



December 1, 2003

Mr. James Sylph
Technical Director
International Auditing and Assurance Standards Board
545 Fifth Avenue, 14th Floor
New York, NY 10017

Re: Proposed International Standard on Auditing "Review of Interim
Financial Information Performed by the Auditor of the Entity"

Dear Mr. Sylph:

IOSCO's Standing Committee No. 1 ("SC 1") appreciates the opportunity to comment on the Exposure Draft of the Proposed International Standard on Auditing, "Review of Interim Financial Information Performed by the Auditor of the Entity."

IOSCO is committed to enhancing the integrity of financial information available to participants in capital markets by promoting the development of high quality accounting and auditing standards, supported by rigorous application and enforcement. In reviewing this Exposure Draft, we have focused on how any auditor involvement with interim financial information can be designed in a way that provides a meaningful level of assurance as to the credibility of information used by participants in capital markets to make investment decisions. Our comments reflect those matters on which we have reached a general consensus and are not intended to include all the comments that might be provided by individual members or behalf of their respective jurisdictions in the future.

Timely disclosure of relevant and reliable financial information is crucial to the efficient operation of capital markets. While the specific requirements for disclosure of periodic financial information, including its frequency and the extent of auditor involvement, vary among jurisdictions, it is clear that interim financial information can have a significant impact on market prices. SC 1 would therefore welcome development of a rigorous standard for interim reviews that addresses the concerns noted in this letter.

Scope of application

We believe that any review of interim financial information of an entity supplying information to investors in the capital markets should be performed by an auditor who has obtained the level of understanding of the entity and its risks and business environment, including its internal controls, that would be

required to perform an audit. This would normally be the auditor who audited that entity's most recent annual financial statements. If this is not the case, the auditor performing the review should obtain an equivalent level of understanding of the entity through communications with the predecessor auditor and by carrying out other procedures. We might term this level of understanding to be "an audit base level of knowledge."

Objective of an Interim Review

We believe that the objective of a review of interim financial information needs to be clearly and comprehensively described in the proposed standard. The objective stated in paragraph 9 of the Exposure Draft is primarily descriptive of the resulting form of report and explains neither the context nor the purpose of the review.

We urge the Board to consider whether guidance that might enhance understanding of the objective of an interim review might be obtained or adapted from relevant statements in other existing ISAs, or otherwise be developed. For example, our review of some of the other ISAs produced the following possible elaborations:

- 1.) The object of a review of interim financial information, as with other assurance engagements, is for a professional accountant to evaluate or measure a subject matter that is the responsibility of another party against identified suitable criteria, and to express a conclusion that provides the intended user with a level of assurance about the subject matter. . . In this regard, the level of assurance provided by the professional accountant's conclusion conveys the degree of confidence that the intended user may place in the credibility of the subject matter." (Adapted from ISA 100, paragraph 4).
- 2.) "The expression "moderate level of assurance" refers to the professional accountant having obtained sufficient appropriate evidence to be satisfied that the subject matter is plausible in the circumstances. It is expressed in the form of "negative assurance", i.e., stating that after carrying out a systematic methodology, nothing came to the auditor's attention, that would call the subject matter into question. The professional accountant designs the engagement to reduce to a moderate level the risk of an inappropriate conclusion". (Adapted from ISA 100, paragraph 30 and statements in other ISAs)
- 3.) "Assurance in the context of this Framework refers to the auditor's satisfaction as to the reliability of an assertion being made by one party for the use of another party. To provide such assurance, the auditor assesses the evidence collected as a result of procedures conducted and expresses a conclusion. The degree of satisfaction achieved and, therefore, the level of assurance that may be provided is determined by the procedures performed and their results. In an audit engagement, the auditor provides a high, but not absolute, level of assurance that the information subject to audit is free of material misstatement. This is expressed positively in the audit report as reasonable assurance. In a review engagement, the auditor provides a

moderate level of assurance that the information subject to review is free of material misstatement. This is expressed in the form of negative assurance.” (ISA 120 Framework of International Standards on Auditing, paragraphs 6-8. We also note that paragraphs 14-16 address the objective and process of a review.)

We supply the preceding passages only as examples of possible additional “types of explanation” that might be useful in clarifying the objective and purpose of an interim review. We have not reviewed the proposed standards on Assurance Engagements to see what might be usefully drawn from those standards. Notwithstanding the statements made in the present ISA 100 that it does not supersede other ISAs and “does not apply to an audit or review of financial statements”, our point is that more needs to be said about the objective and purpose of an interim review. Without a clearly explained objective to work towards, we are concerned that auditors performing an interim review will have difficulty determining the level of work that should be performed.

Agreeing to the Terms of the Engagement

The Exposure Draft contains provisions that some believe might be interpreted as strongly suggesting that the management of the entity publish the review report of the auditor (e.g., Paragraph 12, last bullet point and Paragraph 52). While some may believe that publication of a review engagement report is appropriate whenever a review has been performed, this is a matter to be determined by companies and their auditors in accordance with regulatory requirements in each jurisdiction. In the last bullet of paragraph 12, we believe any potential for misunderstanding could be avoided by revising the wording along the following lines: “Management’s agreement that, where any document containing interim financial information indicates that the information has been reviewed by an independent public accountant, the review report will also be included in the document or management will indicate in the document where such report can be obtained.” A similar amendment would be appropriate in paragraph 52.

Procedures for a Review of Interim Financial Information

Paragraph 20 refers to inquiries and analytical procedures only. Some of the procedures listed in the paragraphs that follow are neither inquiries nor analytical procedures. This section should be revised to describe more appropriately and completely the procedures. We also note that Paragraph 21 contains a long list of inquiry procedures the auditor performs but falls short in the guidance given on analytical procedures, which is mentioned in only one paragraph in the text. Analytical procedures should receive more emphasis in the body of the standard.

Extent of Interim Review Procedures and Corroboration Needed

In our view, the interests of investors will be best served by the IAASB developing a form of interim review engagement that, while based primarily

on inquiry, analysis and discussion, also includes explicit requirements to perform at least limited procedures to verify representations reflected in the interim financial statements when the auditor encounters trends or other information that seem questionable or implausible

In our view, the Exposure Draft is unclear on when or whether an auditor carrying out a review of interim financial information is required to carry out procedures to verify assertions and corroborate management's explanations. For example, should the auditor carry out the process described in ISA 520, Analytical Procedures, paragraphs 17 and 18 (a) and (b)?

While we understand that a review is not an audit and that the extent of procedures for a review will differ from that for an audit, we believe the auditor should evaluate in some way explanations provided by management in a review. And if the auditor's knowledge of the business does not provide a basis for accepting the appropriateness of the explanations, the auditor should seek to corroborate such explanations. We believe the final interim review standard should provide guidance on this subject that would likely be similar to the guidance in paragraph 18 of ISA 520. More broadly, we recommend that the Board explain how the requirements relating to the application of analytical procedures in the context of an audit, as set out in ISA 520, apply in the context of a review.

Paragraph 27 of the Exposure Draft provides guidance to be used when the auditor becomes aware of events or conditions that may cast doubt on the entity's ability to continue as a going concern and is another example of an area in which clarification is needed. We recognize that the extent of required procedures for the *detection* of going concern considerations in a review could differ from those required in an audit. However, since the going concern assumption is fundamental to the basis on which financial statements are prepared, once the auditor becomes aware of events or conditions that cast significant doubt on the entity's ability to continue as a going concern, additional procedures such as those expected for an audit engagement should also be applied in a review. If this were not done, there is a risk that the auditor's interim report, when there is going concern doubt, may not appropriately highlight problems for investors. For example, if the auditor does not perform the procedures in ISA 570, the auditor cannot properly evaluate disclosures in the interim financial information regarding management's plans for the future, as is currently required in Paragraph 27 of the Exposure Draft.

We believe that the last sentence in paragraph 28 of the Exposure Draft which states "However, it is not ordinarily necessary for the auditor to corroborate the feasibility of management's plans..." should be deleted or clarified. "Ordinarily" as used here implies it is usually not necessary (but sometimes is necessary) and only adds to the ambiguity. We believe some corroboration is needed.

Interactions with Other ISAs

The preamble to ISAs states that ISAs are to be applied, as appropriate, in the audit or review of historical financial information. Clarification is needed as to what is meant by "as appropriate" in the context of review engagements. For example, some members take this to mean the ISAs that contain content that specifically addresses review engagements. Others take this to mean all ISAs, including audit-related ISAs, as adapted by the auditor's judgment to review engagements.

We note that the Exposure Draft covers in summary a number of matters that are covered in other ISAs. For example, quality control is covered in paragraph 7, going concern in paragraphs 27 and 28, management representations in paragraphs 33 and 34, accompanying information in paragraph 35 and documentation in paragraph 54. We do not believe it is appropriate to apply a lower level of quality control or documentation, for example, to an interim review. However, the Exposure Draft seems to imply that such may be the case by addressing these matters in a somewhat cursory manner.

Paragraphs 4 and 17 state that a practitioner recently appointed as the auditor must obtain an understanding of the entity before performing the review. Some guidance is also provided on this in paragraphs 17 and 18. As noted in our opening comments in this letter, we believe that an auditor performing a review under this standard should have an "audit base level of knowledge". In our view, more guidance is needed on obtaining the understanding of the entity to provide that audit base level of knowledge for interim reviews. We also note that engagements beginning with a review of interim financial information are not adequately covered in the audit risk standards. There should be references to the procedures in the audit risk ISA "Obtaining an Understanding of the Entity and its Environment," including internal control procedures. There should also be a reference to the procedures in ISA 510, "Initial Engagements-Opening Balances." The extent to which these ISAs apply to interim reviews should be clearly stated in the final standard or it should be indicated that the auditor should develop an understanding that is equivalent to the understanding that would be developed in preparation for an audit engagement.

The last sentence in Paragraph 18 states, "If the predecessor auditor does not respond to the auditor's inquiries or does not provide access to the documentation, the auditor uses alternative procedures to obtain the required understanding." We believe guidance is necessary on alternative procedures that might be performed. In general, except for changes necessary to reflect the lesser extent of work performed and the lower level of assurance provided in the report, we believe the guidance for a review of interim financial statements should mirror guidance for audit engagements in respect of general auditor performance matters such as quality control (draft ISA 220), documentation (ISA 230), communication with those charged with governance (ISA 260), materiality (ISA 320), using the work of another auditor (ISA 600) and using the work of an expert (ISA 620). We believe the Board

should clarify this in the final standard. The relevant guidance from other standards should be reflected consistently in the final ISA on Review of Interim Financial Statements. It may be that this can best be achieved by a combination of including a more robust level of text from the other ISA(s) in this ISA and also cross-referencing back to the other ISA(s).

Interaction of the Interim Review and the Annual Audit

The primary goal of the final interim review standard should be to set out clearly the procedures to be performed in an interim review to enable the auditor to reach an appropriate conclusion and make the appropriate review report. At the same time, we believe there can be significant advantages to an auditor performing certain work done during the interim review in sufficient detail to gather evidence that will also support the audit opinion that the auditor will issue on the annual financial statements. Some of the more obvious examples of this arise in the case of business combinations and unusual transactions, which are noted in paragraph 23 as matters for which auditing procedures "could" be performed.

Paragraph 23 of the Exposure Draft acknowledges that for convenience and efficiency certain audit procedures may be performed concurrently with the review of interim financial information. The text provides some examples, but does not fully develop this topic. Because such audit-level procedures may contribute to strengthening the effectiveness of both the audit and the interim review, as well as being convenient and efficient, we recommend that the Board provide additional guidance on how the auditor should identify opportunities for dual benefit. An approach to auditor involvement with interim financial statements that is integrated with the audit of the annual financial statements should make for a more robust review that will contribute to enhancing the reliability of both interim and annual financial information.

Reporting the Nature, Extent and Results of Interim Review and Appendix 3

We had a significant discussion among our members about whether a report that uses "presents fairly" or "true and fair" language, as in the second example in Appendix 3, would ever be appropriate in the context of a review. We believe there is at least a possibility that use of such language could increase confusion over the difference between the nature of a review and the nature of an audit, and the degree of assurance being expressed.

For this reason, most of our members believe there should be a single consistent form of report for the review of both a complete set of financial statements and condensed financial statements. We recommend using the example of the report for the condensed set of financial statements, with revisions to include the following:

1. A lead-in at the beginning of the report stating that the public accountant performing the review is the auditor of the entity.

2. A reference in the second paragraph to the auditor's understanding of internal control so that there is a higher level of assurance
3. A revision of the language in the conclusion of the example condensed financial information report to state "we are not aware of any material change (rather than modification) that needs to be made to the accompanying interim financial information for it to be in accordance with [the identified financial reporting framework]..."

Ultimately, the Board should also consider how the content of a review engagement report might be affected by the approach proposed in the current project on the auditor's report.

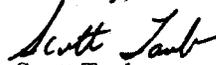
We noted that an adverse report for noncompliance with the reporting framework is not covered in the Exposure Draft. We believe guidance or a sample adverse report, as well as coverage of disclaimers, should be included, if such a report is possible. We also wondered why an example of a modified review report was included only for the case where the interim financial information was comprised of a condensed set of financial statements, i.e., is there some reason why such a report could not occur with a complete set of financial statements? If so, it would be helpful to have this stated explicitly. It would also be helpful to make clear what forms of review report are possible.

Inability to Complete a Review

Paragraph 38 states that "the review would be incomplete if the entity's internal control appears to contain deficiencies so significant that it would be impracticable for the auditor to effectively perform review procedures that would provide a basis for reporting whether the auditor is aware of any material modification that is required ..." We believe more guidance is needed as to the actions the auditor should take if the review cannot be completed because of a deficiency in internal control.

If you have any questions or need additional information on the recommendations and comments that we have provided, please do not hesitate to contact me on (202) 942-4400.

Sincerely,



Scott Taub

Chair

IOSCO Standing Committee No. 1