



Agenda Item 2A

Proposed SAS

The Auditor's Involvement with Offering Documents Other than Filings With the U.S. Securities and Exchange Commission Under the Securities Act of 1933

Introduction

Scope of This Section (Ref: par. .A1-.A4)

.01

This proposed Statement on Auditing Standards (SAS) addresses the auditor's responsibilities when the auditor's report on financial statements (or the auditor's report on a review of interim financial information) of a nonissuer¹ is included or incorporated by reference in an offering of an investment that is not registered with the U.S. Securities and Exchange Commission (SEC) under the Securities Act of 1933 (offering document), and

- a. the auditor performs one or more of the activities in paragraph .07 with respect to an offering document, or
- b. the terms of the audit engagement require the entity to obtain permission from the auditor before using the auditor's report in connection with an offering of investments or similar undertaking. (Ref: par. .A1 and .A2)

In such situations, the auditor is deemed to be involved with the offering document.

.02.

The scope of this standard contemplates offerings that are made pursuant to federal or state securities or franchise laws and regulations, including the antifraud provisions thereof. They include, but are not limited to:

- Transactions that are exempt from the registration requirements of Section 5 of the Securities Act of 1933, including private placement offerings; exempt public offerings; and municipal securities offerings

¹ AU-C Glossary, *Glossary of Terms*

Exempt Securities
ASB Meeting, January 12-14, 2016

- 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.

Hereafter, such offerings are referred to as “exempt offerings.” (Ref: par. .A4)

Effective Date (Ref: par. .A5)

.03

This section is effective for offering documents with which the auditor is involved that are distributed, circulated, or submitted to potential investors on or after Month Day, 20XX. (Ref: par. .A5)

Objective (Ref: par. .A6 and .A7)

.04

The objective of the auditor, in connection with the inclusion or incorporation by reference of the auditor’s report on financial statements of a nonissuer (or the auditor’s report on a review of interim financial information of a nonissuer) in an offering document with which the auditor is involved, is to perform specified procedures at or shortly before the date of the distribution, circulation, or submission of the offering document to potential investors or a regulator to respond appropriately when the auditor becomes aware that offering documents include information that could undermine the credibility of those financial statements and the auditor’s report (or interim financial information).

Definitions (Ref: par. .A8)

.05

For purposes of this section, the following terms have the meanings attributed as follows:

Inclusion letter. When requested by the client, a letter signed and dated by the auditor to acknowledge the auditor’s awareness that the auditor’s report on financial statements or the auditor’s report on a review of interim financial information is being used in an offering document. This letter is not considered to be part of the offering document. (Ref: par. .A8 and .A18)

Involvement. Situations in which the auditor’s report on financial statements (or the auditor’s report on a review of interim financial information) is included or incorporated by reference in an offering document, and the terms of the audit engagement require the entity to obtain permission from the auditor before using the auditor’s report in connection with an offering of investments or similar undertaking, or the auditor performs one or more of the activities in paragraph .07 with respect to that offering document.

Offering Document. For purposes of this section, an offering of an investment that is not registered with the SEC under the Securities Act of 1933.

.06

References to *includes* or *the inclusion of* in an offering document in this section means *includes* or *incorporates by reference* in an exempt offering.

Requirements

Involvement (Ref: Par. .A9 -.A20)

.07

The auditor should apply the requirements of this section in connection with an offering document that includes the auditor's report on financial statements (or the auditor's report on a review of interim financial information) when the auditor is engaged to or otherwise performs one or more of the following activities with respect to a specific offering document:

- a. Assist the entity in preparing financial information included in the offering document (Ref: par. .A10)
- b. Read a draft of the offering document at the entity's request (Ref: par. .A11)
- c. Issue a letter in accordance with 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. A12-.A14)
- d. Participate in due diligence discussions with underwriters, broker-dealers, or other financial intermediaries in connection with an offering document (Ref: par. .A15)
- e. Issue a report on an attestation engagement relating to the offering document (Ref: par. .A16-.A17)
- f. Provide written agreement for the use of the auditor's report in a specific offering document (Ref: par. .A18)
- g. Provide a revised auditor's report for inclusion in a specific offering document (Ref: par. A19)
- h. Sign a copy of the auditor's report for inclusion in a specific offering document (Ref: par. .A20)

The Offering Document and Other Information (Ref: par. .A21-.A23)

.08

When the auditor is deemed to be involved with the offering document, the auditor should perform the procedures described in section 720, *Other Information in Documents Containing Audited Financial Statements*, on the offering document (including material that is incorporated by reference into the offering document) at or shortly before the date that the offering document is distributed, circulated, or submitted (Ref: par. .A5-.A7).

.09

In connection with the procedures required by paragraph .08, 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.

Subsequent Events Procedures (Ref: par. .A5-.A7 and .A24-.A27)

.10

When the most recent separate financial statements of the entity and the related auditor's report are included in the offering document and the auditor is involved, the auditor should perform the following procedures described in section 560, *Subsequent Events and Subsequently Discovered Facts*, at or shortly before the date that the offering document is distributed, circulated, or submitted (Ref: par. .A5-.A7):²

- a. Audit procedures designed to identify events occurring between the date of the auditor's report and the date of the offering document that require adjustment to, or disclosure in, the financial statements. Such procedures, which take into account the auditor's risk assessment in determining the nature and extent of such audit procedures, should include
 - i. obtaining an understanding of any procedures that management has established to ensure that such events are identified.
 - 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 latest subsequent interim financial statements, if any.
- b. Obtain updated written representations from management at or shortly before the date of the offering document, about whether
 - i. any information has come to management's attention that would cause management to believe that any of the previous representations should be modified.
 - ii. any events have occurred subsequent to the date of the financial statements that would require adjustment to, or disclosure in, those financial statements. (Ref: par. .A27)

.11

When the auditor has audited the most recent period for which separate audited financial statements of the entity are included in the offering document and

- a. the entity has been acquired by another entity,

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

- b. the acquirer's audited financial statements included in the offering document reflect a period that includes the date of acquisition, and
- c. the auditor is a predecessor auditor because the auditor is not the continuing auditor of the entity, and
- d. the predecessor auditor has met one (or more) of the criteria in paragraph .07 and the predecessor auditor's report is included in the offering document

the auditor may be unable to perform all of the procedures in paragraph .10. In such circumstances, the auditor should obtain written representations from management and the successor auditor as described in section 560 at or shortly before the distribution, circulation or submission of the offering document.³

.12

If a predecessor auditor, who becomes involved with an offering document, audited the entity's separate financial statements for a prior period included in the offering document but has not audited 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 document, then the predecessor auditor should perform the following procedures described in section 560 through a date at or shortly before the distribution, circulation or submission of the offering document:⁴

- a. Read the financial statements of the subsequent period to be presented on a comparative basis
- b. Compare 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. Obtain written representations from management at or shortly before the date the offering document is distributed, circulated, or submitted (Ref: par. .A5)
- d. Obtain 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.

.13

If the auditor becomes aware of subsequently discovered facts, the auditor should not agree to the inclusion of his or her report until the auditor's consideration of subsequently discovered facts, including the effect on the auditor's report on the financial statements, has been satisfactorily completed in accordance with section 560.⁵ If management does not revise the audited financial statements in circumstances in which the auditor believes they need to be revised, then the auditor should determine whether to withhold the auditor's permission to include the auditor's report. (Ref: par. .A26)

³ Paragraph .19c-d of section 560.

⁴ Paragraph .19 of section 560.

⁵ Paragraphs .15-.18 of section 560.

Unaudited Annual Financial Statements or Unaudited Interim Financial Information

.14

If the auditor concludes, based on known facts, that unaudited annual financial statements or unaudited interim financial information included in an offering document are not in conformity with the requirements of the applicable financial reporting framework, then the auditor should request that management revise the unaudited annual financial statements or unaudited interim financial information appropriately.

.15

If management does not revise the unaudited annual financial statements or unaudited interim financial information appropriately and

- a. the auditor has reported on a review of the unaudited annual financial statements or unaudited interim financial information,
- b. the auditor's review report is included in the offering document, and
- c. the subsequently discovered facts are such that they would have affected the report had they been known to the auditor at the date of the report,

the auditor should perform the applicable procedures, adapted as necessary, in section 560.⁶

.16

If management does not revise the unaudited annual financial statements or unaudited interim financial information appropriately and

- a. the auditor has not reported on a review of the unaudited annual financial statements or unaudited interim financial information or
- b. the auditor's review report is not included in the offering document,

the auditor should modify the report on the audited financial statements to describe the departure from the requirements of the applicable financial reporting framework contained in the unaudited annual financial statements or unaudited interim financial information, as described in section 930, *Interim Financial Information*.⁷

.17

Additionally, the auditor should determine whether to withhold the auditor's permission to include the auditor's report in the offering document. (Ref: par. .A26)

⁶ Paragraphs .14 and .17–.18 of section 560.

⁷ Paragraph .35 of section 930, *Interim Financial Information*.

Application and Other Explanatory Material

Scope of This Section (Ref: par. .01 and .05)

.A1

Although an auditor is not required to become involved in an offering document except through the performance of procedures noted in par. .07, some auditors 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 offering of investments or similar undertaking. Such a provision is used by the auditor to establish a requirement that the auditor become involved with the entity's offerings (Ref: par. .01) In such situations, the auditor is involved with the offering document. For example, an engagement letter might contain a provision similar to the following:

The Entity may wish to include our report on these financial statements in a registration statement proposed to be filed under the Securities Act of 1933 or in some other securities offering. You agree that the aforementioned audit report, or reference to our Firm, will not be included in any such offering without our prior permission or consent. Any agreement to perform work in connection with an offering, including an agreement to provide permission or consent, will be a separate engagement."

Clarification in the Securities Offering Document When There Is No Auditor Involvement

.A2

If the auditor does not include a provision in the terms of the engagement that would require auditor involvement, the auditor may nevertheless include in the terms of the engagement a requirement that any offering document issued by the entity with which the auditor is not involved clearly indicates the auditor is not involved with the contents of such offering document. Such a disclosure related to a municipal offering document could read as:

"[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 official statement." (Ref: par. .01)

.A3

Securities may be sold through a transaction registered pursuant to the provisions of the Securities Act of 1933 which involves the filing of a registration statement with the SEC. Entities offering such securities are considered to be issuers and, accordingly, are not subject to the standards promulgated by the AICPA Auditing Standards Board. When financial statements of a nonissuer are included or incorporated by reference in a registration statement; section 925 provides guidance on the auditor's responsibilities in connection with such situations.

.A4

Investments may be offered through means other than a registered offering through exemptions afforded under federal and state securities laws based on the size and nature of the offering or the issuing entity. Investments offered through means other than a registration statement under the Securities Act of 1933 are within the scope of this standard and include the following: securities offered through private placements; securities offered by municipal entities; and franchise disclosure documents. Offering materials are referred to by various names (for example, prospectus, offering document, official statement, offering circular, and franchise disclosure statement). (Ref: par. 02)

Effective Date

Distributed, Circulated, or Submitted (Ref: par. .03, .08, and .10)

.A5

Offerings often have multiple stages including a preliminary offering and a final offering. Throughout the process draft offering documents may be distributed, circulated, or submitted to the auditor or others. The requirements of this statement pertain to when the offering document is distributed, circulated, or submitted to potential investors or a regulator.

Objective (Ref: par. .04, .08, and .10)

.A6

As discussed in paragraph .A5, offerings often have multiple stages. Thus, there could be multiple applications of this standard related to a single offering. Involvement with a preliminary offering document establishes involvement with the issuance thus requiring the application of the requirements of this section at subsequent stages of the offering.

.A7

Requesting management to keep the auditor advised of the progress of the offering document proceedings through the closing date is important so that the auditor's consideration of events occurring after the date of the auditor's report up to the date of the offering document, or as close thereto as reasonable and practicable, can be completed by the date of the offering document. In addition to performing the procedures required by this section at or shortly before the date of the offering document, the auditor may also perform some or all of the procedures in this section at or shortly before the closing date.

Definitions (Ref: par. .05)

.A8

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 section 925 with a separate meaning.

Involvement (Ref: par. .07)

.A9

Auditors may become aware of an offering through a communication from a client or through the receipt of a draft offering document from an underwriter, broker-dealer or a client. Awareness of an offering does not constitute involvement unless the auditor performs one or more of the activities in paragraph .07.

Preparing Financial Information (Ref: par. 7a)

.A10

Financial information does not include the annual financial statements or 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 his or her audit of the financial statements.

Reading the Offering Document (Ref: par. .7b)

.A11

Reading a draft of the offering document is meant to entail a request from the client to read and provide feedback on the offering document. Paragraphs .08 and .09 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 Letter in Accordance with Section 920 (Ref: par. .7c)

.A12

Underwriting agreements between an entity and its underwriters⁸ may require the auditor to prepare a comfort letter addressed to the underwriters. Section 920 addresses the auditor's responsibilities when engaged to issue letters to requesting parties in connection with a nonissuer entity's financial statements included in registration statements filed with the SEC under the Securities Act of 1933.⁹

.A13

An auditor may provide a comfort letter to a broker-dealer or other financial intermediary acting as principal or agent in offerings of investments issued or backed by entities exempt from registration under the 1933 Act only if the broker-dealer or other financial intermediary provides the required representation letter described in section 920.¹⁰ Paragraph .A93 Example A-2 of section 920 provides an illustration of a

⁸ Paragraph .07 of section 920, *Letters for Underwriters and Certain Other Requesting Parties*, defines underwriter.

⁹ Paragraph .A93 Example A-2 of section 920 provides an illustration of a comfort letter in a non-1933 Act offering, including the required underwriter representations.

¹⁰ Paragraph .11 of section 920.

comfort letter in a non-Securities Act of 1933 offering, including the required underwriter representations.

.A14

If the required representation letter is not provided by the broker-dealer or other financial intermediary, the auditor should follow the requirements and guidance in section 920.¹¹ When a comfort letter is requested by a party other than the underwriter, broker-dealer, or other financial intermediary, the auditor should not provide that party with a comfort letter or letter described in section 920.¹² Instead, the auditor may provide the party with a report on agreed-upon procedures.¹³

Due Diligence Discussions (Ref: par. .07d)

.A15

As part of their due diligence process on a specific offering, underwriters and their counsel may interview the entity's auditors. Such interviews are often referred to as due diligence meetings. The interview typically focuses on the audit engagement, the entity's financial statements, and their system of internal controls. Auditors use professional judgment in determining which questions in an oral due diligence meeting can be addressed.

Offering-Related Attestation Engagements (Ref: par. .07e)

.A16

During the offering process, management or other involved parties often engage practitioners to provide certain needed information through an attestation engagement. For example, in a debt offering, management or its legal advisors may engage a practitioner to review 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 a debt offering, the auditor is deemed to be involved. If the practitioner engaged to perform the attestation engagement is not the financial 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 section.

.A17

An attestation engagement report relating to an offering exempt from the Securities Act of 1933 need not be referred to or included in the offering document to involve the auditor of the financial statements with

¹¹ Paragraph .12 of section 920.

¹² Paragraph .12 of section 920.

¹³ AT section 201, *Agreed-Upon Procedures Engagements*.

the offering. Sometimes, the attestation engagement report may only be included in the official closing documents for the offering.

Letters Similar to Consents (Ref: par. .07.f)

.A18

When an auditor's report is used in connection with an offering transaction that is not registered under the Securities Act of 1933, it is not usually necessary for the auditor to provide any type of written consent, but some exceptions exist (for example, securities subject to Regulation A and certain state franchise statutes require written consent).¹⁴ If the auditor is asked to provide a written consent then the auditor may provide a letter indicating that the auditor agrees to the inclusion of the auditor's report on financial statements in the offering materials. This letter would typically not be included in the offering materials. The following example language may be used to indicate that the auditor agrees to inclusion:

We agree to the inclusion in the offering circular of our report, dated February 5, 20X3, on our audit of the financial statements of [name of entity].

Revised Auditor's Report (Ref: par. .07.g)

.A19

A revised auditor's report might, for example, eliminate the references made by the auditor in the original report to (a) supplementary information that the auditor reported on in relation to the basic financial statements or (b) the audit and reports required by *Government Auditing Standards*.

Signing an Auditor's Report for Specific Inclusion in an Offering Document

.A20

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 manually or electronically signed. For example, the underwriter or bond counsel may require a copy of the auditor's report with an original manual or electronic signature to file with the official closing documents for the offering.

The Offering Document and Other Information (Ref: par. .08-.09)

References to the Auditor as an Expert

.A21

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 issuer wishes to make reference to the auditor's role in connection with an offering that is

¹⁴ Exhibit A paragraphs .19-.20 of section 920.

not registered under the Securities Act of 1933, 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 document.

.A22

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.¹⁵

Independent Auditors

The financial statements of Entity X as of December 31, 20X2 and for the year then ended, included in this offering circular, have been audited by ABC & Co., 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 .A2 may be considered.

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

There may be situations in which the term *expert* is sufficiently defined such that 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. 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.¹⁶

Subsequent Events Procedures (Ref: par. .10-.13)

.A24

In addition to the procedures discussed in paragraph .10, the auditor may consider it necessary and appropriate to inquire of, or extend previous oral or written inquiries to, the entity's legal counsel concerning litigation, claims, and assessments, as described in section 501, *Audit Evidence—Specific Considerations for Selected Items*.

¹⁵ Exhibit B of section 925.

¹⁶ Paragraph .18 of Exhibit A of section 925.

Considerations Specific to Governmental Entities

.A25

The auditor, in determining the extent of procedures to conduct, may consider the structure of the government offering the debt and which components relate to the debt offering. A component not guaranteeing the repayment is not a relevant entity to the users of the bond 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.

.A26

In making the determination whether to withhold the auditor's agreement to include his or her report, the auditor may consider it appropriate to obtain legal advice. (Ref: par. .13 and .17)

.A27

An illustrative updating management representation letter is included in section 580, *Written Representations*.¹⁷ (Ref: par. .10)

¹⁷ Exhibit C of section 580, *Written Representations*.