

REVIEWER ALERT



November 2016

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Upcoming Changes Approved at the November 14, 2016 Peer Review Board (PRB) Open Session

The following agenda items can be found on the [AICPA website](#). See the following [webpage](#) for meeting highlights and an overview of other changes the PRB approved during the meeting.

Modifications of Report and Representation Letter Guidance Changes (Agenda Item 1.2*)-Please see the [following article](#) for details and illustrations

Alternative Practice Structure Supplemental Form for QCPP Compliance and Design Testing (Agenda Item 1.3*)

During the May 2015 Peer Review Board (PRB) meeting, the PRB approved new checklists for evaluating a firm's system of quality control. At that time, the PRB directed staff to develop checklists to replace those at PRP Sections 5100, 5200 and 5300 for firms aligned with non-CPA owned entities. The new 4-page form (reduced from 32 pages), effective for reviews commencing on or after January 1, 2017 (Agenda Item 1.3A):

- Incorporates the concepts covered in the current instructions to PRP Sections 5100, 5200 and 5300 while providing new examples and guidance to increase clarity;
- Refers reviewers to the new Design and Compliance QC checklists to assist them in evaluating design and testing for compliance; and

- Requires reviewers to document
 - Non-compliance with QC Section 10 on the Design checklist, and
 - Non-compliance with the firm's QCPP on the Compliance checklist.

*see agenda item for further information

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Peer Review Reports and Firm Representation Letter Illustrations

Final changes to the Standards were approved by the PRB during its November 14, 2016 Open Session (refer to Agenda Item 1.2). The changes are effective for peer reviews commencing on or after January 1, 2017. Key changes to the guidance pertain to the peer review report and firm representation letter wording used when firms perform audits in accordance with *Government Auditing Standards* (GAS) including compliance audits under the Single Audit Act.

The scenarios presented below are intended to provide illustrations of firm representation letters and peer review reports under the new guidance and consider the following situations:

1. Firms that perform audits subject to both GAS and the Single Audit Act.
2. Firms that perform engagements subject to GAS only, in addition to audits subject to both GAS and the Single Audit Act.

Scenario 1 (firm performs audits subject to both GAS and the Single Audit Act)

The firm of Smith & Jones, LLP performed an audit of a not-for-profit entity that is subject to *Government Auditing Standards* and the Single Audit Act. This firm also audited an employee benefit plan. The financial statements of both the not-for-profit entity and the employee benefit plan fall into the firm's peer review year and both audit engagements were selected and reviewed by the firm's peer reviewer (Bobbye Kelly, CPA). The peer review year end was June 30, 2017 and the exit conference was conducted on October 31, 2017. The peer review report rating was pass. The firm's administering entity is the North Carolina Association of CPAs. Notice that references to Single Audit Act engagements are combined with references to engagements performed under *Government Auditing Standards* as the requirement to select one of each type was met through the selection of engagements from one entity.

Firm Representation Letter (no significant matters to report to the team captain)

October 31, 2017

To Bobbye Kelly, CPA:

We are providing this letter in connection with the peer review of Smith & Jones, LLP as of the date of this letter and for the year ended June 30, 2017.

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We understand that we are responsible for complying with the rules and regulations of state boards of accountancy and other regulators. We confirm, to the best of our knowledge and belief, that there are no known situations in which Smith & Jones, LLP or its personnel have not complied with the rules and regulations of state board(s) of accountancy or other regulatory bodies,

including applicable firm and individual licensing requirements in each state in which it practices for the year under review.

We have provided a list of all engagements to the team captain with periods ending (report date for financial forecasts or projections and agreed upon procedures) during the year under review, regardless of whether issued as of the date of this letter. This list appropriately identified and included, but was not limited to, all engagements performed under *Government Auditing Standards*, including compliance audits under the Single Audit Act, audits of employee benefit plans, audits performed under FDICIA, audits of carrying broker-dealers and examinations of service organizations [Service Organization Control (SOC) 1 and SOC 2 engagements], as applicable. We understand that failure to properly include engagements subject to the scope of the peer review could be deemed as failure to cooperate. We also understand this may result in termination from the Peer Review Program and, if termination occurs, may result in an investigation of a possible violation by the appropriate regulatory, monitoring and enforcement body.

We have completed and issued the following must-select engagements and, to the best of our knowledge and belief, the peer review team has selected and reviewed at least one of each category:

1. Engagements performed under *Government Auditing Standards*, including compliance audits under the Single Audit Act
2. Audits of employee benefit plans

We have discussed significant issues from reports and communications from regulatory, monitoring and enforcement bodies with the team captain, if applicable. We have also provided the team captain with any other information requested, including communications or summaries of communications from regulatory, monitoring or enforcement bodies relating to allegations or investigations of deficiencies in the conduct of an accounting, audit or attestation engagement performed and reported on by the firm, whether the matter relates to the firm or its personnel, within three years preceding the current peer review year-end. We confirm, to the best of our knowledge and belief, that there are no known restrictions or limitations on the firm's or its personnel's ability to practice public accounting by regulatory, monitoring or enforcement bodies within three years preceding the current peer review year-end.

We understand the intended uses and limitations of the quality control materials we have developed or adopted. We have tailored and augmented the materials as appropriate such that the quality control materials encompass guidance that is sufficient to assist us in conforming with professional standards (including the Statements on Quality Control Standards) applicable to our accounting and auditing practice in all material respects.

Sincerely,

William T. Jones, CPA
Managing Partner

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Peer Review Report with a Peer Review Rating of Pass in a System Review

Report on the Firm's System of Quality Control

October 31, 2017

To the Partners of Smith & Jones, LLP and the Peer Review Committee of the North Carolina Association of CPAs.

We have reviewed the system of quality control for the accounting and auditing practice of Smith & Jones, LLP (the firm) in effect for the year ended June 30, 2017. Our peer review was conducted in accordance with the Standards for Performing and Reporting on Peer Reviews established by the Peer Review Board of the American Institute of Certified Public Accountants (Standards).

A summary of the nature, objectives, scope, limitations of, and the procedures performed in a System Review as described in the Standards may be found at aicpa.org/prsummary. The summary also includes an explanation of how engagements identified as not performed or reported in conformity with applicable professional standards, if any, are evaluated by a peer reviewer to determine a peer review rating.

Firm's Responsibility

The firm is responsible for designing a system of quality control and complying with it to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. The firm is also responsible for evaluating actions to promptly remediate engagements deemed as not performed or reported in conformity with professional standards, when appropriate, and for remediating weaknesses in its system of quality control, if any.

Peer Reviewer's Responsibility

Our responsibility is to express an opinion on the design of the system of quality control and the firm's compliance therewith based on our review.

Required Selections and Considerations

Engagements selected for review included an engagement performed under *Government Auditing Standards*, including a compliance audit under the Single Audit Act, and an audit of an employee benefit plan.

As a part of our peer review, we considered reviews by regulatory entities as communicated by the firm, if applicable, in determining the nature and extent of our procedures.

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Opinion

In our opinion, the system of quality control for the accounting and auditing practice of Smith & Jones, LLP in effect for the year ended June 30, 2017, has been suitably designed and complied with to provide the firm with reasonable assurance of performing and reporting in conformity with

applicable professional standards in all material respects. Firms can receive a rating of pass, pass with deficiency(ies) or fail. XYZ & Co. has received a peer review rating of pass.

Bobbye Kelly & Associates

Scenario 2 (firm performs engagements subject to GAS only, in addition to audits subject to both GAS and the Single Audit Act)

The firm of Smith & Jones, LLP performed an audit of a local government that is performed in accordance with *Government Auditing Standards*. The local government does not expend Federal funds. The firm also audited an employee benefit plan and a not-for-profit entity that is subject to *Government Auditing Standards* and the Single Audit Act. The financial statements of the local government, the employee benefit plan and the not-for-profit entity fell into the firm's peer review year. After consulting Interpretation 63-1, the peer reviewer (Bobbye Kelly, CPA) selected the local government and the employee benefit plan and also decided to review only the Single Audit portion of the audit of the not-for-profit entity. The peer review year end was June 30, 2017 and the exit conference was conducted on October 31, 2017. The peer review report rating was pass. The firm's administering entity is the North Carolina Association of CPAs. Notice that references to Single Audit Act engagements are separate from references to engagements performed under *Government Auditing Standards* as the requirement to select one of each type was met through the selection of engagements from two distinct entities.

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Firm Representation Letter (no significant matters to report to the team captain)

October 31, 2017

To Bobbye Kelly, CPA:

We are providing this letter in connection with the peer review of Smith & Jones, LLP as of the date of this letter and for the year ended June 30, 2017.

We understand that we are responsible for complying with the rules and regulations of state boards of accountancy and other regulators. We confirm, to the best of our knowledge and belief, that there are no known situations in which Smith & Jones, LLP or its personnel have not complied with the rules and regulations of state board(s) of accountancy or other regulatory bodies, including applicable firm and individual licensing requirements in each state in which it practices for the year under review.

We have provided a list of all engagements to the team captain with periods ending (report date for financial forecasts or projections and agreed upon procedures) during the year under review, regardless of whether issued as of the date of this letter. This list appropriately identified and included, but was not limited to, all engagements performed under *Government Auditing Standards*, including compliance audits under the Single Audit Act, audits of employee benefit plans, audits performed under FDICIA, audits of carrying broker-dealers, and examinations of service organizations [Service Organization Control (SOC) 1 and SOC 2 engagements], as applicable. We understand that failure to properly include engagements subject to the scope of the peer review could be deemed as failure to cooperate. We also understand this may result in termination from the Peer Review Program and, if termination occurs, may result in an investigation of a possible violation by the appropriate regulatory, monitoring and enforcement body.

We have completed and issued the following must-select engagements and, to the best of our knowledge and belief, the peer review team has selected and reviewed at least one of each category:

1. Engagements performed under *Government Auditing Standards*
2. Compliance audits under the Single Audit Act
3. Audits of employee benefit plans

We have discussed significant issues from reports and communications from regulatory, monitoring and enforcement bodies with the team captain, if applicable. We have also provided the team captain with any other information requested, including communications or summaries of communications from regulatory, monitoring, or enforcement bodies relating to allegations or investigations of deficiencies in the conduct of an accounting, audit, or attestation engagement performed and reported on by the firm, whether the matter relates to the firm or its personnel, within three years preceding the current peer review year-end. We confirm, to the best of our knowledge and belief, that there are no known restrictions or limitations on the firm's or its personnel's ability to practice public accounting by regulatory, monitoring or enforcement bodies within three years preceding the current peer review year-end.

We understand the intended uses and limitations of the quality control materials we have developed or adopted. We have tailored and augmented the materials as appropriate such that the quality control materials encompass guidance that is sufficient to assist us in conforming with professional standards (including the Statements on Quality Control Standards) applicable to our accounting and auditing practice in all material respects.

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William T. Jones, CPA
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Peer Reviewer's Responsibility

Our responsibility is to express an opinion on the design of the system of quality control and the firm's compliance therewith based on our review.

Required Selections and Considerations

Engagements selected for review included an engagement performed under *Government Auditing Standards*, a compliance audit under the Single Audit Act, and an audit of an employee benefit plan.

As a part of our peer review, we considered reviews by regulatory entities as communicated by the firm, if applicable, in determining the nature and extent of our procedures.

Opinion

In our opinion, the system of quality control for the accounting and auditing practice of Smith & Jones, LLP in effect for the year ended June 30, 2017, has been suitably designed and complied with to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Firms can receive a rating of pass, pass with deficiency(ies) or fail. XYZ & Co. has received a peer review rating of pass.

Bobbye Kelly & Associates

REMINDER: Peer Review Guidance Changes Effective January 2017

During 2016, the PRB approved significant changes to the Peer Review Standards, Interpretations and other related guidance that will become effective for reviews commencing on or after January 1, 2017. These changes impact all phases of a peer review – planning, execution and reporting. Included in the [October 2016](#) Reviewer Alert is a detailed discussion of these changes that peer reviewers are encouraged to read. Additionally, a [new webpage](#) has been created that describes how the changes impact both review teams and firms and where more information can be obtained.

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Not Documented, Not Done

As was noted in the April 2016 Reviewer Alert, AICPA Enhanced Oversight has detected numerous instances of insufficient audit evidence. In fact, over half of all the material non-conformity identified through the Enhanced Oversight program related to this issue.

Reviewers have requested additional guidance regarding the degree of reliance which can be placed on oral explanations in lieu of audit documentation.

AU-C, section 230, Audit Documentation, states:

Oral explanations on their own do not represent sufficient support for the work the auditor performed or conclusions the auditor reached but may be used by the auditor to clarify or explain information contained in the audit documentation.

When performing a peer review, a reviewer may seek an oral explanation if audit documentation exists but clarification is needed. For example, after reviewing the firm's audit working papers, the reviewer may find that a particular conclusion appears inconsistent with the results of the audit team's procedures. In such a situation, the reviewer may seek an oral explanation.

However, if audit documentation does not meet the requirements of AU-C section 230, no amount of oral explanation can serve as a substitute. In such situations, the reviewer should conclude that the firm lacked sufficient support that the audit work was performed.

For example, if a member of an engagement team signs off on an audit program indicating that they performed a substantive test, but no documentation of the results of the audit procedures and the conclusions reached exists, the reviewer should conclude that the firm a) failed to perform the substantive test, and b) failed to document their procedures in accordance with AU-C section 230.

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Recent Inherent Risk Assessment Clarifications to Engagement Checklists

Peer review staff recently became aware that reviewers were struggling to evaluate documentation related to a firm's inherent risk assessment. It was determined that the corresponding engagement checklist questions were causing confusion specifically related to the requirements of AU-C 200 and AU-C 315. In certain cases, reviewers were identifying 'no answers' when third party Quality Control Materials included optional inherent risk assessment tools, but the firm elected to use an alternative approach to document their consideration of inherent risk factors. While such optional tools may assist auditors in performing a risk assessment at the assertion level, a separately documented assessment of inherent risk is not required.

To more clearly align with the guidance contained in the auditing standards, the applicable engagement checklists were clarified to indicate that the auditor may make separate or combined assessments of inherent and control risk. As a result, the corresponding inherent risk question within the engagement checklist was modified to have the reviewer focus on a firm's risk of material misstatement for any relevant account or assertion that may be indicative of an inherent risk assessment set at less than high. A reviewer should consider the following factors when concluding on whether or not there was a reasonable basis for such an assessment:

- Documented discussions among the engagement team, the key elements of their understanding obtained regarding each aspect of the entity and its environment, and any significant decisions reached
- A separately documented inherent risk assessment, if applicable

These clarifications were included in the updates to various engagement checklists including the following:

- PRP section 20400, General Audit Engagement Checklist (June 2016)
- PRP section 20500, Governmental Audit Engagement Checklist (June 2016)
- PRP section 20600, Not-for-Profit Audit Engagement Checklist (June 2016)
- PRP section 20700, Employee Benefit Plan Audit Engagement Checklist (August 2016)

New Peer Reviewer Training Courses

The [2016 AICPA Peer Review Update course](#) is now available for purchase at the AICPA Store. This course is an advanced reviewer training course that covers recent changes to peer review guidance in addition to how recent changes in auditing or accounting standards impact peer review. It is also one of the options that a reviewer can complete in order to maintain the qualifications of a team captain or of a review captain.

As a reminder, team captains or review captains should complete one of the training options listed on the [AICPA website](#) within 12 months prior to the commencement of a review.

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Upcoming Peer Review Webcast

FREE RAB Member Training Webcast – CPE Eligible

December 8, 2016 from 2:00 – 4:00pm ET

This course, designed to provide RAB members an update on various topics related to their roles and responsibilities as RAB members. The course will cover:

- findings from recent RAB observations,
- the changes to the reviewer performance & disagreement guidance,
- considerations needed for nonconforming engagements and
- the effect of other peer review guidance changes on the RAB process.

The webcast, offered free of charge, will allow RAB members to analyze the impact of recent guidance changes including the changes to reviewer performance on the report acceptance process, evaluate responses to nonconforming engagements to ensure their appropriateness and identify the most common RAB observation comments.

To register for the webcast, click [here](#). Or copy and paste the URL in your internet web browser: <http://event.on24.com/r.htm?e=1302549&s=1&k=6297107EFFF6B0D30F68C56A13240BCA&d=letcookie=true>

This webcast will be archived shortly after December 8. You can also [register](#) for the rebroadcast that is being offered on January 10.

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August Reviewer Alert Edit

It was brought to our attention that a bullet in the August Reviewer Alert article *Additional SSARS No. 21 Considerations – Reporting and Engagement Letters* implied that including the city and state where the accountant practices in the letterhead of the accountant's review or compilation report is not in compliance with SSARS No. 21. This is not accurate and was not our intent. Therefore, we have removed this bullet from the list of scenarios that would **NOT** ordinarily result in a nonconforming engagement.

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AICPA Releases Free Resource - Competency Framework: Assurance Services

The [AICPA Competency Framework: Assurance Services](#) is designed to help CPAs understand the knowledge and skills necessary to perform high-quality audit, attestation, review, compilation and preparation engagements. The framework is underpinned by the need for objectivity, integrity and ethical behavior and includes a commitment to continuously acquire new skills and knowledge. The technical competencies are organized into five core skill sets: Client Acceptance; Engagement Planning; Engagement Analysis or Testing; Concluding the Engagement; and Guiding Principles. The Framework then identifies specific skills within each of the above core skill sets. The skills for each core skill set are provided for those at the foundational, intermediate, advanced and expert levels.

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