



Agenda Item 1

Auditor Involvement with Exempt Offering Documents

Objective of Agenda Item

To approve the proposed AU-C section 945, *Auditor Involvement with Exempt Offering Documents* (AU-C section 945 or proposed SAS), and amendments to other standards as final.

Task Force members are:

- Chris Smith – BDO (Chair)
- Martha Garner – PwC
- Jeffrey Markert – KPMG
- Christine Piché – CliftonLarsonAllen
- Jere Shawver – Baker Tilly
- Kim Tredinnick – Baker Tilly (retired)

Issues for Discussion

Issue I. Scope of the Standard (Types of Offerings Included)

At the January 2017 ASB meeting the Board agreed to table discussion of the scope of this standard until the Task Force could do more outreach and research on issues pertaining to franchise offerings as the nature of such offerings is different than security offerings exempt from registration under the Securities Act of 1933. The Task Force has performed outreach to attorneys representing franchisees and franchisors and has concluded that the inclusion of franchise offerings in the scope of this standard is appropriate. Further, the Task Force substantially revised Appendix A—Examples of Exempt Offerings to the proposed SAS to better articulate those securities within the scope of the standard.

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To assist the ASB in its determination of the scope, the following describes franchise offerings:

- Regulated at the federal level via the Federal Trade Commission (FTC) under the FTC’s Amended Franchise Rule (Rule) 16 CFR Parts 436 and 437, *Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunities; Final Rule*¹
 - Under the FTC Rule, states may impose additional requirements.
- The *exempt offering document* for franchise offerings are made via a franchise disclosure document (FDD).
 - The FDD is updated at least annually to be used to sell franchises.
 - An FDD differs from a municipal offering in which the sale of the security is based on the Official Statement (exempt offering document) which is issued in a “final form” and continuing disclosures are provided outside the Official Statement.
 - **Audited Financial Statements:** FTC Rule requires annual audited financial statements (with a phase-in period) within 120 days of the close fiscal year²
 - **Auditor’s Consent:** Certain states require an auditor’s consent to use the auditor’s report in the FDD
 - North American Securities Administrators Association (NASAA) published a document, “2008 Franchise Registration and Disclosure Guidelines”³ that provides illustrative language for Consent of Accountant

<p>Form F – Consent of Accountant</p> <p style="text-align: center;">CONSENT</p> <p>_____ (Name of Accountant) consents to the use in the Franchise Disclosure Document issued by _____ (name of Franchisor) (“Franchisor”) on <u>issuance date of Franchise Disclosure Document</u>, as it may be amended, of our report dated _____ (date of accountant’s report), relating to the financial statements of Franchisor for the period ending _____.</p>
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- This language differs from paragraph A23 of the proposed SAS. The proposed SAS limits the consent to a specifically dated FDD.

¹ <https://www.ftc.gov/sites/default/files/070330franchiserulefrnotice.pdf>

² Section 436.5(u) Item 21: Financial Statements ([Page 15559 of FTC Rule](#))

³ [2008 Franchise Registration and Disclosure Guidelines](#)

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- Annual updates constitute a new FDD – thus the FDD is either distributed/circulated (in a non-registration state) or submitted (in a registration state) annually.
- Other updates
 - Material changes to the disclosures in the FDD triggers a quarterly update⁴ (for example, change in executives, litigation)
 - Updates can either be amendments to the FDD or an entirely new FDD
- Auditor Involvement – Application of the Proposed SAS
 - Par 8(a): Auditor’s report is included in FDD (Per FTC Rule)
 - Par 8(b): Triggers
 - If franchisor offers franchises in a state requiring an auditor’s consent to use the auditor’s report – Auditor will be involved in the offering.
 - Or, if auditor performs any other triggering activity in 8(b), the auditor is involved.
 - Ongoing Involvement
 - FTC Rule requires audited financial statements to be filed annually. Thus, it is possible that an auditor will be involved perpetually with the FDD.
 - Updates to FDD – will depend on a case by case basis whether triggers to involvement have been met. If FDD is amended (rather than fully revised) involvement is unlikely.

The Task Force believes the nature and process of distributing/circulating an FDD (in a non-registration state) or submitting an FDD (in a registration state) works within the context of this proposed SAS.

Expected ASB Action

Does the ASB agree with the Task Force recommendation that the scope of the standard as proposed (including franchise offerings) is appropriate?

⁴ Section 436.7(b) and 9(c): ([Page 15560 of FTC Rule](#))

Issue II. Subsequent Events

First, the ASB discussed the term *subsequent events* as used in the context of this proposed SAS noting that the time period differs from the term as defined in AU-C Glossary.

AU-C Glossary: Events occurring between the date of the financial statement and the date of the auditor's report.

AU-C 945: Events occurring between the date of the auditor's report and the date of the distribution, circulation, or submission of the exempt offering document that are so significant, the absence of disclosure of which could undermine the credibility of the previously issued financial statements and the auditor's report thereon.

At the January 2017 ASB meeting, it was proposed that the term "subsequent events" be defined within the context of AU-C 945. The Task Force contemplated a proposed definition but raised concerns that redefining the term for purposes of AU-C 945 could cause confusion and also noted that it is not an issue specific to this SAS. AU-C 925, *Filing With the U.S. Securities and Exchange Commission* has a similar construct (requiring subsequent event procedures for a time period after the auditor's report date). Thus, rather than specifically define the term in the AU-C Glossary the Task Force added a parenthetical to paragraph 11 (hereafter, referred to as subsequent events), the first instance the time frame is discussed, to convey how subsequent events is used in the context of this SAS. Another option considered but dismissed was to create a new term (e.g., events subsequent to the date of the auditor's report) to use throughout this SAS. Thus, the Task Force concluded that the identification of the time period intended for subsequent procedures in Paragraph 11 sufficiently conveys the context for the purposes of this SAS.

Second, the Task Force revised the Application Guidance (Paragraph A31) to clarify that the nature of the subsequent event procedures is to identify events that would have caused the auditor to revise the auditor's report rather than consider whether all amounts and disclosures are appropriate as of the offering date. Given the revisions, the Task Force removed the example that a debt offering subsequent to the date of the auditor's report would generally not require revision to the auditor's report. The example was derived from a comment raising concerns that the proposed SAS would create a need for a client to revise financial statement disclosures as GASB has a requirement to disclose certain nonrecognized events, such as issuance of bonds.⁵ The Task Force considered moving the example to a Consideration Specific to Governmental Entities however concluded that the GAAP requirement whether FASB or GASB for subsequent events is defined as of the date the financial statements are issued (or available to be issued). Thus, the Task Force concluded that the guidance in A31, which is framework neutral, is sufficient and would not lead to an automatic revision of financial statements at each offering.

⁵ Paragraph 13 of GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*.

Third, in reviewing the construct of the SAS which now notes procedures as being *derived from* AU-C section 560 (see Paragraph 11), the Task Force revised the application guidance in A32 to refer to all the application guidance and other explanatory material in AU-C section 560 rather than just paragraph A10 of section 560. The Task Force considers the broader reference to the application guidance in section 560 more appropriate than citing the specific guidance to consider inquiring or extending previous oral or written inquiries.

Expected ASB Action

Does the ASB agree with the Task Force recommendation that the time period intended for subsequent events is sufficiently conveyed in the context of the proposed SAS?

Does the ASB agree that the guidance on subsequent events can remain framework neutral?

Does the ASB agree with the broad reference to the application and other explanatory material in Paragraph A32?

Items Presented

Agenda Item 1 – Issues Paper

Agenda Item 1A – Proposed SAS (marked from January 2017 ASB meeting)

Agenda Item 1B – Proposed SAS (marked from Exposure Draft) for reference purpose only

Mr. Smith will refer to the Issues Paper (Item 1) and the proposed SAS (Item 1A) in leading the discussion.