditor with the necessary knowledge to discharge his or her responsibilities in relation to the summary financial statements in accordance with the ISA. Paragraph 4 of the close off document of ISA 805 (Revised) explains that application of the requirements and guidance in the ISA will not provide sufficient appropriate evidence on which to base the opinion on the summary financial statements if the auditor has not also audited the financial statements from which the summary financial statements are derived.

Criteria

13. Unlike extant ISA 800, ED-ISA 800 addressed the issue of criteria. It recognized that established criteria for preparing and presenting summary financial statements may not exist. It explained that, when established criteria do not exist, the risk increases that the summary financial statements may not contain the information necessary so as not to be misleading in the circumstances. It therefore required the auditor to consider whether the criteria applied in preparing and presenting the summary financial statements are suitable in the circumstances before accepting the engagement.
14. In arriving at this position, the IAASB recognized that the existence of established criteria for preparing and presenting summary financial statements can vary from jurisdiction to jurisdiction. In some jurisdictions, criteria may be established in accounting standards, law, regulation, or securities exchange listings requirements. As was the case for one jurisdiction, criteria may also be established in assurance guidance. However, there are many jurisdictions that do not have established criteria; yet summary financial statements are still prepared and reported on by auditors.
15. Given this variety amongst jurisdictions, the IAASB concluded that the ISA should provide for circumstances where established criteria exist, as well as circumstances where they do not exist.
16. Accordingly, the IAASB agreed that the close off document of ISA 805 (Revised) should:
 - (a) State that, unless law or regulation prohibits the auditor from declining an engagement to report on summary financial statements, the auditor should accept such an engagement only when the auditor concludes that the applied criteria are acceptable in the circumstances;

- (b) Require the auditor to appropriately modify the report on the summary financial statements, when the auditor determines the applied criteria are not acceptable and law or regulation prohibits the auditor from declining such an engagement (see paragraphs 9-10 of the close off document of ISA 805 (Revised));
- (c) Explain that, in many cases, the auditor may presume that criteria established by an authorized or recognized standards setting organization or by law or regulation are acceptable (see paragraph 11 of the close off document of ISA 805 (Revised));
- (d) Recognize that, where established criteria do not exist, acceptable criteria may be developed by management; and
- (e) Require the auditor to evaluate whether the summary financial statements adequately disclose the applied criteria (see paragraph 15(c) of the close off document of ISA 805 (Revised)).

Opinion on Summary Financial Statements

- 17. Extant ISA 800 requires the auditor to report whether the summary financial statements are “consistent, in all material respects” with the audited financial statements from which they are derived. This wording is currently used in certain jurisdictions. However, standard setters in some jurisdictions have chosen different phrases, such as “fairly stated, in all material respects, in relation to ...” and “fairly summarized, in all material respects, ...”
- 18. The explanatory memorandum that accompanied ED-ISA 800 noted that the IAASB revised the wording of the opinion because it was concerned that the extant wording may be subject to different interpretation, perhaps because of translation issues.
- 19. In developing ED-ISA 800, the IAASB considered alternative phrases such as “fairly stated, in all material respects” and “fairly summarized, in all material respects.” However, the IAASB concluded that use of these phrases was not appropriate because of a concern that they may be confused with “present fairly” used in the context of the underlying audited financial statements.
- 20. The IAASB therefore proposed that the auditor express an opinion whether the summary financial statements are an appropriate summary of the audited financial statements from which they are derived, in accordance with the specified established criteria or the basis described.
- 21. A small majority of respondents did not support the proposed form of opinion. Some preferred the existing form of opinion, i.e., “consistent, in all material respects.”
- 22. The IAASB debated the comments and concluded that the original concerns were not sufficient to propose a new form of opinion that is not currently used to any great extent. It agreed that, based on the procedures in paragraph 15 of the close off document of ISA 805 (Revised), and any other procedures that the auditor may consider necessary in the circumstances, the auditor should form an opinion whether the summary financial statements are a fair summary of the audited financial statements in accordance with the applied criteria. The procedures specified in paragraph 15 of the close off document of

ISA 805 (Revised) include an evaluation whether, in view of the applied criteria, the summary financial statements contain the information necessary so as not to be misleading in the circumstances.

23. In addition, and as explained in paragraph 5 above, the close off document of ISA 805 (Revised) provides for circumstances where national law or regulation governing reporting on summary financial statements prescribes wording for the opinion that is different from that described above.

Cases Where the Underlying Audited Financial Statements are not Made Available

24. Because summary financial statements by their nature are expected to contain only limited disclosure, there is a risk that they may not contain the information necessary so as not to be misleading in the circumstances. For this reason, some respondents were strongly of the view that the underlying audited financial statements and related auditor's report should be made available to intended users of the summary financial statements under all circumstances.
25. The legal environment in some jurisdictions provides that the audited financial statements from which the summary financial statements are derived need not to be made available to the intended users of the summary financial statements. The IAASB therefore concluded that it is not possible to limit acceptance of engagements to report on summary financial statements to those where the audited financial statements from which they are derived will be available to the intended users of the summary financial statements. The IAASB, however, agreed that the close off document of ISA 805 (Revised) should provide for the following:
 - (a) Where law or regulation *explicitly* provides that the audited financial statements need not be made available to the intended users of the summary financial statements, the auditor should not accept the engagement unless the law or regulation establishes the criteria for preparing and presenting the summary financial statements. Unless these circumstances apply, the auditor evaluates whether the audited financial statements are available to the intended users of the summary financial statements without undue difficulty (see paragraph 13-14 of the close off document of ISA 805 (Revised));
 - (b) Where law or regulation explicitly provides that the audited financial statements need not be made available to the intended users of the summary financial statements, the auditor should evaluate whether the summary financial statements describe clearly the law or regulation in accordance with which the summary financial statements need not be made available (see paragraph 15(b)(ii) of the close off document of ISA 805 (Revised)).



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