



American Institute of CPAs
1211 Avenue of the Americas
New York, NY 10036-8775

May 20, 2011

Mr. James Gunn

IAASB Technical Director

International Auditing and Assurance Standards Board

545 Fifth Avenue, 14th Floor

New York, NY 10017

Exposure Draft: Proposed International Standard on Review Engagements 2400 (Revised), *Engagements to Review Historical Financial Statements*

Dear Mr. Gunn:

The American Institute of Certified Public Accountants (AICPA) is pleased to comment on the referenced exposure draft. We support the efforts of the International Auditing and Assurance Standards Board (IAASB) to develop guidance that addresses the needs of small and medium-sized entities and small and medium practices, including the revision of extant International Standard on Review Engagements (ISRE) 2400, *Engagements to Review Financial Statements*. However, as more fully explained herein, we believe that the exposure draft contains several significant issues that should be addressed prior to the issuance of a final revised ISRE 2400.

Our comments on the exposure draft are organized in the following categories:

1. Responses to IAASB request for specific comments
2. Concerns regarding the requirement that the practitioner obtain evidence that the financial statements agree with, or reconcile to, the entity's underlying accounting records
3. Concerns regarding permitting the expression of an adverse conclusion in a limited assurance engagement

4. Concerns regarding the practitioner's response when the practitioner is unable to obtain sufficient appropriate evidence as the basis for a conclusion on the financial statements (scope limitation)
5. The need for additional guidance with respect to the practitioner's responsibility for other information in documents containing reviewed financial statements
6. The need for an illustration of management's written representations
7. Need for illustration of an emphasis-of-matter paragraph regarding going concern

1. Responses to IAASB request for specific comments

IAASB question 1:

Do respondents who are users or preparers of financial statements believe the proposed ISRE will result in an assurance engagement that is meaningful?

Response:

As users and preparers of financial statements, we believe that proposed ISRE 2400 will result in an assurance engagement that is meaningful. The limited assurance engagement has been a highly accepted engagement in the United States of America since 1978 and is particularly meaningful for small and medium-sized entities.

IAASB question 2:

Do respondents who are practitioners believe that proposed ISRE 2400 will result in engagements that can be understood and performed by practitioners in a cost-effective manner in a way that clearly distinguishes the engagement from an audit?

Response:

Although we believe that for the most part, proposed ISRE 2400 will result in engagements that can be understood and performed by practitioners in a cost-effective manner and in a way that clearly distinguishes the engagement from an audit, we caution the IAASB that its stated intention of emphasizing the "procedural nature of a review engagement in contrast to an audit" could lead to engagements that are conducted with an emphasis on completing procedures outlined in the proposed ISRE versus accumulating review evidence in order to obtain limited assurance. This procedural emphasis contradicts the last sentence on page 6 of the explanatory material that states, "The IAASB believes, however, that the evidential basis for a review must be sufficient and appropriate for the practitioner to conclude and report on the financial statements in the form required by the ISRE, and that it is important to recognize this essential element of a review as an assurance engagement." Although the procedures performed in a review engagement are necessarily limited compared to an audit engagement, the concept

of accumulating sufficient appropriate evidence remains the same. In an audit, the auditor performs procedures in order to obtain reasonable assurance. In a review, the practitioner performs limited procedures in order to obtain limited assurance. The fact that both an audit and a review are assurance engagements should be emphasized.

IAASB question 3:

Do respondents believe that the objectives stated in the proposed ISRE appropriately describe the expected outcome of the practitioner's work in a review engagement, and the means by which the objectives are to be achieved? Is there any wording in the objectives that might have unintended consequences, or that might blur understanding of the difference between a review and an audit?

Response:

The objectives, as stated in proposed ISRE 2400, are as follows:

14. The practitioner's objectives in conducting a review of financial statements are:

(a) To conclude, through performing primarily inquiry and analytical procedures, and evaluating the sufficiency and appropriateness of evidence obtained, whether anything has come to the practitioner's attention that causes the practitioner to believe the financial statements are not prepared, in all material respects, in accordance with an applicable financial reporting framework; and (Ref: Para. A11)

(b) To report on the financial statements as a whole, and communicate as required by this ISRE.

15. If the practitioner is not able to form a conclusion in accordance with this ISRE on the financial statements, the practitioner is required to either disclaim a conclusion in the report provided for the engagement or, where appropriate, withdraw from the engagement if withdrawal is possible under applicable law or regulation. (Ref. Para A12–A14)

We believe that the objectives, as stated in paragraph 14, are incomplete because they do not provide a reference point against which the practitioner can determine whether he or she has obtained the targeted level of assurance. The most significant aspect of the review engagement is that it is a limited assurance engagement, and the fact that it is an assurance engagement means that it has certain similarities to an audit. In addition, as stated previously, we believe that stressing the performance of procedures in paragraph 14(a) versus stressing the obtaining of limited assurance may have the unintended consequence of practitioners simply performing the review engagement in a checklist manner. We believe that the objective in paragraph 14 would be more appropriate if revised as follows (deleted language is shown in strikethrough; new language is shown in boldface italics):

14. The practitioner's objectives in conducting a review of financial statements are:

- (a) *To perform procedures designed to obtain limited assurance that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework;*
- (b) ~~To conclude, through performing primarily inquiry and analytical procedures, and evaluating the sufficiency and appropriateness of evidence obtained,~~ *based on the procedures performed (primarily analytical procedures and inquiry) and the results obtained,* whether anything has come to the practitioner's attention that causes the practitioner to believe the financial statements are not prepared, in all material respects, in accordance with an applicable financial reporting framework; and (Ref: Para. A11)
- (~~b~~c) To report on the financial statements as a whole, and communicate as required by this ISRE.

The revised objective would also assist in accomplishing the aim of the IAASB of positioning the review as a distinct assurance engagement, which is different from an audit in key respects.

IAASB question 4:

Do respondents believe that the factors affecting engagement acceptance and continuance, and the preconditions for performing a review under the proposed ISRE, are appropriate and clearly communicated in the proposed ISRE?

Response:

We believe that the factors affecting engagement acceptance and continuance and the preconditions for performing a review under proposed ISRE 2400 are appropriate and clearly communicated in proposed ISRE 2400.

IAASB question 5:

The approach to performing a review set out in the proposed ISRE (paragraphs 43 and 44) requires the practitioner to identify areas in the financial statements where material misstatements are likely to arise, based on the practitioner's understanding of the entity and its environment, and the applicable financial reporting framework, and then to focus the design and performance of inquiry and analytical procedures in those areas.

- a. Do respondents believe this approach is appropriate for a review?
- b. Do respondents believe that the requirement and guidance in the proposed ISRE adequately convey this intended approach?

- c. Do respondents believe that the requirements and guidance relating to the practitioner’s understanding (explained in paragraph 43), and designing and performing inquiry and analytical procedures (explained in paragraph 44), are sufficient to promote performance of reviews on a reasonably consistent basis with the application of the practitioner’s professional judgment and understanding, taking account of the circumstances in individual review engagements?

Response:

Although we agree with the risk awareness approach developed in proposed ISRE 2400, we do not believe that the standard uses the appropriate wording to describe the approach that a practitioner should utilize in performing a review engagement. Paragraphs 43–45 of proposed ISRE 2400, as well as other paragraphs in the proposed standard, refer to “areas in the financial statements where material misstatements are likely to arise.” The wording implies that the financial statements are likely to be materially misstated. We believe that the wording should be replaced throughout the standard (where appropriate) with “areas in the financial statements where there is an increased risk that the financial statements may be materially misstated.” In this way, the standard would keep to the risk approach.

IAASB question 6:

Do respondents agree with the requirements and guidance in the proposed ISRE (paragraphs 57 and 58) describing the trigger point at which additional procedures are required? Do respondents agree with the related requirements concerning the practitioner’s response when there are matters that cause the practitioner to believe the financial statements may be materially misstated?

Response:

We agree with the requirements and guidance in proposed ISRE 2400 describing the trigger point at which additional procedures are required, as well as the related requirements concerning the practitioner’s response when matters exist that cause the practitioner to believe that the financial statements may be materially misstated.

IAASB question 7:

With respect to the practitioner’s review report (as illustrated in Appendix 2 of the proposed ISRE):

- a. Do respondents believe the report adequately communicates to users the work undertaken by the practitioner for the review?
- b. Do respondents believe that the form of the practitioner’s conclusion (that is, “nothing has come to the practitioner’s attention that causes the practitioner to believe ...”) communicates adequately the assurance obtained by the

- practitioner? Is this form of wording of the practitioner's conclusion preferable to other forms that have been explored by the IAASB as discussed above, including those that use wording perceived as being more positive? If not, please explain and provide alternative wording that could be used to express the practitioner's conclusion.
- c. Is the practitioner's conclusion expressed in this form likely to be understandable and meaningful to users of the financial statements? Does this form of conclusion achieve the intended purpose of properly differentiating the conclusion reported in a review from the opinion expressed in an audit of financial statements?

Response:

Although we generally believe that the illustrative practitioner's review report is well developed and in the public interest, we are concerned about the reporting requirements regarding communicating the practitioner's responsibility.

Specifically, the illustrative review reports included in appendix 2 include the following under the caption "Practitioner's Responsibility":

Our responsibility is to express a conclusion on the accompanying financial statements based on our review. We conducted our review in accordance with International Standard on Review Engagements (ISRE) 2400, *Engagements to Review Historical Financial Statements*. ISRE 2400 requires us to conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material respects in accordance with the applicable financial reporting framework. This Standard also requires us to comply with relevant ethical requirements.

We believe that the third sentence of the preceding paragraph will be confusing to users of reviewed financial statements. We believe that the report would be more useful if revised as follows to coincide with our proposed revision to the objective of the review engagement (see our response to IAASB question 3) (deleted language is shown in strikethrough; new language is shown in boldface italics):

Our responsibility is to ~~express a conclusion on the accompanying financial statements based on our review.~~ We conducted our review in accordance with International Standard on Review Engagements (ISRE) 2400, *Engagements to Review Historical Financial Statements*. ISRE 2400 requires us to ~~conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material respects in accordance with the applicable financial reporting framework.~~ This Standard also ~~requires us to~~ ***perform procedures designed to obtain limited assurance that the financial statements are prepared, in all material respects, in accordance with the applicable financial***

reporting framework and to comply with relevant ethical requirements.

In addition, we believe that the disclosure in the report that the review “also requires performance of additional procedures when the practitioner becomes aware of matters that cause the practitioner to believe the financial statements as a whole may be materially misstated,” if included, may result in users inappropriately assuming a higher level of assurance from the practitioner’s report because additional procedures may have been performed. We believe that the use of the term *primarily* when discussing the performance of analytical procedures and inquiries appropriately implies that additional procedures may have been performed. We therefore recommend deleting the sentence “A review also requires performance of additional procedures when the practitioner becomes aware of matters that cause the practitioner to believe the financial statements as a whole may be materially misstated.”

If the IAASB agrees that the preceding edits are appropriate, paragraph 83(a)-(b) should be revised to reflect the previous wording.

Finally, we noted that paragraph 83(c) states that the practitioner shall include in the report a description of a review of financial statements and its limitations, including a statement that a review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing, and consequently does not enable the practitioner to obtain assurance that the practitioner would become aware of all significant matters that might be identified in an audit, and accordingly, the practitioner does not express an audit opinion on the financial statements. We believe that the requirement should mirror the language used in the standard auditor’s report and would be more appropriate and clearer to users of reviewed financial statements if it read as follows (deleted language is shown in strikethrough; new language is shown in boldface italics):

- (c) A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (ISAs), and consequently ~~does not enable the practitioner to~~ **has not obtained reasonable** assurance ~~that the practitioner would become aware of all significant matters that might be identified in an audit~~ **that the financial statements are free of material misstatement** and, accordingly, the practitioner does not express an audit opinion on the financial statements; and

If the preceding changes are made, we believe that the illustrative review reports included in appendix 2 should be revised to mirror the preceding language.

Also, we are confused about the reason why the IAASB included the reporting requirements regarding the nature of the review in a paragraph after paragraph 82, which includes the other reporting requirements. Paragraph 82(f) awkwardly refers to paragraph 83. We believe that the requirements would be more easily understood if paragraph 83 was included in paragraph 82.

In response to the questions posed by the IAASB in the preceding (b) and (c), we do believe that the form of the practitioner's conclusion adequately communicates the assurance obtained by the practitioner. We believe that this wording is far superior to any of the other options that were considered by the IAASB. Additionally, this wording is consistent with the wording currently used by practitioners issuing reports in accordance with extant ISRE 2400, as well as practitioners performing their engagements in accordance with the review standards of jurisdictions where the review engagement is well understood and well accepted by users. We believe that the conclusion expressed in this form clearly differentiates the review conclusion from the opinion expressed in an auditor's report.

Requested comments on proposed effective date

The explanatory memorandum to proposed ISRE 2400 includes the following comment and question:

Recognizing that proposed ISRE 2400 is a substantive revision of extant ISRE 2400, and given the public interest need to harmonize practice internationally as soon as practicable, the IAASB believes that an appropriate effective date for the standard would be 18 months after approval of the final standard. Assuming the IAASB finalizes the revised standard in the first half of 2012, it would then likely be effective for reviews of financial statements for periods ending on or after December 31, 2013. The IAASB welcomes comment on whether this would likely provide a sufficient period to support effective implementation of the ISRE.

We believe that the effective date of proposed ISRE 2400 should be the same as that included in proposed International Standard on Related Services 4410 (Revised), *Compilation Engagements* as consistent effective dates would ease the implementation process for practitioners and small and medium sized practices. The proposed effective date stated in that document is for compilation engagements performed for financial information for periods ending on or after June 30, 2013.

2. Concerns regarding the requirement that the practitioner obtain evidence that the financial statements agree with, or reconcile to, the entity's underlying accounting records

Paragraph 56 of proposed ISRE 2400 states, "The practitioner shall obtain evidence that the financial statements agree with, or reconcile to, the entity's underlying accounting records."

Although we have no objection to the preceding requirement, we are concerned about the heading prior to the previously-referenced paragraph that reads "Reconciling the Financial Statements to the Underlying Accounting Records." We believe that the heading should be revised to coincide with the language used in

paragraph 56, so that it reads “Obtaining Evidence That the Financial Statements Agree With, or Reconcile to, the Entity’s Underlying Accounting Records.”

In addition, the application paragraphs to the requirement stated in paragraph 56 read as follows:

Reconciling the Financial Statements to the Underlying Accounting Records (Ref: Para. 56)

A94. The practitioner ordinarily obtains evidence that the financial statements agree with, or reconcile to, the underlying accounting records by tracing the financial statement amounts and balances to the relevant accounting records such as the general ledger, or to a summary record or schedule that reflects the agreement or reconciliation of the financial statement amounts with the underlying accounting records (such as a trial balance).

Significant or Unusual Transactions in the Accounting Records

A95. The practitioner may consider, where practicable, reviewing the accounting records with a view to identifying significant or unusual transactions that may require specific attention in the review.

We believe that the application material includes wording that may be confusing to practitioners performing a limited assurance engagement. For example, tracing is an audit procedure and also is referred to incorrectly in proposed ISRE 2400 in that the auditor would trace amounts from the accounting records to the financial statements versus the other way around. In addition, although the practitioner is not precluded from agreeing or reconciling the financial statements to the underlying accounting records, we believe that proposed ISRE 2400 would be improved if additional language was provided to put the application material in the appropriate context.

3. Concerns regarding permitting the expression of an adverse conclusion in a limited assurance engagement

Paragraphs 77–78 provide for a practitioner to express an adverse conclusion in a review engagement. We do not believe that an adverse conclusion is appropriate in a limited assurance engagement. We believe that the expression of an adverse conclusion is equivalent to expressing an adverse opinion, and as such, we do not believe that a practitioner should be permitted to express any type of opinion without performing an audit engagement.

Our concern is illustrated by the use of the wording in illustration 4 in appendix 2. The adverse conclusion, as illustrated in that example, reads as follows:

Due to the significance of the matter discussed in the Basis for Adverse Conclusion paragraph, we conclude that the consolidated financial statements do not present fairly (or *do not give a true and*

fair view of) the financial position of ABC Company and its subsidiaries as at December 31, 20X1, and (*of*) their financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

The positive wording used in the adverse conclusion significantly differs from the “nothing has come to our attention” wording that is used in an unmodified review conclusion. We believe that the more appropriate response in a limited assurance engagement is a qualified conclusion or withdrawal, when permitted, from the engagement.

4. Concerns regarding the practitioner’s response when the practitioner is unable to obtain sufficient appropriate evidence as the basis for a conclusion on the financial statements (scope limitation)

We question whether it is appropriate to permit the practitioner to disclaim a conclusion in a limited assurance engagement, unless the practitioner has no other options. We believe that a disclaimer may be confusing to users of the reviewed financial statements. Instead, we believe that a more appropriate response when the practitioner is unable to obtain sufficient appropriate evidence as the basis for a conclusion on the financial statements is, unless prohibited by law or regulation, to withdraw from the engagement.

5. The need for additional guidance with respect to the practitioner’s responsibility for other information in documents containing reviewed financial information

Paragraph A120 discusses the situation in which reviewed financial statements are included in a document that contains other information, such as a financial report. However, proposed ISRE 2400 does not discuss whether the practitioner has any responsibility with respect to that other information. We recommend that proposed ISRE 2400 be revised to discuss the practitioner’s responsibility, if any, with respect to such other information.

6. The need for an illustration of management’s written representations

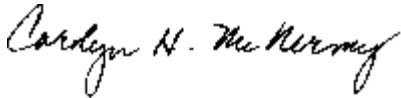
We noted that although proposed ISRE 2400 appropriately includes appendixes providing an illustrative engagement letter and illustrative practitioner’s review reports, it does not provide an illustration of management’s written representations. We believe that the inclusion of such an illustration would be useful to practitioners, especially those who have not performed a review engagement in the past.

7. Need for illustration of an emphasis-of-matter paragraph regarding going concern

Paragraphs 84–86 and A133–A134 provide requirements and guidance with respect to emphasis-of-matter paragraphs. However, proposed ISRE 2400 does not provide guidance regarding reporting when an uncertainty exists regarding an entity’s ability to continue as a going concern. We believe that practitioners would benefit from an illustration showing how a practitioner may report in such a situation.

Thank you for the opportunity to comment on this exposure draft. If you have any questions regarding the comments in this letter, please contact Mike Glynn at +1.212.596.6250 or mglynn@aicpa.org.

Respectfully submitted,



Carolyn H. McNerney

Chair, AICPA Accounting and Review Services Committee