

The Auditor's Report on Other Historical Financial Information and the Auditor's Report on Summarized Audited Historical Financial Information— Proposed Explanatory Memorandum

Introduction

This memorandum provides background to and an explanation of the proposed revised International Standard on Auditing (ISA) 800, under a new title of “The Independent Auditor’s Report on Other Historical Financial Information” and the proposed new ISA 810, “The Auditor’s Report on Summarized Audited Historical Financial Information” approved for exposure by the International Auditing and Assurance Standards Board (IAASB) in March 2005.

Background

Extant ISA 800, “The Auditor’s Report on Special Purpose Audit Engagements” was last revised in March 1994. ISA 700 (Revised), “The Independent Auditor’s Report on a Complete Set of General Purpose Financial Statements” and conforming amendments to ISA 200, “Objective and General Principles Governing an Audit of Financial Statements,” which were approved in December 2004, not only gave rise to conforming amendments to extant ISA 800, but also highlighted the need for a more comprehensive revision. In particular, the scope of ISA 700 (Revised) was limited to auditors’ reports on complete sets of general purpose financial statements prepared in accordance with a financial reporting framework designed to achieve fair presentation. Consequently, as explained below, the scope of the proposed revised ISA 800 had to be expanded beyond auditors’ reports on special purpose audit engagements to include auditors’ reports on general purpose audit engagements that do not meet the scope of ISA 700 (Revised).

Proposed New ISA Establishing Standards and Guidance for Auditors’ Reports on Summarized Audited Historical Financial Information

Standards and guidance on the auditor’s report on summarized audited historical financial information are contained in extant ISA 800, paragraphs 21-25. The project proposal to revise extant ISA 800 recommended that consideration be given to the nature of an engagement to report on summarized audited historical financial information, i.e., whether it is an audit, an other assurance engagement, or a related services engagement, and, consequently, whether the related standards and guidance should be retained within the proposed revised ISA 800.

The IAASB concluded that, because summarized historical financial information is derived from audited historical financial information and the auditor’s report on summarized financial information is closely linked to the auditor’s report on the historical financial information from which it has been derived, the standards and guidance should form part of the ISAs. However, the IAASB is of the view that the standards and guidance would be better placed in a separate ISA, i.e., ISA 810, “The Independent Auditor’s Report on Summarized Audited Historical Financial Information.”

Significant Proposals

PROPOSED REVISED ISA 800

Scope of the Proposed Revised ISA 800

The proposed revised ISA 800 covers auditors' reports on historical financial information other than a complete set of general purpose financial statements prepared in accordance with a financial reporting framework designed to achieve fair presentation. Standards and guidance for this are contained in ISA 700 (Revised). Paragraphs 1-6 of the proposed revised ISA 800 explain auditors' reports the ISA establishes standards and guidance, and the interrelationship with ISA 700 (Revised) and the proposed revised ISA 701, "Modifications to the Opinion in the Independent Auditor's Report."

Paragraph 4 of the proposed revised ISA 800 explains that historical financial information prepared in accordance with a financial reporting framework designed for a general purpose could be used for a special purpose, and historical financial information prepared in accordance with a financial reporting framework designed for a special purpose could be used for a general purpose. Therefore, for purposes of the proposed revised ISA 800, a distinction is drawn between the purpose for which the financial reporting framework was designed, and the purpose for which the financial information has been prepared or the use to which the financial information is put. A similar distinction is not drawn in ISA 700 (Revised), which focused on the purpose for which the financial reporting framework was designed. A conforming amendment is proposed to ISA 700 (Revised) to clarify the fact that the standards and guidance in ISA 700 (Revised) apply to auditors' reports on complete sets of financial statements, which have been prepared in accordance with a financial reporting framework designed for a general purpose to achieve fair presentation, but which will be used for a special purpose. The standards and guidance in paragraphs 47-53 of the proposed revised ISA 800 also apply to these engagements. These standards and guidance contain considerations specific to reporting on historical financial information prepared for a special purpose.

To avoid repetition and to highlight more clearly those matters that are different when reporting on other historical financial information, the proposed revised ISA 800 contains references to the relevant standards and guidance of ISA 700 (Revised).

Application of Ethical Requirements and Other ISAs in an Audit to Report on Other Historical Financial Information

Paragraph 8 of the proposed revised ISA 800 requires the auditor to comply with relevant ethical requirements relating to audit engagements and each of the ISAs relevant to the audit of the other historical financial information. Generally, the ISAs are written in the context of an audit of financial statements, which is described in paragraph 34 of ISA 200 as a complete set of financial statements or a single financial statement. The proposed revised ISA 800 also establishes standards and provides guidance for auditors' reports on one or more specific elements, accounts or items of a financial statement, and other historical financial information prepared for a special purpose. Paragraphs 10-11 explain that in an audit of other historical financial information the auditor may find it necessary to adapt the standards and guidance in the other ISAs to the particular engagement circumstances. The auditor, however, has to be satisfied that application of the adapted standards and guidance will

result in an audit conducted in accordance with ISAs, that is, compliance with each of the ISAs relevant to the audit of the other historical financial information.

Applicable Financial Reporting Framework

Paragraphs 13-21 of the proposed revised ISA 800 provide guidance on the application of the requirement in ISA 200, paragraph 37, for the auditor to determine whether the financial reporting framework adopted by the responsible party in preparing and presenting the other historical financial information is acceptable in the engagement circumstances. Paragraph 20 explains that, depending on the engagement circumstances, the set of criteria constituting the financial reporting framework may encompass not only the accounting standards promulgated by means of law or regulation, by authorized or recognized standards setting organizations, or the provisions of a contract, but may also encompass:

- The effect of the legal environment, including statutes, regulations and court decisions in relation to accounting matters;
- Published views on emerging accounting issues and accounting interpretations of varying authority issued by standards setting, professional or regulatory organizations;
- Industry practices widely recognized and prevalent; and
- Accounting literature.

The auditor considers whether, in the context of the engagement circumstances, the financial reporting framework exhibits the characteristics of suitable criteria described in paragraph 36 of the International Framework for Assurance Engagements.

Form of Opinion and Forming the Opinion

Paragraph 22 of the proposed revised ISA 800 explains that the form of opinion that the auditor considers to be appropriate depends on the engagement circumstances. According to paragraph 23, if the financial reporting framework has been designed to achieve fair presentation uses the terms “give a true and fair view” or “presents fairly, in all material respects” to express the audit opinion on the other historical financial information, unless otherwise required by law or regulation. Where these terms are used, the auditor considers the fair presentation of the financial information in accordance with the guidance in ISA 700 (Revised), paragraphs 14-15, adapted as necessary to the engagement circumstances.

The terms “give a true and fair view” or “presents fairly, in all material respects” may be used in an audit opinion on a single financial statement or a specific element, account or item of a financial statement. However, the guidance states that fair presentation ordinarily is achieved only when the financial statement, element, account or item has been prepared in accordance with all the requirements of a financial reporting framework designed to achieve fair presentation relevant to such financial statement, element, account or item, and includes all the relevant accompanying notes.

According to paragraph 24, if the other historical financial information has been prepared in accordance with a financial reporting framework that does not require, or that prohibits, departure from, or disclosures beyond, the specific requirements of the framework in order to achieve fair

presentation, the auditor uses the term “prepared, in all material respects, in accordance with the applicable financial reporting framework” to express the audit opinion on the other historical financial information.

Paragraph 25 provides for circumstances where there is no obligation on the responsible party to achieve fair presentation in preparing and presenting the other historical financial information in accordance with the applicable financial reporting framework. In these circumstances, the auditor may not be in a position to require departure from, or disclosures beyond, the specific requirements of the framework in order to achieve fair presentation. Consequently, the auditor does not use the terms “give a true and fair view” or “presents fairly, in all material respects,” to express the audit opinion on the other historical financial information. The auditor may use the term “prepared, in all material respects, in accordance with the applicable financial reporting framework.”

Paragraph 31 clarifies that, when terms other than “give a true and fair view” or “presents fairly, in all material respects, are used to express the audit opinion on the other historical financial information (for example, “prepared, in all material respects, in accordance with the applicable financial reporting framework”), the auditor nevertheless considers whether the other historical financial information may be misleading in the engagement circumstances.

Restriction on Use and Distribution

When the other historical financial information has been prepared in accordance with a financial reporting framework designed for a special purpose, paragraph 35 of the proposed revised ISA 800 requires the auditor to make a user of the financial information aware of the fact that it has been prepared in accordance with a financial reporting framework designed for a special purpose and, as a result, may not be suitable for another purpose. In addition, when the other historical financial information has been prepared for a special purpose, paragraph 53 requires the auditor to consider including a statement in the auditor’s report that the auditor’s report is intended only for the intended users and should not be distributed to or used by parties other than the intended users.

PROPOSED REVISED ISA 810

Scope of the Proposed ISA 810

The standards and guidance in proposed ISA 810 apply when the auditor is engaged to report on summarized financial information derived from historical financial information audited by that auditor.

Criteria

The proposed ISA 810 recognizes that established criteria for preparing and presenting summarized audited historical financial information may not exist. Paragraph 13 establishes criteria to be used in such circumstances. Paragraph 12 explains that when established criteria do not exist, the risk that the summarized audited historical financial information may misrepresent the audited historical financial information increases. Consequently, the auditor considers whether the criteria in paragraph 13 are acceptable in the engagement circumstances, including, in particular, the purpose for which the summarized audited historical financial information has been prepared, before accepting an engagement to report on such information.

Nature of Procedures

Paragraph 14 of the proposed ISA 810 contains guidance on the procedures performed by the auditor as the basis for the auditor's opinion on the summarized audited financial information. The procedures include evaluating whether the summarized audited historical financial information, in all material respects, contains the information that the auditor considers necessary in the engagement circumstances so as not to result in a misrepresentation of the audited historical financial information (including the related notes) as a whole.

Paragraph 15, however, recognizes that circumstances may exist where the responsible party is required or expressly permitted by law or regulation to issue summarized audited financial information, and such law or regulation (a) establishes the criteria for preparing and presenting the summarized audited financial information, but (b) does not require the responsible party to prepare and present summarized audited financial information that, in all material respects, contains the information necessary in the engagement circumstances so as not to result in misrepresentation of the audited historical financial information. Where this is the case, the auditor (a) does not evaluate whether the summarized audited historical financial, in all material respects, contains the information necessary so as not to result in misrepresentation of the audited historical financial information, and (b) expresses an opinion whether the summarized audited financial information has been prepared, in all material respects, in accordance with the established criteria.

Audit Opinion on Summarized Audited Historical Financial Information

Extant ISA 800 requires the auditor to report whether the summarized audited historical financial information is "consistent, in all material respects" with the historical financial information from which it has been derived. Other standard setters have chosen different terms, such as "fairly stated, in all material respects, in relation to ..." (United States), and "fairly summarized, in all material respects, ..." (Canada).

The IAASB is of the view that, except in the circumstances described in paragraph 15 of the proposed revised ISA 800, it is not appropriate for the auditor to limit his or her procedures to a "consistency check." As explained above, the auditor also evaluates whether the summarized audited historical financial information, in all material respects, contains the information that he or she considers necessary in the engagement circumstances so as not to result in misrepresentation of the audited historical financial information (including the related notes) as a whole. The findings of this evaluation are to be reflected in the auditor's opinion.

The IAASB considered the terms "fairly stated, in all material respects" and "fairly summarized, in all material respects," but concluded they may not be appropriate. ISA 700 (Revised) and proposed revised ISA 800 distinguish financial reporting frameworks designed to achieve fair presentation from other frameworks, and provide guidance on the use of the terms "give a true and fair view" and "presents fairly, in all material respects." Consequently, the use of terms such as "fairly stated, in all material respects," and "fairly summarized, in all material respects" in the audit opinion on summarized audited historical financial information, may not be appropriate.

The IAASB proposes that, except in the circumstances described in paragraph 15 of the proposed revised ISA 800, the auditor express an opinion whether the summarized financial information appropriately summarizes, in all material respects, the historical financial information from which it has been derived.

PRESCRIBED REPORTS

Both proposed ISAs recognize that the auditor's report on other historical financial information may be required by law or regulation to be in a prescribed form that may not conform to the requirements of the ISAs. When required to report in a prescribed form, the auditor considers whether the substance and wording of the prescribed report are appropriate in the engagement circumstances. If the auditor concludes that the substance or wording of the prescribed report is not appropriate in the engagement circumstances, the auditor is required to make appropriate changes to conform to the requirements of the ISAs, either by rewording the prescribed report or by substituting the prescribed report with a report that conforms to the requirements of the ISAs. If the auditor is not permitted to do so, the auditor does not report on the other historical financial information or summarized audited historical financial information, unless the auditor is required by law or regulation to report in such prescribed format.

Conforming Amendments

The proposed revised ISA 800 gave rise to conforming amendments to ISA 200, ISA 700 (Revised) and ISA 701. These are set out in the appendix to this exposure draft.

Effective Date

The IAASB recommends that the proposed ISAs 800 and 810 have the same effective date as that of ISA 700 (Revised) and ISA 701. ISA 700 (Revised) and ISA 701 are effective for auditors' reports issued on or after December 31, 2006.

Guide for Commentators

The IAASB welcomes comments on the proposed ISAs 800 and 810. The IAASB is seeking comments on all matters addressed in the exposure draft. Comments are most helpful when they refer to specific paragraphs, include the reasons for the comments, and, where appropriate, make explicit suggestions for any proposed changes to wording. When a respondent agrees with proposals in this exposure draft (especially those calling for change in current practice), it will be helpful for the IAASB to be made aware of this view.

Recognizing that the proposed ISAs will apply to audits of all sizes and in all sectors of the economy, the IAASB is also interested in comments on matters set out below:

SPECIAL CONSIDERATIONS IN THE AUDIT OF SMALL ENTITIES

Consistent with the IAASB's decision to include any special considerations in the audit of small entities within the text of the ISAs, respondents are asked to comment on whether, in their opinion, considerations in the audit of small entities have been dealt with appropriately in the proposed ISAs. Reasons should be provided if not in agreement, as well as suggestions for alternative or additional guidance.

SPECIAL CONSIDERATIONS IN THE AUDIT OF PUBLIC SECTOR ENTITIES

A representative of a working group of the Auditing Standards Committee of the International Organization of Supreme Audit Institutions participated in the development of the proposed ISAs 800 and 810. Special considerations in the audit of public sector entities have been included within the text proposed ISAs. Respondents are asked to comment on whether, in their opinion, special considerations in the audit of public sector entities have been dealt with appropriately in the proposed ISAs. Reasons should be provided if not in agreement, as well as suggestions for alternative or additional guidance.

TRANSLATIONS

Recognizing that many respondents intend to translate the proposed ISAs 800 and 810 for adoption in their own environments, the IAASB welcomes comment on potential translation issues noted in reviewing this exposure draft.

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