



Agenda Item 3

Auditor Involvement with Exempt Offering Documents

Objective of Agenda Item

To discuss comments received in response to proposed AU-C section 945, *Auditor Involvement with Exempt Offering Documents* (AU-C section 945 or proposed SAS), and amendments to other standards (Exposure Draft).

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

General

In total, 20 comment letters were received in response to the Exposure Draft.¹ All but one respondent were supportive of the Auditing Standards Board's (ASB or Board) proposal to create AU-C section 945 to include performance requirements when the auditor is involved with an exempt offering document. One respondent (PBTk) suggested the concept of association be restored to professional standards and did not support the broader concept of involvement as proposed in the ED. (**Comment 1**)

Given the overwhelming support, the Task Force believes its charge is still valid. The remainder of the document presents issues raised by various respondents that the Task Force believes merit further discussion by the Board.

Note: For Board member's reference, when the paper cites a comment received, the specific comment number is noted as (**Comment x**). The number corresponds to the comment number in the reference material - **Agenda Item 3C: Analysis of Comments Received**.

Issues for Discussion

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

In issuing the Exposure Draft, the ASB requested feedback on whether 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.

Those that responded to Issue 1 agreed that the scope of the proposed SAS, including franchise offerings, was appropriate.

However, one of the Task Force members has raised concerns regarding the application of this standard to franchise offerings as the nature of these offerings differs from security offerings exempt from registration under the Securities Act of 1933. The *exempt offering document* for franchise offerings are made via a franchise disclosure document (FDD). The understanding of the Task Force is that the FDD is updated at least annually and continues to be used as an offering document to sell franchises. This differs from, for example, 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. Accordingly, the Task Force has concerns about the potential ongoing involvement of auditors with franchise offerings. For example, one of the periodic updates to an FDD includes annual financial statements and the Task Force needs to better understand the nature of the requirement to determine if such an update would be considered a distribution, circulation, or submission of the exempt offering document triggering requirements of the auditor.

The Task Force proposes tabling the discussion of the scope of this standard until it can do more outreach and research on issues pertaining to franchise offerings, unless information comes to the attention of the Task Force prior to this meeting that could provide resolution.

Input Sought from ASB:

1. Does the ASB agree with the Task Force recommendation that the scope of the standard be tabled until the May 2017 meeting to allow the Task Force to do more outreach and research on the topic?

Issue II. Triggers to Involvement

In issuing the Exposure Draft, the ASB requested feedback on (a) whether respondents believed the activities that have been identified should trigger involvement and (b) whether additional activities should be considered as triggers for involvement.

A majority of respondents supported the triggers proposed as both appropriate and complete to trigger involvement. There were two respondents who suggested modifications to proposed triggers:

- PBTk suggested that the only necessary trigger is signing a report for inclusion based upon their feedback that the standards bring the definition of association back into the standards. **(Comment 33)**
- Commonwealth of Virginia, Auditor of Public Accounts recommended that item 8(b)vi (providing written agreement for the use of the auditor's report in the offering document) be removed. The rationale was that the condition provided does not involve the same level of participation by the auditor as the other conditions listed and, in government audit offices, audit reports are generally public documents available to anyone. **(Comment 36)**

While the majority of respondents did support the triggers, two particular triggering activities garnered a great deal of comments which are addressed in Issues IV and V. Thus, the Task Force believes the triggers are generally appropriate and will make necessary modifications based on the outcome of the discussion of Issues IV and V.

One respondent (Deloitte), citing recent actions from the U.S. Securities Exchange Commission, suggested the proposed SAS recommend involvement even if a triggering event is not performed. **(Comments 6, 40, 117)** The Task Force agreed to remain silent in both the requirements and application sections on such a suggestion as the Task Force feels strongly that triggers should be well defined. Firms may require their clients or former clients to involve them in exempt offerings, regardless of performing triggering activities, which the Task Force believes is sufficient.

Input Sought from ASB:

2. Does the ASB agree with the Task Force recommendation that the seven proposed triggers remain appropriate (subject to the discussion of Issues IV and V)?
3. Does the ASB agree with the Task Force that the SAS omit any requirement for the auditor to consider performing the procedures in the absence of triggering activities?

Issue III. Subsequent Event Procedures

In issuing the Exposure Draft, the ASB requested respondents 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.

The majority of respondents agreed with the proposed requirements for subsequent event procedures to be performed when the auditor is deemed involved with an exempt offering document. However the following respondents had stronger views in opposition/conflict:

- Office of the Auditor General - Michigan opposed the subsequent event procedures, considering the proposed requirement as overly burdensome on the auditor as the entity issuing the exempt offering has no requirement to evaluate the impact of events occurring subsequent to the issuance of their financial statements. **(Comment 57)**

Given the majority of respondents supported the requirement, no proposed changes.

- Moss Adams expressed concern that certain events triggering involvement do not necessarily warrant the extent of subsequent events procedures included in the proposed SAS. For example, they questioned whether assisting the entity in preparing information that is contained in the offering document necessitates performance of the proposed subsequent event procedures [par. 8(b)i]. The respondent recommended the ASB further consider whether subsequent event procedures are appropriate for all of the proposed triggering activities, particularly those proposed in paragraph 8(b)i. (**Comment 64**)

The Task Force believes given the objective of the SAS, subsequent event procedures are appropriate for all triggering events. No proposed changes.

- PCPS raised concerns that a provision by the Governmental Accounting Standards Board (GASB) requires disclosure of certain nonrecognized events, such as issuance of bonds, would create a need for a client to revise financial statement disclosures, and thus the auditor revising its report for the inclusion of this note disclosure. (**Comment 56**)

The Task Force noted that the GASB identifies the time period to consider as between financial statement date and date of issuance. The inclusion of financial statements in an offering does not in itself constitute a reissuance, thus this Task Force did not have the same concerns as PCPS. However, paragraph 12 includes edits to focus on the potential need to revise the auditor's report rather than adjustment or disclosure in the financial statements and application guidance was added to A23X.

Input Sought from ASB:

4. Does the ASB agree with the Task Force recommendation that the subsequent event procedures are appropriate when involved with an exempt offering document regardless of the triggering activity?

IV. Trigger 8(b)vii - Signing a Copy of the Auditor's Report for Inclusion in the Offering Document

Numerous respondents (Grant Thornton, NSAA, EY, PwC, Deloitte, and VSCPA) requested clarification on what "signing a copy of the auditor's report" is meant to entail. (**Comments 107, 108, 109, 110, 111, 112, 115, 116**) The Board discussed this issue in May 2016 and the guidance in the application guidance was revised to clarify that signing a report when the financial statements are restated constitutes involvement. However, respondents requested further clarification.

The Task Force discussed various scenarios of what could be considered "signing" a report and proposes the following as it pertains to a triggering activity:

Exempt Securities
ASB Meeting, January 9-12, 2017

- Scenarios that DO constitute signing the auditor's report:
 1. Signing a revised auditor's report: Providing an updated report as a result of revision to or restatement of financial statements *or* the auditor performs significant additional procedures in accordance with AU-C 585, *Considerations of Omitted Procedures*.

- Scenarios that DO NOT constitute signing the auditor's report:
 1. Providing a copy of a previously signed report: Providing a copy of a previously signed auditor's report, regardless of whether a reproduction of the original report or a newly signed report. This example assumes the financial statements remain as they existed at the time the auditor's report was first issued.
 2. Providing a 'short-form' report: Revising the originally issued report to eliminate the references made by the auditor in the original report required by *Government Auditing Standards*, issued by the Comptroller General of the United States.
 3. Basic statements vs. special presentation based on request: Revising the originally issued report to eliminate the references made by the auditor in the original report to supplementary information that the auditor reported on in relation to the basic financial statements. For example, when a previously issued auditor's report has already been provided on the comprehensive annual financial statements, (the auditor's report on the comprehensive financial statements may have included additional paragraphs pertaining to, for example, the combining schedules and other statistical information).

A few respondents (EY, PBTK, and PCPS) questioned whether there is a distinction between revised and restated financial statements and what is meant by reissuance. The Task Force believes that whether the financial statements are revised or restated, the auditor would have to consider those changes and potentially revise the auditor's report. The broader concept of what constitutes revision, restatement, or reissuance is a matter for the Board's consideration that, the Task Force believes, would go beyond this particular standard. (**Comments 109, 113, and 114**)

The Task Force believes that providing a report when the basic financial statements are unchanged from the original issuance of the report should not be a triggering activity. Issuing such a report is within the scope of the original audit and not a triggering activity. Further, given the ability for an auditor to provide multiple copies and versions of an auditor's report upon issuance, providing a report later at the client's request did not raise to the level of a triggering activity. The Task Force also believes that performing additional audit procedures would also trigger involvement.

Input Sought from ASB:

5. Does the ASB agree with the Task Force recommendation that the notion of signing a report as a trigger occurs when the basic financial statements change from the original issuance of the report or when the auditor performs significant additional procedures?

V. Trigger 8(b)ii – Reading a Draft of the Offering Document at the Entity’s Request

A number of respondents commented on the wording of the trigger “reading a draft of the offering document at the entity’s request.” The Task Force considered the following and resolved to make no changes.

- Moss Adams noted that proposed SAS appears to attempt to draw a line between when an entity requests the auditor perform certain activities and when the auditor performs those activities anyway suggested the proposed standard address awareness to reading a draft. In certain situations, the auditor may receive such a request from the entity but decline to provide the requested feedback, perhaps in order to remain outside the scope of the proposed SAS if there were no other triggers. The auditor may nevertheless choose to read the offering document of their own accord in order to comply with the requirements of AU-C 720, *Other Information in Documents Containing Audited Financial Statements*. **(Comment 86)**

The Task Force believes that the spirit of the requirement would resolve the situation described – if requested and the auditor reads the document the auditor would be involved. Thus, no revisions were made.

- NSAA, Virginia, Michigan, and VSCPA all suggested that the trigger be expanded to include feedback on the document as they believe solely reading the document is not a trigger itself. **(Comments 87, 88, 89, 91)**

The Task Force does not consider providing feedback a necessary component of the trigger. In situations where no inconsistencies are noted, there would be no requirement under AU-C 720 to provide feedback. Thus, no revisions were made.

- EY suggested even if not requested by client involvement should occur. **(Comment 90)**

The Task Force would consider the auditor’s choice to read an exempt offering document as awareness, not an acknowledgement of the offering which is how the triggers are structured. Thus, no revisions were made.

Input Sought from ASB:

6. Does the ASB agree with the Task Force recommendation that the matters raised do not require revision to the trigger?

Items Presented

Agenda Item 3 – Issues Paper

Agenda Item 3A – Proposed SAS (marked from Exposure Draft)

Agenda Item 3B – Proposed SAS (clean)

Agenda Item 3C – Analysis of Comments Received (for reference only)

Mr. Smith will refer to the Issues Paper (Item 3) and the proposed SAS (Item 3A) in leading the discussion.

ⁱ To access the comment letters, please follow this link:

<http://www.aicpa.org/research/exposedrafts/accountingandauditing/pages/loc-on-ed-of-proposed-sas-auditor-involvement-with-exempt-offering-documents.aspx>