



Agenda Item 7

Discussion Memo: Proposed Clarified Attestation Standards

Objectives of Agenda Item 7

To vote to ballot for final issuance the July 21-23, 2015 drafts of chapters 1-4 of the July 24, 2013 exposure draft *Attestation Standards: Clarification and Recodification* (July 2013 ED) and chapters 5-7 of the January 28, 2014 exposure draft *Subject-Matter Specific Attestation Standards: Clarification and Recodification* (January 2014 ED), as well as the preface to the attestation standards

(Actual issuance of the chapters will not occur until all of the chapters are finalized, at which time they will be issued as a single Statement on Standards for Attestation Engagements.)

Background

In clarifying the attestation standards, the ASB began by clarifying the general attestation standards, which provide a framework for performing and reporting on examination, review, and agreed-upon procedures engagements. The requirements and application guidance in chapter 1, "Concepts Common to All Attestation Engagements," of the proposed clarified attestation standards are applicable to any attestation engagement. Examination, review, and agreed-upon procedures engagements are addressed in separate chapters (chapter 2, "Examination Engagements;" chapter 3, "Review Engagements;" and chapter 4, "Agreed-Upon Procedures Engagements"). These chapters build on the common concepts chapter and include performance and reporting requirements and application guidance tailored to the specific type of engagement. The subject-matter specific chapters (chapters 5-7) build on chapters 1-4.

The term *chapters* rather than *sections* is used in the ED; however, ultimately the clarified chapters will be codified in AICPA *Professional Standards*, and will be referred to as AT sections.

The ASB discussed revisions to the July 2013 ED at its October 2014, January 2015, and May 2015 meetings and discussed revisions to the January 2014 ED at its January 2015 and May 2015 meetings.

The draft Statement on Standards for Attestation Engagements (SSAE) was revised to reflect comments made at the May, 2015 ASB meeting and the resulting draft was sent to the ASB members for review and fatal flaw comments on June 10, 2015. The accompanying draft reflects the comments received from that process and is marked to show changes *from the draft of the SSAE sent to the ASB on June 10*.

The most recent revisions reflect the correction of drafting errors, elimination of inconsistencies, and minor editorial changes. These revisions are not considered to be substantive.

The discussion is expected to focus on any ASB concerns about the most recent revisions, though members are always free to bring up other issues. In addition, the ASB is being asked to consider the matters described below.

1. Pro Forma Financial Information

The discussion at the May 2015 ASB meeting explored differences between chapter 6, "Reporting on Pro Forma Financial Information," of the draft (which addresses examinations and reviews of pro forma financial information) and paragraphs 52-53 of AU-C section 920 (which addresses the issuance of comfort letters on pro forma financial information), as they relate to

- the practitioner's/auditor's required understanding of the accounting and financial reporting practices of the constituent parts of a business combination for which pro forma financial information has been prepared, and
- which constituent entities' historical financial statements have to be audited or reviewed as a condition for examining or reviewing the pro forma financial information.

After the meeting, ASB members attempted to determine current practice for these engagements through discussions with various individuals who frequently perform these engagements. The results of this effort were presented to the Audit Issues Task Force (AITF) at its July 8, 2015 meeting.

The AITF concluded that for the purposes of the clarified attestation standards, chapter 6 should reflect the guidance in the extant standards (AT section 401, *Reporting on Pro Forma Financial Information*), which is the same as the guidance included in chapter 6 of the January 2014 ED. A separate effort will be undertaken to determine whether the requirements in AU-C section 920 accurately reflect current practice and whether changes need to be made to that section and, if necessary, to chapter 6 of the clarified attestation standards.

Agenda item 7H reflects the AITF's view.

2. Criteria

The June 2015 draft of the proposed SSAE uses the terms "identified criteria," "applicable criteria," and "criteria" interchangeably. Usage varies even in consecutive paragraphs. The July 2015 draft adopts a convention in which the adjectives are eliminated. The term defined in chapter 1 is "criteria" and the draft now uses that term consistently, unless the context requires an adjective for clarity.

3. Incorporation of AT Section 9101.72 in Chapter 2

A member of the ASB's Service Organizations Task Force suggested incorporating the substance of interpretation No. 8, "Including a Description of Tests of Controls or Other Procedures, and the Results Thereof, in an Examination Report," of AT section 101, *Attest*

Engagements, in chapter 2. That interpretation discusses whether a description of tests performed by the practitioner in an examination engagement and the results of those tests may be included in a separate section of the examination report—similar to the description of tests and results in an engagement performed under AT section 801, *Reporting on Controls at a Service Organization*.

The issue is primarily editorial, rather than substantive. The Service Organizations Task Force representative understood, when making the suggestion, that this guidance is unnecessary for engagements performed under proposed chapter 8, “An Examination of a Service Organization’s Controls Relevant to User Entities’ Internal Control Over Financial Reporting,” of the clarified attestation standards because chapter 8 establishes the requirement for a service auditors’ description of tests and results, even though chapter 2 is silent on this matter.

Further, because interpretations and application guidance have equivalent authority it makes no practical difference whether the guidance is located in the standard as application guidance or in an interpretation for services other than SOC 1 engagements. The member of the Service Organizations Task Force who raised this issue was concerned about the availability of the guidance in Interpretation No. 8 for practitioners performing other attestation engagements, such as those performed under the AICPA guide *Reporting on Controls at a Service Organization Relevant to Security, Availability, Processing Integrity, Confidentiality and Privacy*, which results in a report that includes a description of tests performed and results.

The attestation clarification plan envisions that the extant attestation interpretations will be retained in the clarified attestation standards to the extent they are still relevant, although some will require editing given revisions to the standards and the clarity drafting conventions. The guidance will be retained whether it is moved into chapter 2 or presented in an interpretation. Nonetheless, it might improve access to the guidance to include it as an application paragraph in chapter 2.

The following paragraph, which could be placed following paragraph 2.A80 of chapter 2, would address this matter. It is based on the guidance in paragraph 72 of Interpretation No. 8 (AT section 9101.72), edited to broaden the guidance beyond merely internal control, eliminate redundancies, and conform to clarity drafting conventions.

2.A81 As part of the report’s description of the nature of an examination engagement, the practitioner may be requested to provide a description of procedures performed and the results thereof. In determining whether to include such a description in the practitioner’s examination report, the practitioner may consider the following factors:

- Whether such a description is unlikely to overshadow the practitioner’s overall opinion or cause report users to misunderstand the opinion
- Whether the parties making the request have an appropriate business need or reasonable basis for requesting the information (for example, the specified parties are required to maintain and monitor controls that either encompass or are dependent on controls that are the subject of an examination and, therefore, need information about the tests of controls to enable them to have a basis for concluding that they have met the requirements applicable to them)
- Whether the specified parties have an understanding of the nature and subject matter of the engagement and experience in using the information in such reports

- Whether the practitioner's procedures performed directly relate to the subject matter of the engagement.

The addition of procedures performed, and the results thereof, in a separate section of an examination report may increase the potential for the report to be misunderstood when taken out of the context of the knowledge of the requesting parties. This potential for an increase in the risk of misunderstanding may lead the practitioner to add a restricted-use paragraph to the examination report. (Ref: par. 2.62g)

Question for the ASB

Should this paragraph be added to chapter 2 or should the guidance be left in the interpretation?

4. Nonindependence in AUP Engagements

Paragraph 1.24 of chapter 1 of the proposed attestation standards indicates that a practitioner must be independent to perform an attestation engagement, unless required by law or regulation to accept the engagement and report on it. It follows that in the case of such a law or regulation the practitioner does not have to be independent.

In the case of such nonindependence in an examination engagement, chapter 2 directs the practitioner to disclaim an opinion. An earlier draft of chapter 3 proposed guidance related to the effect of such a law or regulation on review engagements, but the ASB deleted it because responses to inquiries indicated that such laws and regulations probably do not exist for review engagements and thus it would be unnecessary to discuss this subject or introduce the concept of a disclaimer in a review engagement.

Although review engagements subject to this provision have not been identified, further discussions indicate that agreed-upon procedures (AUP) engagements might be affected. The draft provides no guidance on how to address the lack of independence when law or regulation requires performance of an AUP engagement. Because AUP reports already disclaim an opinion or conclusion on the subject matter, the lack of independence could be communicated through the addition of a notification in the report, similar to that included in compilation reports. In that case, the following paragraph could be added to chapter 4, preceding paragraph 4.9, (equivalent to the placement in chapter 2) as a precondition for engagement performance.

4.9 Chapter 1 indicates that a practitioner must be independent when performing an attestation engagement in accordance with the attestation standards unless the practitioner is required by law or regulation to accept the engagement and report on the subject matter or assertion.^[1] When the practitioner is not independent but is required by law or regulation to accept an agreed-upon procedures engagement and report on the subject matter or assertion, the practitioner's report should specifically state that the practitioner is not independent. The practitioner is neither required to provide, nor precluded from providing, the reasons for the lack of independence; however, if the practitioner chooses to provide the reasons for the lack of independence, the practitioner should include all the reasons therefor.

^[1] Paragraph 1.24 of chapter 1, "Concepts Common to All Attestation Engagements."

In this situation the report would provide the findings but would indicate the lack of independence. Apparently this would be consistent with practice for AUP engagements performed under the Yellow Book.

Question for the ASB

Should such a paragraph be added to the draft or should the draft continue to be silent on the issue?

5. Combining Limited-Use and General-Use Reports

Chapters 2, 3, and 4 contain application guidance on combining limited-use and general-use reports. Although these chapters do not establish a requirement, they result in different outcomes. Chapter 2 and 3 explicitly state that the use of the general-use report is not affected by the restricted-use report. Chapter 4 suggests restricting the use of the general-use report. The two paragraphs are reproduced below.

The relevant paragraphs are (bold face added):

Chapter 2 (Chapter 3 contains similar guidance)	Chapter 4
<p>2.A91 A practitioner may also issue a single combined report that includes (a) reports that are required by paragraph Error! Reference source not found. to include an alert that restricts their use, and (b) reports that are for general use. If these two types of reports are clearly differentiated within the combined report, such as through the use of appropriate headings, the alert that restricts the use of the practitioner’s report may be limited to the report required by paragraph Error! Reference source not found. to include such an alert. In such circumstances, the use of the general use report is not affected. (Ref: par. Error! Reference source not found.)</p>	<p>4.A1 A practitioner may issue a single combined report that includes (a) reports on subject matter or presentations that require a restriction on use to specified parties and (b) reports on subject matter or presentations that ordinarily do not require such a restriction. The use of such a single combined report may be restricted to the specified parties. In some instances, a separate restricted-use report may be included in a document that also contains a general-use report. The inclusion of a separate restricted-use report in a document that contains a general-use report does not affect the intended use of either report. The restricted-use report remains restricted as to use, and the general-use report continues to be for general use. (Ref: par. Error! Reference source not found.)</p>

Question for the ASB

Should the guidance in chapter 4 be amended to delete the notion of restricting the use of the combined report or should the nonmandatory suggestion in chapter 4 be retained?

Agenda Materials

The agenda materials for the discussion of the clarified attestation standards are the following: (All of the drafts are marked from the drafts sent to the ASB on June 10, 2015 for review and fatal flaw comments.)

Item 7A: “Preface to the Attestation Standards”

- Item 7B: Chapter 1, "Concepts Common to All Attestation Engagements"
- Item 7C: Chapter 2 "Examination Engagements"
- Item 7D: Chapter 3 "Review Engagements"
- Item 7E: Chapter 4 "Agreed-Upon Procedures Engagements"
- Item 7F: Chapter 5, "Financial Forecasts and Projections," which was renamed "Prospective Financial Information" at the January 2015 ASB meeting (clarifies AT section 301)
- Item 7G: Chapter 6, "Reporting on Pro Forma Financial Information," (clarifies AT section 401)
- Item 7H: Chapter 7, "Compliance Attestation," (clarifies AT section 601)

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