

Inquiry and Analytical Procedures in Conducting a Review Engagement

This is the sixth article in the series highlighting the requirements of the new review engagement standard, Canadian Standard on Review Engagements (CSRE) 2400 – *Engagements to Review Historical Financial Statements*, which becomes effective for reviews of financial statements for periods ending on or after December 14, 2017, with no option for early adoption.

INQUIRY AND ANALYTICAL PROCEDURES IN CONDUCTING REVIEW ENGAGEMENTS

This article outlines the importance of inquiry and analytical review procedures in conducting a review engagement. CSRE 2400 paragraph 46 requires a practitioner to design and perform inquiry and analytical procedures to:

- Address all material items in the financial statements, including disclosures; and
- Focus on addressing areas in the financial statements where material misstatements are likely to arise.

In selecting the procedures to be performed, the practitioner needs to use professional judgment. Inquiry and analytical procedures need to be designed to ensure that the practitioner obtains sufficient appropriate evidence as the basis for a conclusion on the financial statements as a whole. A number of matters that a practitioner should consider when designing and performing inquiry and analytical procedures are discussed below.

Analytical Procedures

When designing and interpreting analytical procedures the practitioner should:

- Apply professional skepticism. It may not always be appropriate to only complete a comparison of the financial statement item totals with the prior year, although this may assist in identifying areas where material misstatements are likely to arise. Often, for example, comparison with the prior year on a disaggregated basis (sales by product line or customer) rather than comparing total sales to the prior year would provide better evidence.

- Interpret the results from performing analytical procedures and consider if they are consistent with other information known to the practitioner and whether further procedures should be considered. For example, if the ratio of days' sales in inventory shows an increase, more work may be needed to ensure that there is no misstatement in inventory due to inaccurate counts or valuation errors.
- Consider the anticipated outcome of analytical procedures before conducting analysis. Without making this consideration, a "no change" comparison may incorrectly indicate that there is not a material misstatement in the current year amounts. For example, if the practitioner knew that the particular industry was doing very well their expectation would be that there should be an increase in sales. Consequently, no change in sales from the prior year should indicate that further work is necessary.
- Exercise care to ensure that explanations contained in the working papers as to the results of analytical procedures are not overly broad. For example, if the explanation received for the increase in inventory was that sales declined, the practitioner would not only need to ensure that sales indeed declined, but also consider whether this is indicative of inventory valuation issues. The explanation for the increase in inventory needs to be further probed and perhaps additional analysis should be performed on inventory.

Inquiry

Together with performing analytical procedures, the practitioner is required to make sufficient inquiries relating to the material financial statement items and areas where material misstatement may arise. The inquiries should be probing questions, which provide the evidence required. Professional judgment is needed in determining the correct inquiries, and then professional skepticism is needed to make sure that the responses received make sense in relation to the other information known to the practitioner. Again, the practitioner should be alert as to whether the answers to the inquiries require that further procedures be considered. For example, if an explanation received for the increase in accounts payable is that cash flow is tight, but the practitioner knows from his review of the bank accounts that the balances on these accounts have improved from the prior year, the practitioner should consider revising his or her inquiry. The practitioner should perhaps inquire as to why the cash balances have improved and compare the results of this inquiry with the change in accounts payable. It may also be necessary to expand his or her inquiry to consider the accounts payable cut-off, which may be incorrect, thereby resulting in a misstatement of accounts payable.

Obtaining Responses from Appropriate People

Inquiries should be made of the appropriate people who have knowledge of the subject matter of the inquiry. For example, asking the bookkeeper if the provision for rehabilitation of the mining site has been properly calculated could lead to the incorrect answer, as the bookkeeper most probably did not prepare these complex calculations. It would be better to direct more detailed questions to the person who completed the calculation.

Soliciting Sufficient Responses

Inquiries should solicit a response, which is sufficient in detail so that the practitioner can obtain sufficient evidence. For example, asking why expenses increased is too general. It would be better to ask specific questions about each expense, such as asking why wages have gone up even though there were no new employees in the entity. If legal fees have increased, it would be a good idea to ask if there were there any legal problems in the year.

DOCUMENTATION

As per CSRE 2400 paragraphs 104 to 107, the practitioner is required to document the analysis performed together with the inquiries made and the results of the inquiries. Documentation of the results of inquiries should contain the name of the individual who the inquiry was made of and the date of the inquiry. The practitioner must assess these results in order to properly understand whether sufficient appropriate evidence has been obtained and whether a conclusion on the financial statements as a whole can be made.

CONCLUSION

The practitioner needs to be satisfied that inquiry and analytical procedures are designed and performed in accordance with the requirements of CSRE 2400, paragraph 46.

RESOURCES AND TOOLS

Various tools and resources available to assist with understanding CSRE 2400 include the following:

- [Guide to Review Engagements \(CSRE\) 2400](#). In addition to being a useful guide in general, it provides guidelines in Chapter 5.1-2 on how best to formulate inquiries and analyze the responses.
- CPA Canada's *Audit & Assurance Alert: Engagements to Review Historical Financial Statements (CSRE 2400)*.

- CPA Canada's *Audit & Assurance Alert*: [Comparison between CSRE 2400 and the 8000 Series](#).
- [Review Engagement Practitioner Client Briefing](#) helps clients understand what they need to know regarding the new review engagement standard.
- Professional development courses available through CPA Ontario.
- Review engagement checklists for CSRE 2400 in the [Professional Engagement Guide](#).
- Practice Advisory Services. For further guidance, members are encouraged to contact a Practice Advisor at CPA Ontario:
 - Phone: 416 962.1841, ext. 4456 or 1 800 387.0735, ext. 4456.
 - Email: practiceadvisory@cpaontario.ca or memberadvisory@cpaontario.ca.