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Agenda Item

14

Committee: IAASB

Meeting Location: Washington D.C.

Meeting Date: December 10-14, 2007

Proposal to Amend the Scopes of International Standard on Review Engagements (ISRE) 2410, “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” and ISRE 2400, “Engagements to Review Financial Statements”

Objectives of Agenda Item

1. To review a proposal to amend the scope of ISRE 2410 and ISRE 2400.

Matter for Consideration

2. It has been noted to the IAASB chair and staff that a review *by an entity’s auditor* of historical financial information¹ other than a complete or condensed set of interim financial statements does not fall within the scopes of either ISRE 2400, “Engagements to Review Financial Statements” or ISRE 2410. In the particular case noted, the auditor of an entity was engaged to review the entity’s balance sheet at a date agreed to by parties to a joint venture. The parties were interested in the venture’s net asset position. They agreed that a review (as opposed to an audit) by the entity’s auditor would be adequate to meet their needs.

BACKGROUND

3. The explanatory memorandum that accompanied the exposure draft of proposed ISRE 2410 asked respondents to consider whether the proposed scopes of ISREs 2400 and 2410 were appropriate. After careful consideration of the comments on the exposure draft, the IAASB concluded that the distinguishing factor between ISREs 2400 and 2410 should be audit-based knowledge.
4. The IAASB also noted that reviews of interim financial information, particularly for listed entities, were becoming more prevalent and, accordingly, agreed that it was appropriate to proceed with ISRE 2410. However, it was debated whether a review of

¹ ED-ISA 200, “Overall Objective of the Independent Auditor, and the Conduct of an Audit in Accordance with International Standards on Auditing” defines “historical financial information” as information expressed in financial terms in relation to a particular entity, derived primarily from that entity’s accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.

annual financial statements by an entity's auditor would be covered by ISRE 2400 or ISRE 2410. The IAASB concluded that such an engagement would be covered by ISRE 2410; but this was not specifically referred to in the scope of ISRE 2410 because this type of review was thought to be a rare occurrence. Similarly, no reference to other such reviews by the auditor was made.

5. As a result:

- (a) ISRE 2400 applies in the case of a review of financial statements performed by a practitioner, *who is not the auditor of the entity*. Paragraph 2 of ISRE 2400 notes that the ISRE is directed towards the review of financial statements; however, it is to be applied to the extent practicable to engagements to review financial or other information. The words in italics were inserted when the IAASB approved ISRE 2410.
 - (b) ISRE 2410 applies in the case of a *review of interim financial information by the auditor of the entity*. Paragraph 2 of ISRE 2410 explains that, for purposes of the ISRE, interim financial information is information that is prepared and presented in accordance with an applicable financial reporting framework and comprises either a complete or a condensed set of financial statements for a period that is shorter than the entity's financial year. There is no suggestion that it is to be applied in other circumstances or to other forms of historical financial information.
6. International Standard on Assurance Engagements (ISAE) 3000, "Assurance Engagements" applies to engagements other than "audits or reviews of historical financial information covered by ... ISAs or ... ISREs." Given the scope of ISRE 2410, the auditor of an entity may therefore turn to ISAE 3000 when engaged by that entity to review historical financial information other than interim financial information. The requirements and guidance in the ISREs, however, are more directly relevant to an engagement to review historical financial information than those in ISAE 3000, and were clearly the standards to be applied to all relevant reviews prior to the amendment to ISRE 2400 referred to in paragraph 5(a) above.

PROPOSAL

7. It is therefore proposed that the scope of ISRE 2410 be amended to provide for a review by an entity's auditor of historical financial information other than interim financial information. This reflects the initial intention of the IAASB that the entity's auditor should apply audit-based knowledge when carrying out reviews of historical financial information. It also reflects the fact that, in approving ISRE 2410, the IAASB had no intention of removing such reviews from the scope of the ISREs. The proposed amendments are as follows:

Introduction

1. The purpose of this International Standard on Review Engagements (ISRE) is to establish standards and provide guidance on the auditor's professional responsibilities when the auditor undertakes an engagement to review interim

financial information of an audit client, and on the form and content of the report. The term “auditor” is used throughout this ISRE, not because the auditor is performing an audit function but because the scope of this ISRE is limited to a review of interim financial information performed by the independent auditor of the financial statements of the entity.

2. For purposes of this ISRE, interim financial information is financial information that is prepared and presented in accordance with an applicable financial reporting framework² and comprises either a complete or a condensed set of financial statements for a period that is shorter than the entity’s financial year.
3. **The auditor who is engaged to perform a review of interim financial information should perform the review in accordance with this ISRE.** Through performing the audit of the annual financial statements, the auditor obtains an understanding of the entity and its environment, including its internal control. When the auditor is engaged to review the interim financial information, this understanding is updated through inquiries made in the course of the review, and assists the auditor in focusing the inquiries to be made and the analytical and other review procedures to be applied. A practitioner who is engaged to perform a review of interim financial information, and who is not the auditor of the entity, performs the review in accordance with ISRE 2400, “Engagements to Review Financial Statements.” As the practitioner does not ordinarily have the same understanding of the entity and its environment, including its internal control, as the auditor of the entity, the practitioner needs to carry out different inquiries and procedures to meet the objective of the review.

3a. This ISRE is directed towards a review of interim financial information by an entity’s auditor. However, it is to be applied, adapted as necessary in the circumstances, when an auditor undertakes an engagement to review historical financial information other than interim financial information of an audit client.

8. In addition, it is proposed that a footnote is added to the following sentence in the examples of review reports in the appendix to ISRE 2410:

We conducted our review in accordance with International Standard on Review Engagements 2410, “Review of Interim Financial Information Performed by the Independent Auditor of the Entity.”*

The footnote should read as follows:

* In the case of a review of historical financial information other than interim financial information, this sentence should read as follows: “We conducted our review in accordance with International Standard on Review Engagements 2410, which applies to a review of historical financial

² For example, International Financial Reporting Standards as issued by the International Accounting Standards Board.

information performed by the independent auditor of the entity.” The remainder of the report should be adapted as necessary in the circumstances.

9. An alternative approach, if the IAASB were to be of the view that ISRE 2410 should be restricted to reviews of *interim financial information* by the entity’s auditor, would be for the scope of ISRE 2400 to be amended to provide for reviews of historical financial information other than interim financial information by an entity’s auditor (as it did prior to the release of ISRE 2410). This alternative has the attraction of preserving the position prior to the issue of ISRE 2410, the purpose of which was expressly to deal with reviews of interim financial information. Nevertheless, it may be thought to be the less satisfactory approach as ISRE 2410 is a more up to date standard that takes into account the position of the auditor of an entity in undertaking a review. This approach could be achieved by amending paragraph 1 of ISRE 2400 as follows:

Introduction

1. The purpose of this International Standard on Review Engagements (ISRE) is to establish standards and provide guidance on the practitioner’s professional responsibilities when ~~a practitioner, who is not the auditor of an entity, undertakes~~ undertaking an engagement to review financial statements and on the form and content of the report that the practitioner issues in connection with such a review. ~~A practitioner, who is the auditor of the entity, engaged to perform~~ However, if the auditor of an entity is engaged to perform a review of the entity’s interim financial information performs such a review in accordance with, ISRE 2410, “Review of Interim Financial Information Performed by the Independent Auditor of the Entity:” applies. ISRE 2410 defines “interim financial information” as financial information that is prepared and presented in accordance with an applicable financial reporting framework and comprises either a complete or a condensed set of financial statements for a period that is shorter than the entity’s financial year.

Additional Matter for Consideration

10. The review of the matter above has highlighted a related issue. As indicated in paragraph 6, ISAE 3000 excludes from its scope “reviews of historical financial information covered by ... ISREs.” It therefore includes the “engagements to review other [i.e., non-historical] financial or other information” to which ISRE 2400 refers (see paragraph 5(a) above), and to which ISRE 2400 extends its provisions “to the extent practicable.” It is unsatisfactory for potential engagements to fall under different series of standards.
11. Furthermore, the Preface to the International Standards on Quality Control, Auditing, Review, Other Assurance and Related Services notes that “... ISREs are to be applied in the review of *historical financial information*.”
12. In addition, ISAE 3000 includes the following advice: “Although ISAs and ISREs do not apply to engagements covered by ISAEs, they may nevertheless provide guidance to practitioners.” This confirms that the applicability of ISREs and ISAEs is mutually exclusive. It also provides some basis for looking to ISRE 2400 when undertaking an

engagement to review other financial or other information, should it be helpful to do so, and may therefore be regarded as a substitute for the rather weak suggestion in ISRE 2400 to apply its provisions to the extent practicable to such engagements.

13. It would seem appropriate that ISRE 2400 be restricted to reviews of historical financial information. This makes the scopes of ISRE 2400 and 2410 and ISAE 3000 mutually compatible.
14. The IAASB is therefore asked to consider whether, in addition to the proposal to amend the scope of ISRE 2410 (see paragraphs 7-8 above), the scope of ISRE 2400 should be amended as follows:

Introduction

...

2. This ISRE is directed towards the review of financial statements. However, it is to be applied, adapted as necessary in the circumstances, to the extent practicable to engagements to review other historical financial ~~or other~~ information. Guidance in the International Standard on Auditing (ISAs) may be useful to the practitioner in applying this ISRE.

Action Requested

15. Since the proposals are designed to correct anomalies in the scopes of the current standards, it is suggested that they do not need to be exposed for public comment, should be given appropriate publicity, and should be effective immediately.
16. The IAASB is asked to review the proposals and approve the proposed amendments.

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