



EXPOSURE DRAFT

PROPOSED STATEMENT ON AUDITING STANDARDS

AUDITOR INVOLVEMENT WITH EXEMPT OFFERING DOCUMENTS

*(AICPA, Professional Standards, AU-C sec. 945; Amends Statement on Auditing Standards
No. 122 Section 560, Subsequent Events and Subsequently Discovered Facts)*

July 13, 2016

Comments are requested by October 13, 2016

Prepared by the AICPA Auditing Standards Board for comment from persons interested in
auditing and reporting issues.

Comments should be addressed to Sherry Hazel at shazel@aicpa.org.

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Explanatory Memorandum

Introduction

This memorandum provides background to the proposed Statement on Auditing Standards (SAS) *Auditor Involvement With Exempt Offering Documents*. If released as final, this SAS would be codified in AU-C section 945 of *AICPA Professional Standards*.

Background

Certain securities are exempt from registration under the Securities Act of 1933, as amended. These securities remain subject to the antifraud provisions of that act; these provisions prohibit any person from misrepresenting or omitting material facts in an offering or sale of securities. The U.S. SEC cannot directly regulate such offerings, so there is no requirement by the SEC for auditor involvement with exempt offerings. Accordingly, an auditor generally is not required to participate in or undertake any procedures with respect to an exempt offering. Further, entities that issue exempt offerings may include an auditor's report in an offering document without obtaining the auditor's permission as no laws or rules prohibit such an inclusion. Franchise offerings regulated by the Federal Trade Commission (FTC) are similar in that there is no requirement for auditor involvement with such offerings.

The AICPA provided industry-specific auditing guidance regarding an auditor's professional responsibilities when the auditor's report was included in a municipal security offering document (AICPA Audit and Accounting Guides *State and Local Governments* and *Health Care Entities*). The guidance described situations in which an auditor was deemed "involved" with the offering and the procedures to perform in such situations. Some firms require involvement with municipal securities and other exempt offerings as a matter of practice risk management. They typically accomplish this by including a provision in the engagement letter requiring the client to obtain the auditor's permission before using the auditor's report in the offering or disclosure documents.

Prior to the ASB's project to revise its standards for clarity, the guidance on auditor involvement presented in AICPA guides was phrased using "should" and, thus, was interpreted as industry-specific requirements. During the conforming change process to incorporate the clarified standards, the "should" statements were revised or eliminated as the clarified standards do not address what actions constitute "involvement," nor do they define auditor requirements with respect to exempt offerings. To consider the impact of the changes to the guides, the Auditing Standards Board (ASB) developed a task force to address the topic of auditor involvement with exempt offerings.

Effective Date

If adopted and issued as a final standard, the proposed SAS will be effective for exempt offering documents with which the auditor is involved that are initially distributed, circulated, or submitted on or after June 15, 2018. Early application of the SAS, once issued, will be permitted.

Explanation of Proposed SAS

The proposed SAS includes performance requirements when the auditor is involved with an exempt offering document. Exempt offerings are defined as securities exempt from registration under the Securities Act of 1933, as amended, or franchise offerings regulated by the FTC. Involvement is determined by a two-benchmark model:

- The auditor's report on financial statements or the auditor's review report on interim financial information is included or incorporated by reference in an exempt offering document.
- The auditor performs one or more specified activities with respect to the exempt offering document. Specified activities which trigger involvement are included in the proposed SAS.

Performance requirements when involved are generally consistent with the following:

- AU-C section 560, *Subsequent Events and Subsequently Discovered Facts*¹
- AU-C section 720, *Other Information in Documents Containing Audited Financial Statements*

Although an auditor is not required to become involved in an exempt offering document unless the benchmarks defining involvement are met, auditors are not precluded from becoming voluntarily involved with an offering document in other circumstances.

Issues

In drafting the proposed SAS the ASB identified the following issues:

Exempt Offerings

The proposed SAS addresses the auditor's responsibilities when both of the following conditions exist:

- a. The auditor's report on financial statements or the auditor's review report on interim financial information of an entity is included or incorporated by reference in an offering document relating to
 - i. securities exempt from registration under the Securities Act of 1933, as amended or
 - ii. franchise offerings regulated by the Federal Trade Commission.
- b. The auditor is engaged to perform, or otherwise performs, one or more of the activities that trigger involvement (discussed in paragraph 8b of the proposed SAS).

Issue 1

Commenters are asked to provide feedback on the types of offerings included in the scope of the standard, specifically whether franchise offerings should be included in the scope of the proposed SAS.

¹ All AU-C sections referenced in this document can be found in AICPA *Professional Standards*.

Specified Activities That Trigger Involvement

The specified activities that trigger involvement (triggers) establish parameters so as to avoid an auditor unknowingly becoming subject to the requirements of the proposed SAS. The proposed SAS identifies seven triggers in paragraph 8*b* as follows:

- i. Assisting the entity in preparing information included in the offering document
- ii. Reading a draft of the offering document at the entity's request
- iii. Issuing a comfort or similar letter in accordance with AU-C section 920, *Letters for Underwriters and Certain Other Requesting Parties*, or an attestation engagement report in lieu of a comfort or similar letter on information included in the offering document
- iv. Participating in due diligence discussions with underwriters, placement agents, broker-dealers, or other financial intermediaries in connection with an offering document
- v. Issuing an attestation report on information relating to the offering
- vi. Providing written agreement (for example, an inclusion letter) for the use of the auditor's report in the offering document
- vii. Signing a copy of the auditor's report for inclusion in the offering document

The triggers are based on long-standing industry guidance (AICPA Audit and Accounting Guides *State and Local Governments* and *Health Care Entities*) regarding an auditor's professional responsibilities in connection with municipal securities offerings, with some modifications.

Issue 2

Commenters are asked to provide feedback on (a) whether they believe the activities that have been identified should trigger involvement and (b) whether additional activities should be considered as triggers for involvement.

Subsequent Event Procedures

When the auditor is involved with an exempt offering document, the ASB believes the auditor should be required to determine if any material events occurred subsequent to the report date that could undermine the credibility of the audited financial statements or interim financial information and the auditor's report thereon. Some have argued that given the absence of a regulatory requirement for subsequent event procedures, the auditor's decision whether to perform such procedures is a risk management determination. There is also a question as to whether the management of the entity issuing the exempt offering has requirements or responsibilities to evaluate the impact of subsequent events on financial statements included in the offerings. If a preparer has no requirement to evaluate the impact of events occurring subsequent to the issuance of the financial statements, some have argued it would not be appropriate to require the auditor to perform subsequent event procedures relating to the auditor's report on those financial statements.

Issue 3

Commenters are asked to provide their views regarding the proposed requirement for subsequent event procedures to be performed when the auditor is deemed involved with an exempt offering document.

Guide for Respondents

Comments are most helpful when they refer to specific paragraphs, include the reasons for the comments, and, when appropriate, make specific suggestions for any proposed changes to wording. When a respondent agrees with proposals in the exposure draft, it will be helpful for the ASB to be made aware of this view as well.

Written comments on the exposure draft will become part of the public record of the AICPA and will be available for public inspection at the offices of the AICPA after October 13, 2016 for one year. Responses should be sent to Sherry Hazel at shazel@aicpa.org by October 13, 2016.

Respondents are asked, in particular, to respond to the issues described above.

Comment Period

The comment period for this exposure draft ends on October 13, 2016.

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PROPOSED STATEMENT ON AUDITING STANDARDS
AUDITOR INVOLVEMENT WITH EXEMPT OFFERING DOCUMENTS

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Proposed Statement on Auditing Standards, Auditor Involvement With Exempt Offering Documents

Introduction

Scope of This Statement on Auditing Standards

1. This Statement on Auditing Standards (SAS) addresses the auditor's responsibilities when both of the following conditions exist:

- a. The auditor's report on financial statements or the auditor's review report on interim financial information of an entity is included or incorporated by reference in an offering document relating to
 - i. securities exempt from registration under the Securities Act of 1933, as amended (Securities Act of 1933) or
 - ii. franchise offerings regulated by the Federal Trade Commission.

Hereafter, such offerings are referred to as "exempt offerings."

- b. The auditor is engaged to perform, or otherwise performs, one or more of the activities in paragraph 8*b* with respect to the offering document.

In such situations, the auditor is deemed to be involved with the offering document. (Ref: par. A1–A3)

2. Exempt offerings are made pursuant to federal or state securities laws and regulations or pursuant to federal or state franchise laws and regulations, including, in each case, the antifraud provisions thereof. Exempt offerings include, but are not limited to, the following:

- Securities transactions that are exempt from the registration requirements of Section 5 of the Securities Act of 1933, such as private placement offerings, exempt public offerings, and municipal securities offerings
- Offerings of securities issued or backed by governmental, municipal, banking, tax-exempt, or other entities that are exempt from registration under the Securities Act of 1933
- Franchise offerings

Effective Date

3. This SAS is effective for exempt offering documents with which the auditor is involved that are initially distributed, circulated, or submitted on or after June 15, 2018. (Ref: par. A4)

Objective

4. The objective of the auditor when involved with an exempt offering document is to perform procedures specified in this SAS to determine whether the information included in the offering document could undermine the credibility of the financial statements and the auditor's report thereon and respond appropriately.

Definitions

5. For purposes of this SAS, the following terms have the meanings attributed as follows:

Inclusion letter. A letter requested by the entity, addressed to the entity, and signed and dated by the auditor indicating that the auditor agrees to the inclusion of the auditor's report on financial statements (or the auditor's review report on interim financial information) in the offering document. This letter is not considered to be part of the offering document. (Ref: par. A5)

Exempt offering document. The disclosure document that provides financial and nonfinancial information related to the entity issuing the exempt offering (or in the case of a franchise offering, the franchisor) and the offering itself.

Security. *Security* has the meaning as defined in Section 2(a)(1) of the Securities Act of 1933, as amended.

6. References in this SAS to an auditor's report are to be read to encompass an auditor's report on financial statements¹ or an auditor's review report on interim financial information in accordance with AU-C section 930, *Interim Financial Information*.

7. References in the remainder of this SAS to an auditor's report that is *included* in an offering document are to be read to also encompass an auditor's report that is *incorporated by reference* in an offering document.

¹ An auditor's report in accordance with AU-C section 700, *Forming an Opinion and Reporting on Financial Statements*, AU-C section 800, *Special Considerations—Audits of Financial Statements Prepared in Accordance With Special Purpose Frameworks*, or AU-C section 805, *Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts, or Items of a Financial Statement*.

Requirements

Involvement

8. The auditor should apply the requirements of this SAS in connection with an exempt offering when both of the following conditions exist:

- a.* The auditor's report is included in the exempt offering document.
- b.* The auditor is engaged to perform, or otherwise performs, one or more of the following activities with respect to the exempt offering document: (Ref: par. A6)
 - i.* Assisting the entity in preparing information included in the offering document (Ref: par. A7—A8)
 - ii.* Reading a draft of the offering document at the entity's request (Ref: par. A9)
 - iii.* Issuing a comfort or similar letter in accordance with AU-C section 920, *Letters for Underwriters and Certain Other Requesting Parties*, or an attestation engagement report in lieu of a comfort or similar letter on information included in the offering document (Ref: par. A10—A12)
 - iv.* Participating in due diligence discussions with underwriters, placement agents, broker-dealers, or other financial intermediaries in connection with an offering document (Ref: par. A13)
 - v.* Issuing an attestation report on information relating to the offering (Ref: par. A14—A15)
 - vi.* Providing written agreement (for example, an inclusion letter) for the use of the auditor's report in the offering document (Ref: par. A16)
 - vii.* Signing a copy of the auditor's report for inclusion in the offering document (Ref: par. A17)

9. When the auditor is involved with the offering document, the auditor should perform the procedures in paragraphs 10–17 at or shortly before the date of distribution, circulation, or submission of the offering document, and as appropriate upon any subsequent distribution, circulation, or submission of the offering document. (Ref: par. A18)

Other Information Included in the Offering Document

10. When the auditor is involved with the offering document, the auditor should perform the procedures described in AU-C section 720, *Other Information in Documents Containing Audited Financial Statements*, on the offering document.

11. When performing the procedures required by paragraph 10, the auditor should determine that the auditor's name is not being used in a way that indicates that the auditor's responsibility is greater than the auditor intends. (Ref: par. A19—A23)

Subsequent Events Procedures

12. When the auditor is involved with an offering document, the auditor should perform the following procedures described in AU-C section 560, *Subsequent Events and Subsequently Discovered Facts*:²

- a. Procedures designed to identify events occurring between the date of the auditor's report and the date of the distribution, circulation, or submission of the offering document that require adjustment to, or disclosure in, the financial statements. Such procedures should include the following:
 - i. Obtaining an understanding of any procedures that management may have performed to identify such events
 - ii. Inquiring of management and, when appropriate, those charged with governance about whether any such events have occurred that might affect the financial statements
 - iii. Reading minutes, if any, of the meetings of the entity's owners, management, and those charged with governance that have been held after the date of the financial statements and inquiring about matters discussed at any such meetings for which minutes are not yet available
 - iv. Reading the entity's most recent subsequent interim financial statements, if any
- b. Obtain updated written representations from management about the following:
 - i. Whether any information has come to management's attention that would cause management to believe that any of the previous representations should be modified
 - ii. Whether any events have occurred subsequent to the date of the financial statements that would require adjustment to, or disclosure in, those financial statements
 - iii. That minutes of the meetings of shareholders, directors, and committees of directors are complete and authentic records of proceedings at all such meetings held since previous representations were provided (Ref: par. A24—A26)

13. If a predecessor auditor's report on a prior period is included in the offering document but the predecessor auditor did not audit the entity's separate financial statements for the most recent audited period for which the entity's audited financial statements are included in the offering

² Paragraphs .09–.10 of section 560, *Subsequent Events and Subsequently Discovered Facts*.

document, and the predecessor auditor is involved with the offering, then the predecessor auditor should perform the following procedures described in AU-C section 560:³

- a.* Reading the financial statements of the subsequent period to be presented on a comparative basis
- b.* Comparing the prior period financial statements that the predecessor auditor reported on with the financial statements of the subsequent period to be presented on a comparative basis
- c.* Obtaining written representations from management
- d.* Obtaining a representation letter from the successor auditor stating whether the successor auditor's audit revealed any matters that, in the successor auditor's opinion, might have a material effect on, or require disclosure in, the financial statements reported on by the predecessor auditor.

14. When the auditor of an acquired entity is involved with the offering document and *(a)* the acquirer's audited financial statements included in the offering document reflect a period that includes the date of acquisition and *(b)* the auditor is not the continuing auditor of the acquiring entity, the auditor may be unable to perform all of the procedures in paragraph 12 of this SAS. In such circumstances, the auditor should obtain written representations from management and the successor auditor as described in AU-C section 560.⁴

15. If the auditor identifies subsequent events that may require adjustment of, or disclosure in, the audited financial statements or reviewed interim financial information, the auditor should not agree to the inclusion of the auditor's report until the auditor's consideration of the subsequent events has been satisfactorily evaluated in accordance with AU-C section 560.⁵

16. If the auditor becomes aware of subsequently discovered facts, the auditor should not agree to the inclusion of the auditor's report until the auditor's consideration of the subsequently discovered facts, including the effect on the auditor's report, has been satisfactorily evaluated in accordance with AU-C section 560.⁶

17. If management does not revise the financial statements in circumstances in which the auditor believes they need to be revised, in addition to following the requirements in AU-C section 560, the auditor should not agree to the inclusion of the auditor's report in the offering document.⁷

³ Paragraph .19 of AU-C section 560.

⁴ Paragraph .19*c-d* of AU-C section 560.

⁵ Paragraph .11 of AU-C section 560.

⁶ Paragraphs .15–.18 of AU-C section 560.

⁷ Paragraphs .17–.18 of AU-C section 560.

Application and Other Explanatory Material

Scope of This Statement on Auditing Standards (Ref: par. 1)

A1. Securities and franchise offerings may be offered by means other than a registered offering through exemptions to registration afforded under federal or state laws and regulations based on the size and nature of the offering or the issuing entity or franchisor, as applicable. Securities offered through means other than a registration statement under the Securities Act of 1933 and franchise offerings are within the scope of this SAS. Appendix A, “Examples of Exempt Offerings,” provides examples of types of offerings within the scope of this SAS. AU-C section 925, *Filings With the U.S. Securities and Exchange Commission Under the Securities Act of 1933*, addresses the auditor’s responsibilities when financial statements of a nonissuer are included or incorporated by reference in a registration statement under the Securities Act of 1933.

A2. The auditor may include a provision in the terms of the engagement requiring the entity to obtain permission from the auditor before using the auditor’s report in connection with an exempt offering. The existence of such a provision in an engagement letter does not establish involvement unless the auditor is engaged to perform or otherwise performs one or more of the activities in paragraph 8*b* with respect to the offering document. An example provision for an engagement letter may read as follows:

The Entity may wish to include our report on these financial statements in an exempt offering document. The Entity agrees that the aforementioned audit report, or reference to our Firm, will not be included in any such offering document without our prior permission or consent. Any agreement to perform work in connection with an offering document, including an agreement to provide permission or consent, will be a separate engagement.

Clarification in the Offering Document When There Is No Auditor Involvement

A3. The auditor may include in the terms of the engagement a provision that any offering document issued by the entity with which the auditor is not involved, other than as determined by paragraph 8 clearly indicates the auditor is not involved with the contents of such offering document. An example disclosure related to an exempt offering document may read as follows:

[*Name of Firm*], our independent auditor, has not been engaged to perform and has not performed, since the date of its report included herein, any procedures on the financial statements addressed in that report. [*Name of Firm*] also has not performed any procedures relating to this offering document.

Effective Date (Ref: par. 3)

A4. Exempt offerings may have multiple stages, for example distribution of a preliminary offering document and a final offering document. The effective date relates to the initial distribution of an exempt offering on or after June 15, 2018.

Definitions (Ref: par. 5)

A5. An inclusion letter may also be referred to as an *agree-to-include letter*, an *acknowledgement letter*, or an *awareness letter*. Note that *awareness letter* is defined in AU-C section 925 with a different meaning in that context.

Involvement (Ref: par. 8)

A6. Auditors may become aware of an offering through a communication from an entity or through the receipt of a draft offering document from an underwriter, placement agent, broker-dealer, or the entity. Awareness of an offering does not constitute involvement unless the auditor performs one or more of the activities in paragraph 8*b*.

Assisting in Preparing Information (Ref: par. 8*bi*)

A7. Information does not include the audited financial statements, interim financial information covered by the auditor's report, or the required supplementary information or supplementary information other than required supplementary information accompanying those financial statements that the auditor already considered during the audit of the financial statements or review of interim financial information.

A8. Self-review, management participation, and advocacy threats to a covered member's compliance with the AICPA Code of Professional Conduct may exist when a member provides corporate finance consulting services to an entity.⁸ A member may assist the entity in drafting its offering document or memorandum without impairing independence⁹ so long as the member complies with the AICPA Code of Professional Conduct.^{10, 11}

Reading the Offering Document (Ref: par. 8*bii*)

A9. Reading a draft of the offering document encompasses situations in which the auditor receives a request from the entity to read and provide feedback on the offering document. Paragraphs 10–11 discuss the auditor's responsibility to read the offering document as part of required procedures when the auditor is deemed to be involved.

Issuing a Comfort or Similar Letter or an Attestation Report (Ref: par. 8*biii*)

A10. Underwriting agreements between an entity and its underwriters may include a request for the entity's auditor to prepare a comfort letter that will assist the underwriters with their due diligence in connection with the offering. Comfort letters may also be requested by parties other

⁸ The "Independence Rule" (ET sec. 1.200.001) of the AICPA Code of Professional Conduct.

⁹ The "Corporate Finance Consulting" interpretation (ET sec. 1.295.130 02*f*) of the "Nonattest Services" subtopic (ET sec. 1.295) under the "Independence Rule."

¹⁰ The "General Requirements for Performing Nonattest Services" interpretation (ET sec. 1.295.040), of the "Nonattest Services" subtopic under the Independence Rule.

¹¹ The "Corporate Finance Consulting" interpretation (ET 1.295.130.03) of the "Nonattest Services" subtopic under the "Independence Rule" also lists examples of types of corporate finance consulting services that would impair a member's independence in connection with an offering.

than the underwriters. AU-C section 920 provides guidance related to the issuance of comfort letters.

A11. An auditor may issue a comfort letter that provides negative assurance to a requesting party (as defined in AU-C section 920) only if the requesting party provides the written opinion from external legal counsel or the required representation letter described in AU-C section 920.¹² If the requesting party does not provide the required written opinion from external legal counsel or a representation letter, the auditor may issue a modified comfort letter that does not provide negative assurance.¹³

A12. When a comfort letter is requested by a party other than a requesting party as defined in AU-C section 920, the auditor should not provide that party with a comfort letter or similar letter described in AU-C section 920.¹⁴ Instead, the auditor may perform procedures requested by that party and issue a report on agreed-upon procedures.¹⁵

Participating in Due Diligence Discussions (Ref: par. 8biv)

A13. As part of their due diligence process on a specific exempt offering, underwriters and their counsel may ask to interview the entity's auditors either formally or informally.¹⁶ The meetings at which such interviews occur are often referred to as oral due diligence meetings. The interview typically focuses on the audit engagement, the entity's financial statements, and the entity's system of internal controls over financial reporting. Auditors use professional judgment in determining whether to participate in oral due diligence meetings if the underwriter has not provided the representation letter described in paragraph A11 or if external legal counsel has not provided the required written opinion. If the auditor agrees to participate, auditors use professional judgment in determining which questions in an oral due diligence meeting can be addressed.

Issuing Attestation Reports on Information Related to the Offering (Ref: par. 8bv)

A14. During the offering process, management or other involved parties may engage practitioners to perform an attestation engagement related to the offering. For example, in a debt offering, management or its legal advisors may engage a practitioner to perform procedures on the entity's compliance with the revenue coverage requirements on outstanding debt securities or to verify the calculation of escrow account requirements for an advance refunding of debt securities. If the auditor whose report accompanies the financial statements included in the offering document also provides an attestation engagement report relating to that offering, the auditor is deemed to be involved. If the practitioner engaged to perform the attestation engagement is not the financial

¹² Paragraphs .07, .11, and .A92 of AU-C section 920, *Letters for Underwriters and Certain Other Requesting Parties*.

¹³ Paragraph .12 and example Q, "Letter to a Requesting Party That Has Not Provided the Legal Opinion or the Representation Letter Required by Paragraph .11," of exhibit B, "Examples of Comfort Letters," of AU-C section 920.

¹⁴ Paragraph .13 of AU-C section 920.

¹⁵ AT section 201, *Agreed-Upon Procedures Engagements*.

¹⁶ The "Confidential Client Information Rule" (ET sec 1.700.001) of the AICPA Code of Professional Conduct states that the auditor should not disclose any confidential client information without the specific consent of the client.

statement auditor, the practitioner engaged to perform the attestation engagement is not deemed to be involved with the offering document in the manner discussed in this proposed SAS.

A15. An attestation engagement report relating to an exempt offering need not be referred to or included in the offering document to involve the auditor of the financial statements with the offering. Sometimes, the attestation engagement report may only be included in the closing documents for the offering.

Providing a Written Agreement (Ref: par. 8bvi)

A16. When an auditor's report is used in connection with an exempt offering, it is not usually necessary for the auditor to provide any type of written agreement, but some exceptions exist.¹⁷ If the auditor is asked to provide an inclusion letter, the auditor may provide a letter indicating that the auditor agrees to the inclusion of the auditor's report in the offering document. This letter would typically not be included in the offering document. The following example language may be used to indicate that the auditor agrees to inclusion:

We agree to the inclusion in the [*Name of Offering Document*] of our report, dated February 5, 20X3, on our audit of the financial statements of [*Name of Entity*].

Signing an Auditor's Report for Inclusion in the Offering Document (Ref: par. 8bvii)

A17. Signing the auditor's report involves an original manual or electronic signature on the auditor's report, not a reproduction of an auditor's report that was previously manually or electronically signed. For example, providing a copy of the auditor's report with an original manual or electronic signature at the underwriter or bond counsel's request to file with the official closing documents for the offering does not constitute a signing of the auditor's report. Signing an updated auditor's report when, for example, the financial statements are restated does constitute a signing of the auditor's report.

Distribution, Circulation, or Submission (Ref: par. 9)

A18. As discussed in paragraph A4, exempt offerings often have multiple stages. Thus, a single offering could involve multiple applications of this SAS. Requesting management to keep the auditor advised of the progress of the preparation of the offering document proceedings through the final distribution, circulation, or submission of the final offering document is important so that the auditor's consideration of events occurring after the date of the auditor's report up to the distribution, circulation, or submission of the final offering document can be completed.

Other Information Included in the Offering Document (Ref: par. 10—11)

A19. When revision of the other information in the offering document is necessary due to a material inconsistency or a material misstatement of fact that management refuses to correct, AU-C section 720 requires the auditor to notify those charged with governance of the auditor's concerns regarding the other information and take any further appropriate action. With regard to exempt offerings, actions may also include determining whether to withhold the auditor's

¹⁷ Paragraphs 19–20 of exhibit A, "Background," of AU-C section 925, *Filings With the U.S. Securities and Exchange Commission Under the Securities Act of 1933*.

agreement to include the auditor's report. In such cases, the auditor may consider it appropriate to obtain legal advice.

References to the auditor as an "expert"

A20. The term *expert* has a specific statutory meaning under the Securities Act of 1933. Outside the Securities Act of 1933 context, the term *expert* is typically undefined. Accordingly, except as described in paragraph A23, when an entity wishes to make reference to the auditor's role in connection with an exempt offering, the caption to that section of the document would generally be titled "Independent Auditors" (or something similar) rather than "Experts," with no reference to the auditor as an expert anywhere in the offering document.

A21. The following is an example of a typical description of the auditor's role when an entity wishes to make reference to the auditor in an exempt offering:¹⁸

Independent Auditors

The financial statements of [*Name of Entity*] X as of December 31, 20X2 and for the year then ended, included in this offering document, have been audited by [*Name of Firm*], independent auditors, as stated in their report appearing herein.

If the auditor is not involved with the offering document and the terms of the engagement require disclosure of this fact, additional disclosure similar to that illustrated in paragraph A3 may be considered.

A22. If the entity refuses to delete references to the auditor as an "expert," the auditor may consider whether to permit inclusion of the auditor's report, based on the auditor's professional judgment and an evaluation of liabilities the auditor may be assuming. In such situations, the auditor may consider it appropriate to obtain legal advice.

A23. In situations in which the term *expert* is sufficiently defined the auditor may agree to be referred to as an expert outside the context of a registration statement filed under the Securities Act of 1933, as amended. For example, if the term *expert* is defined under applicable state law, the auditor may agree to be named as an expert in an offering document in an intrastate offering. The auditor may also agree to be named as an expert, as that term is used by the Office of Thrift Supervision (OTS), in offering documents that are subject to the jurisdiction of the OTS. An understanding of any auditor liability provisions that may be included in the applicable federal or state statutes is an important consideration.¹⁹

Subsequent Events Procedures (Ref: par. 12)

A24. In addition to the procedures discussed in paragraph 12 of this SAS, the auditor may consider it necessary and appropriate to inquire of or extend previous oral or written inquiries to

¹⁸ Exhibit B, "Illustrative Disclosures and Reports," of AU-C section 925.

¹⁹ Paragraph 18 of exhibit A of AU-C section 925.

the entity's legal counsel concerning litigation, claims, and assessments, as described in AU-C section 501, *Audit Evidence—Specific Considerations for Selected Items*.

A25. An illustrative updating management representation letter is included in AU-C section 580, *Written Representations*.²⁰

Considerations Specific to Governmental Entities

A26. In determining the extent of procedures to perform in connection with a governmental debt offering, the auditor may consider the structure of the government and which component units relate to the debt offering. A component unit not guaranteeing the repayment is ordinarily not a relevant entity to the users of the debt offering. Alternatively, if the debt is offered by a particular component unit, the scope of subsequent event procedures would likely be limited to the applicable component unit responsible for the repayment of the debt. However, if the full set of financial statements for the reporting entity were included, the scope of subsequent event procedures would likely also encompass the primary government.

²⁰ Exhibit C, "Illustrative Updating Management Representation Letter," of AU-C section 580, *Written Representations*.

A27.

Appendix A—Examples of Exempt Offerings (Ref: par. A1)

1. Sections 3 and 4 of the Securities Act of 1933, as amended, specify the classes of securities and classes of securities transactions that are exempt from registration under federal securities laws. Examples include the following:

- a. Municipal securities – Section 3(a)(2)
- b. Intrastate offerings – Section 3(a)(11)
- c. Small issues – Section 3(b)(1)
 - i. Regulation D Rule 504 exemption (“seed capital” exemption)
 - ii. Regulation D Rule 505 exemption
 - iii. Regulation A exemption
- d. Transactions by an entity not involving any public offering (for example, private placements, nonpublic offerings, private sales) –Section 4(a)(2)
 - i. Regulation D Rule 506 offering
 - ii. Resales of securities to Qualified Institutional Buyers (Rule 144A)
- e. Securities sold for employee benefit plans (Rule 701)
- f. Crowdfunding – allows for limited-size offerings to be sold in small amounts to a large number of investors (for example, over the Internet) – Section 4(a)(6)
- g. Private resales of securities – Section 4(a)(7)
- h. Offers and sales of securities outside the United States (Regulation S)
- i. Other classes of securities specifically exempted
 - i. Securities issued by religious, charitable, educational and other nonprofit organizations
 - ii. Securities issued or guaranteed by banks (Note however that issuances of bank securities may be subject to other regulators, for example, the Office of Thrift Supervision.)
 - iii. Miscellaneous other securities such as short-term notes, drafts and bills of exchange, insurance policies, certificates issued by a receiver or trustee in bankruptcy, and interests in a railroad equipment trust

2. Franchise offerings are regulated at the federal and state level. Federal regulation occurs through the Federal Trade Commission under the *Disclosure Requirements and Prohibitions Concerning Franchising* (the FTC rule). The FTC rule requires franchisors to provide a franchise disclosure document (FDD) to each prospective buyer, but does not require FDDs to be filed or

registered with the FTC. At the state level, regulations vary widely. Some states have franchise statutes and regulations that are more stringent than the FTC requirements, and which may require a franchisor to file or register its offering with state franchise authorities.

A28.

Appendix B—Amendment to SAS No. 122 Section 560, *Subsequent Events and Subsequently Discovered Facts*

1. AU-C section 560, *Subsequent Events and Subsequently Discovered Facts*, states that the auditor is not required to perform any audit procedures regarding the financial statements after the date of the auditor's report. However, requirements exist in AU-C section 925, *Filings With the U.S. Securities and Exchange Commission Under the Securities Act of 1933*, and the proposed SAS that would require, in certain circumstances, procedures to be performed after the date of the auditor's report. This proposed amendment highlights, through a footnote, that there may be instances in which the requirements of AU-C section 560 apply after the report date.

(***Boldface italics*** denotes new language. Deleted text is shown in ~~strike~~through.)

[No proposed amendment to paragraphs .01–.11.]

Subsequently Discovered Facts That Become Known to the Auditor Before the Report Release Date

.12 The auditor is not required to perform any audit procedures regarding the financial statements after the date of the auditor's report. However, if a subsequently discovered fact becomes known to the auditor before the report release date,^{fn 3} the auditor should

- a. discuss the matter with management and, when appropriate, those charged with governance.
- b. determine whether the financial statements need revision and, if so, inquire how management intends to address the matter in the financial statements.^{fn 4}

^{fn 3} The term *report release date* is defined in paragraph .06 of section 230, *Audit Documentation*.

^{fn 4} ***There may be instances in which the auditor applies the requirements in this section after the date of the auditor's report as described in AU-C section 925, Filings With the U.S. Securities and Exchange Commission Under the Securities Act of 1933, and AU-C section 945, Auditor Involvement With Exempt Offering Documents.***

[Subsequent footnotes 4–14 renumbered. No further amendments to section 560.]

2. If issued as final, this proposed amendment will be effective for offering documents with which the auditor is involved that are initially distributed, circulated, or submitted on or after June 15, 2018.