

Agenda Item 3



Consideration of Additional Guidance for SSARs Engagements

Objective of Agenda Item

To obtain ARSC views on proposed additional guidance for preparation, compilation, and review engagements and on other issues that the ARSC may consider appropriate.

Issues for Discussion with ARSC

Issue #1 – Reporting on Consolidating Information

TIS 9170.01, Consolidating Information Presented on the Face of the Financial Statements reads as follows:

Q&A Section 9170

Supplementary Information

.01 Consolidating Information Presented on the Face of the Financial Statements

Inquiry—An entity wants to present consolidating information in order to present the separate financial statements of the components of the consolidated group. Does the auditor’s reporting responsibility change depending on whether the consolidating information is presented on the face of the financial statements in separate columns or whether the consolidating information is shown outside the basic consolidated financial statements?

Reply—An entity may present consolidating information either on the face of the statements or outside the basic financial statements.

When the auditor is engaged to express an opinion only on the consolidated financial statements, and consolidating information is included on the face of the financial statements, such consolidating information would be considered supplementary information, the same as if the information was presented outside the basic financial statements, as long as such information is clearly differentiated from the financial statements because of its nature and how it is presented. For example, when the consolidated financial statements include columns of information about the components of the consolidated group, the balance sheets might be titled “Consolidated Balance Sheet—December 31, 20X1, With Consolidating Information,” and the columns including the consolidating information, might be marked “Consolidating Information.”

Consideration of Additional Guidance for SSARs Engagements
Discussion Memorandum
ARSC Meeting, November 15-17, 2016

When the consolidating information is presented outside the basic financial statements, the consolidating information might be titled “Consolidating Balance Sheets, December 31, 20X1.” If the other information is clearly differentiated from the basic financial statements, such information may be identified as *unaudited* or as *not covered by the auditor’s report*.

When the consolidated financial statements include consolidating information that has not been separately audited, and the auditor is engaged to report on the consolidating information in relation to the basic consolidated financial statements as a whole, the auditor’s report on the consolidating information might read as follows:

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information is presented for purposes of additional analysis rather than to present the financial position, results of operations, and cash flows of the individual companies and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

When the auditor is engaged to express an opinion on both the consolidated financial statements and the separate financial statements of the components presented in consolidating financial statements, the auditor’s reporting responsibilities with respect to the separate financial statements are the same as his or her responsibilities with respect to the consolidated financial statements. In such cases, the consolidating financial statements and accompanying notes should include all the disclosures that would be necessary for presentation in accordance with generally accepted accounting principles of separate financial statements of each component.

While the non-authoritative Technical Practice Aid (TPA) addresses an auditor’s reporting responsibilities with respect to supplementary consolidating information presented on the face of audited financial statements, the guidance can be adapted and applied to supplementary consolidating information presented on the face of financial statements subjected to a compilation or review. The following illustrates how the TPA could be revised to apply to compilation and review engagements:

Inquiry—An entity wants to present supplementary consolidating information in order to present the separate financial statements of the components of the consolidated group.

Consideration of Additional Guidance for SSARs Engagements
Discussion Memorandum
ARSC Meeting, November 15-17, 2016

Does the ~~auditor's~~ accountant's reporting responsibility change depending on whether the consolidating information is presented on the face of the financial statements in separate columns or whether the supplementary consolidating information is shown outside the basic consolidated financial statements?

Reply—No. An entity may present supplementary consolidating information either on the face of the statements or outside the basic financial statements; the accountant's reporting responsibility does not change depending on the placement of the consolidating information.

When the ~~auditor-accountant~~ is engaged to issue a compilation or a review report ~~express an opinion~~ only on the consolidated financial statements, and consolidating information is included on the face of the financial statements, such consolidating information would be considered supplementary information, the same as if the consolidating information was presented outside the basic financial statements, as long as such information is clearly differentiated from the financial statements because of its nature and how it is presented. For example, when the consolidated financial statements include columns of information about the components of the consolidated group, the balance sheets might be titled "Consolidated Balance Sheet—December 31, 20X1, With Supplementary Consolidating Information," and the columns including the supplementary consolidating information, might be marked "Supplementary Consolidating Information." When the supplementary consolidating information is presented outside the basic financial statements, the supplementary consolidating information might be titled "Consolidating Balance Sheets, December 31, 20X1." If the other information is clearly differentiated from the basic financial statements, such information may be identified as ~~unaudited or as not covered by the auditor's~~ accountant's (compilation or review) report.

~~When the consolidated financial statements include consolidating information that has not been separately audited, and the auditor is engaged to report on the consolidating information in relation to the basic consolidated financial statements as a whole, the auditor's report on the consolidating information might read as follows:~~

~~Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information is presented for purposes of additional analysis rather than to present the financial position, results of operations, and cash flows of the individual companies and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures, in accordance with auditing standards generally accepted in the~~

Consideration of Additional Guidance for SSARs Engagements
Discussion Memorandum
ARSC Meeting, November 15-17, 2016

~~United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.~~

~~Paragraph .34 and paragraph .80 of AR-C sections 80 and 90, respectively states that when supplementary information accompanies financial statements and the accountant's compilation or review report thereon, the accountant is required to clearly indicate the degree of responsibility, if any, the accountant is taking with respect to such information in either~~

- ~~a. an other-matter paragraph in the accountant's compilation or review report on the financial statements or~~
- ~~b. a separate report on the supplementary information~~

~~Paragraph .35 of AR-C section 80 provides the requirements when the accountant has performed a compilation engagement with respect to both the financial statements and the supplementary information.~~

~~Paragraph .36 of AR-C section 80 provides the requirements when the accountant has performed a compilation engagement with respect to the financial statements but the supplementary information was not subject to the compilation engagement.~~

~~Paragraph .81 of AR-C section 90 provides the requirements when the accountant has subjected the supplementary information to the review procedures applied in the accountant's review of the basic financial statements.~~

~~Paragraph .82 of AR-C section 90 provides the requirements when the accountant has not subjected supplementary information to the review procedures applied in the accountant's review of the basic financial statements.~~

When the ~~auditor-accountant~~ is engaged to ~~issue a compilation or a review report express an opinion~~ on both the consolidated financial statements and the separate financial statements of the components presented in consolidating financial statements, the ~~auditor's-accountant's~~ reporting responsibilities with respect to the separate financial statements are the same as his or her responsibilities with respect to the consolidated financial statements. In such cases, the consolidating financial statements and accompanying notes should include all the disclosures that would be necessary for presentation in accordance with generally accepted accounting principles of separate financial statements of each component.

An illustration of an accountant's review report when the accountant has been engaged to subject or has subjected supplementary consolidating information presented on the face of the statements to review procedures applied in the accountant's review of the basic financial statements is as follows:

Independent Accountant's Review Report

Consideration of Additional Guidance for SSARSs Engagements
Discussion Memorandum
ARSC Meeting, November 15-17, 2016

[Appropriate Addressee]

I (We) have reviewed the accompanying consolidated financial statements of XYZ Company and subsidiaries, which comprise the consolidated balance sheets as of December 31, 20X2 and 20X1, and the related consolidated statements of income, retained earnings, and cash flows for the years then ended, and the related notes to the financial statements. A review includes primarily applying analytical procedures to management's (owners') financial data and making inquiries of association management (owners). A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole. Accordingly, I (we) do not express such an opinion.

Management's Responsibility for the Financial Statements

Management (Owners) is (are) responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement whether due to fraud or error.

Accountant's Responsibility

My (Our) responsibility is to conduct the review engagements in accordance with Statements on Standards for Accounting and Review Services promulgated by the Accounting and Review Services Committee of the AICPA. Those standards require me (us) to perform procedures to obtain limited assurance as a basis for reporting whether I am (we are) aware of any material modifications that should be made to the consolidated financial statements for them to be in accordance with accounting principles generally accepted in the United States of America. I (We) believe that the results of my (our) procedures provide a reasonable basis for my (our) conclusion.

Accountant's Conclusion

Based on my (our) reviews, I am (we are) not aware of any material modifications that should be made to the accompanying consolidated financial statements in order for them to be in accordance with accounting principles generally accepted in the United States of America.

Supplementary Consolidating Information

The supplementary consolidating information presented in the columns marked "Supplementary Consolidating Information" on the face of the accompanying consolidated financial statements is presented for the purpose of additional analysis and is not a required part of the basic financial statements. The supplementary consolidating information is the responsibility of management (owners) and was derived from, and relates directly to, the underlying accounting and other records used to prepare the consolidated financial statements. The supplementary consolidating information has been subjected to the review procedures applied in my (our) review of the basic consolidated financial statements and, based on my

Consideration of Additional Guidance for SSARs Engagements
Discussion Memorandum
ARSC Meeting, November 15-17, 2016

(our) review, I am (we are) not aware of any material modifications that should be made to the supplementary consolidating information. I (We) have not audited the supplementary consolidating information and, accordingly, do not express an opinion on such information.

[Signature of accounting firm or accountant, as appropriate]

[Accountant's city and state]

[Date of the accountant's review report]

If the ARSC concludes that guidance with respect to reporting when consolidating information is presented on the face of financial statements subjected to a compilation or review, such guidance may be included in:

- The 2017 edition of the AICPA Guide *Preparation, Compilation, and Review Engagements*.
- A new Technical Practice Aid specific to compilation and review engagements.
- As application guidance in AR-C sections 80 and 90.

Action Requested of ARSC

ARSC is asked to consider whether guidance with respect to consolidating information presented on the face of financial statements subjected to a compilation or review is necessary and, if so, in what format such guidance should be presented.

Issue #2 – Initial Review Engagements

A question has been raised with respect to the accountant's performance responsibilities in an initial review engagement (may be the result of the elevation of a prior year compilation engagement).

When performing an initial review engagement, the accountant is required to obtain sufficient appropriate review evidence as to whether the opening balances contain misstatements that may materially affect the current year financial statements. The accountant may obtain sufficient appropriate review evidence as to whether the opening balances contain misstatements that materially affect the current year financial statements by

- Inquiring as to whether the opening balances agree with the prior period closing balances
- Considering whether review evidence obtained during the procedures performed on the current year financial statement provides limited assurance with respect to the opening balances
- Performing other review procedures on the opening balances

Consideration of Additional Guidance for SSARs Engagements
Discussion Memorandum
ARSC Meeting, November 15-17, 2016

While AR-C section 90 could be amended to provide the requirement and guidance, it is proposed that, since paragraph .17 of AR-C section 90 includes the requirement that the accountant design and perform procedures to obtain limited assurance as a basis for reporting whether the accountant is aware of any material modifications that should be made to the financial statements in order for the statements to be in accordance with the applicable financial reporting framework, interpretative guidance could be developed for inclusion in the 2017 edition of the AICPA Guide *Preparation, Compilation, and Review Engagements*.

Action Requested of ARSC

ARSC is asked to consider whether additional guidance with respect to initial review engagements is necessary and, if so, whether it would be appropriate to include such guidance in the 2017 edition of the AICPA Guide *Preparation, Compilation, and Review Engagements*.

Issue #3 – Independence and Preparation Engagements

Because preparation of financial statements is a nonattest service, the accountant is not required to consider whether he or she is independent in order to perform an engagement to prepare financial statements.

Nevertheless, and as a practical matter, it is common for an accountant to prepare financial statements and then subsequently to be engaged to perform a compilation, review, or audit of those same financial statements. Accountants run the risk that their independence may have been impaired due to the performance of the nonattest preparation service and therefore would be precluded from performing an audit or review. The accountant may perform a compilation but would be required to disclose the lack of independence in the accountant's compilation report.

The following was included in the AICPA Guide *Preparation, Compilation, and Review Engagements*:

Independence

3.09 An engagement to prepare financial statements is a nonattest service and does not require a determination about whether the accountant is independent of the entity. However, it is important to note that the performance of nonattest services for attest clients could impair independence. Therefore, if the accountant anticipates being engaged to perform a review or audit engagement for the entity, the accountant will want to take steps necessary to ensure that independence is not impaired as a result of preparing the financial statements. If the accountant anticipates being engaged to perform a compilation engagement for the entity, the accountant may want to take such steps as the accountant can perform the compilation engagement if his or her independence is impaired but would be required to disclose the lack of independence in the accountant's compilation report.

Consideration of Additional Guidance for SSARs Engagements
Discussion Memorandum
ARSC Meeting, November 15-17, 2016

3.10 The “Nonattest Services” subtopic (AICPA, *Professional Standards*, ET sec. 1.295) of the "Independence Rule" (AICPA, *Professional Standards*, ET sec. 1.200.001) addresses the accountant’s considerations with respect to independence when performing nonattest services for attest clients. For example, the accountant may prepare monthly or other interim financial statements and be engaged to perform an audit, review, or compilation engagement with respect to the annual financial statements. The accountant should be aware that the performance of the preparation services may impair independence unless the safeguards described in this subtopic are met.

In addition, the 2016 Preparation, Compilation, and Review Engagements Risk Alert included a summary of the issue.

It has been suggested that additional guidance may be necessary with respect to this issue. Such guidance may include an additional illustrative engagement letter (in either or both the exhibit to AR-C section 70 or the Guide).

Action Requested of ARSC

ARSC is asked to consider whether additional guidance with respect to independence and preparation engagements is necessary and, if so, what that guidance may entail.

Open Discussion of Practice Issues

The ARSC will have an open discussion as to whether any other practice issues exist that would require the development of authoritative or non-authoritative guidance.

Agenda Items Presented:

None