

For the attention of Jim Sylph
International Federation of Accountants
545 Fifth Avenue, 14th Floor
New York, NY, 10017
USA

19 December 2008

Dear Sir

IAASB Consultation Paper – “Matters to Consider in a Revision of International Standard on Review Engagements 2400 *Engagements to Review Financial Statements*”

We appreciate the opportunity to comment on the above consultation paper prepared by staff of the national standard setters for Canada, New Zealand and South Africa to assist IAASB in determining the scope of IAASB’s planned revision of ISRE 2400.

Following extensive consultation with members of the PricewaterhouseCoopers network of firms, this response summarises the views of member firms who commented on this consultation paper. “PricewaterhouseCoopers” refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

Overall comments

The consultation paper presents quite a thorough analysis of detailed technical and process issues that could be addressed in revising extant ISRE 2400.

Our discussions of the questions posed in the consultation paper generated considerable debate. On many of the questions there were very diverse views. On further exploration, it became apparent that the diversity of views reflected differences in perceptions regarding the purpose of financial statement/information reviews—for example, the likely range of users, their expectations and needs, and the assurance such engagements are intended to and should provide.

We came to the conclusion that a clearer understanding of the intended purpose, audience and deliverables of financial statement review engagements is a **necessary precondition** to a properly focused revision of ISRE 2400. In the absence of such an understanding, our concern is that the project will result in endless debates at a conceptual level with little hope of constructive resolution, or, even worse, will result in a standard that provides a product that fails to meet the real needs of users and thus simply creates expectation gaps. If, on the other hand, consensus can be achieved in relation to the various parameters above, it will then be more straightforward to design and articulate in ISRE 2400 a responsive and more specific engagement standard. In our view, a common understanding of what we are trying to achieve is vital in order to design the appropriate work effort, and a report that conveys the assurance provided.

Accordingly, we strongly encourage IAASB to engage directly with potential users in a variety of jurisdictions in order to explore more fully their needs and expectations. We recognise the challenges in planning and conducting such a consultation. However, we believe it is vital that this project is both user focused and practical, and that the project will ultimately be both more efficient and effective if this step is taken. In fact, we seriously question the merits of proceeding with the project without first obtaining such an understanding.

We elaborate on the reasons for this recommendation below.

User expectations

The results from the two surveys quoted in the consultation paper (tables on pages 9 and 10) were not only somewhat surprising, but caused concern. They indicate a considerable range in the level of assurance perceived by *practitioners* to be provided by review engagements relative to audits – indeed, some practitioners perceived it to be a surprisingly high level of assurance. This diversity of views within the profession causes concern because it may well influence the interpretation of the work effort requirements and how they are applied in practice. Furthermore, it appears plausible that users may take more assurance than has actually been obtained, given the nature of this particular assurance engagement – creating the so-called expectation gap.

The survey results also clearly indicate the current wording of the report is not particularly effective in communicating the nature of the engagement and its limitations. Thus, as well as articulating the work effort that is needed to support the desired level of assurance, we believe that IAASB also needs to focus on the content and wording of the review engagement report.

User expectations, and their level of understanding when a negative form of assurance is provided, need to be more clearly established.

The market for review engagements

The recent IAASB strategy development and consultation process generated significant discussion in relation to the needs of small and medium sized entities (SMEs) and small and medium practices. There was little support for the possible creation of separate Big GAAS/Little GAAS frameworks (“an audit is an audit” – a position with which we wholeheartedly agree), and this naturally led IAASB to consider the legitimate and useful alternatives to audits for SMEs.

This is reflected in the IFAC position paper, published in October 2008, which supports a single set of international auditing standards, but also identifies ISRE 2400 review engagements as a possible alternative to audits for SMEs (in the absence of a statutory audit requirement). Several territories already have well established practices in undertaking financial statement review engagements for SMEs, and others are increasingly exploring this option in response to possible widening statutory exemption of small companies from audit requirements. Whilst we do not believe that a review engagement is an *alternative* to an audit *per se*, we are receptive to the proposition that review engagements may meet the assurance needs of at least some users at the SME level.

Some concern was expressed within our network, however, about the effectiveness of stand-alone financial information review engagements for larger, more complex organisations.

ISA 600 contemplates the option of a “review of the financial information of the component using component materiality”. In many cases, this work might be performed by a component auditor who will also be performing a statutory audit of the component and, if so, the review would be similar to an interim review engagement and informed by the auditor’s audit-based knowledge. But ISA 600 does not limit this option to those circumstances.

We are not aware of any other significant market demand for financial information review assurance engagements with public reporting for larger entities, other than the review of interim financial information, which is dealt with separately in ISRE 2410. The latter engagements are undertaken typically for listed or other public interest entities, and are undertaken by the entity’s independent auditor. Consequently they are informed by full audit knowledge.

Implications for the issues raised in the consultation paper

The ISAs are designed to apply to the audit of any entity, both large and small. We found, however, that when we discussed the issues in the consultation paper regarding review engagements, views often differed depending on whether the respondent was thinking in the context of a review of financial statements of an SME, or a review of financial statements of a larger entity.

There was, for instance, considerable debate as to the extent to which an understanding of the entity’s internal control over financial reporting was required in a review engagement. These differences appeared, in part at least, to reflect different perceptions regarding the type and size of client for which the financial statement review engagements would typically be undertaken. In the context of a review of component

financial information in an ISA 600 group audit, for example, some believed it important that the understanding of the entity and its environment be the same as would be required by ISA 315. Equally, many thought that a similar level of understanding would be needed to have an appropriate basis on which to conduct the necessary inquiries and analytical procedures for a stand-alone review of the financial statements of a large, complex entity. In the context of a review of an SME, however, some did not believe that as comprehensive an understanding would be necessary in order to obtain a moderate level of assurance. The differences in view seemed more substantive than just adapting the principle to the different size of entity – they related more fundamentally to the basis that would be needed to conclude that the entity's financial statements were plausible in the circumstances.

There was also a considerable diversity of views as to the extent to which, and the manner in which, fundamental ISA concepts such as a risk-based approach, fraud assessment, identification of significant risks, materiality, etc should be applied in the context of a review engagement. This latter debate also appeared to be influenced by the extent to which participants viewed financial statement review engagements as primarily being designed as an audit substitute for SMEs.

We came to the conclusion that the work effort that would be necessary to obtain a particular defined level of assurance might differ quite substantially for SMEs and for large, complex organisations. At a minimum, we believe that this needs to be more thoroughly investigated before setting out to draft a proposed revised standard.

Conclusion

For all of these reasons, we believe that a much better articulation of the purpose of this type of engagement and the level of assurance it is intended to provide is needed. If this standard is to meet the needs of users, markets and business, it is vital that IAASB more fully understands those needs. It is entirely possible that needs will differ in different jurisdictions. That, in and of itself, would be valuable information. Without such knowledge, IAASB may design a global generic type of engagement that either fails to meet real needs, or, even worse, is perceived to meet specific needs when, in fact, it was never designed to do so and fails short in this regard.

As noted earlier, once there is a common understanding of the level of assurance the review engagement is intended to provide, we believe that many of the questions in the issues paper can be debated and resolved relatively easily.

We would be happy to discuss our views further with you. If you have any questions regarding this letter, please contact Roger Marshall (+44 20 7213 3171) or Alun Richards (+44 20 7804 2706).

Yours faithfully,

PricewaterhouseCoopers