



Agenda Item 2

Discussion Memo

Proposed Chapter 8, “Reporting on an Examination of Controls at a Service Organization Relevant to User Entities’ Internal Control Over Financial Reporting” of the Proposed Clarified Attestation Standards (Clarified AT 801)

Objectives

- To obtain confirmation from the ASB that the Service Organizations Task Force (task force) has adequately addressed the ASB’s comments on chapter 8. (At its May and July 2015 meetings, the ASB provided comments on revised drafts of the September 18, 2014 exposure draft *Reporting on an Examination of Controls at a Service Organization Relevant to User Entities’ Internal Control Over Financial Reporting: Clarification and Recodification*. The ASB also provided feedback on a pre-meeting draft dated August 20 2015, marked to show how the task force planned to address the ASB’s July 21-23, 2015 comments.)
- To vote to ballot chapter 8 for final issuance.

Background

AT section 801, *Reporting on Controls at a Service Organization*, was originally issued in April 2010 as Statement on Standards for Attestation Engagements (SSAE) No. 16. SSAE No. 16 represents a convergence with International Standard on Assurance Engagements (ISAE) 3402, *Assurance Reports on Controls at a Service Organization*. On September 18, 2014, the ASB issued an exposure draft entitled *Reporting on an Examination of Controls at a Service Organization Relevant to User Entities’ Internal Control Over Financial Reporting: Clarification and Recodification* (chapter 8 of the proposed clarified attestation standards). The ASB is revising AT section 801 to

- align it with the proposed structure of the clarified attestation standards presented in the July 24, 2013 exposure draft *Attestation Standards: Clarification and Recodification* (July 2013 ED)
- incorporate in chapter 8 certain application guidance included in the May 2013 edition of the AICPA guide *Service Organizations: Reporting on Controls at a Service Organization Relevant to User Entities’ Internal Control Over Financial Reporting* (guide)
- address issues encountered in practice.

Chapter 8 of the proposed clarified attestation standards builds on the requirements and application guidance in chapter 1, “Concepts Common to All Attestation Engagements,” and chapter 2, “Examination Engagements,” of the July 2013 ED to provide performance and reporting requirements and application guidance tailored to a service auditor’s engagement. Based on the proposed new structure of the clarified attestation standards, chapter 8 would not

repeat requirements and guidance included in chapters 1-2, unless there is a need to tailor the requirements and guidance in those chapters to a specific subject matter. (In some cases, a reference to a requirement in another chapter is inserted in the “requirements column” of proposed chapter 8 to provide a footing for an application paragraph.) However, as directed by the ASB at its July/August 2013 meeting, the paragraphs in the subject-matter specific chapters that identify the required elements of the report should contain a complete list of those elements, even if they repeat report elements identified in chapter 2.

How the Task Force Addressed Issues Raised at the July 2015 ASB Meeting

1 Applicability of the Requirements in Chapters 1, 2, and 8 to Services Provided by a Subservice Organization

The ASB asked the task force to determine whether paragraph 8.10 of the July 2015 draft of chapter 8 (shown below) should be interpreted to mean that all of the requirements in chapter 8 and the related requirements in chapters 1 and 2 are applicable to a subservice organization when the inclusive method is used. If that is not the case, the task force should revise the paragraph as needed, for example, by identifying the requirements that are not applicable.

8.10 When the inclusive method is used, the service auditor should apply the requirements in this chapter to the services provided by the subservice organization, including the requirement to obtain management’s acknowledgement and acceptance of responsibility for the matters in paragraph 8.9*b* (i-vi) as they relate to the subservice organization. (Ref: par. 8.A20-and 8.A37)

(Paragraph 8.9*b* of the July draft lists all of the matters management is to acknowledge and accept responsibility for as a precondition of the engagement.)

The task force reports that in most inclusive engagements, the service organization is the only engaging party (not the service organization and the subservice organization). The task force concluded that when the subservice organization is not the engaging party, any requirements that relate to establishing the terms of the engagement would not be applicable to the subservice organization. Instead of identifying the requirements that do not apply to the subservice organization, the task force believes the issue is addressed by paragraph 1.16 of chapter 1, which states

1.16. Subject to paragraph 1.20, the practitioner should comply with each requirement of the attestation standards that is relevant to the engagement being performed, including any relevant subject-matter specific chapters, unless in the circumstances of the engagement,

- a. the entire chapter is not relevant; or
- b. the requirement is not relevant because it is conditional and the **condition does not exist**.

The task force concluded that when a subservice organization is not an engaging party, the condition of being an engaging party does not exist for the subservice organization and therefore, any requirements related to an engaging party do not apply to the subservice organization.

The task force revised old paragraph 8.10 (new par. 8.11) as shown below

8.108.11 When the inclusive method is used, the service auditor should apply the requirements in chapters 1, 2, and this chapter, as applicable, to the services provided by the subservice organization, including the requirement to obtain management's acknowledgement and acceptance of responsibility for the matters in paragraph ~~8.9b(i)-(vi)~~ 8.10b as they relate to the subservice organization. (Ref: par. ~~8.A20-8.A19~~ and ~~8.A37-8.A36~~)

2. Use of Report by Non-engaging Party Subservice Organization

Some ASB members expressed concern that a non-engaging party subservice organization in an inclusive engagement may be considered an intended user of the service auditor's report even though no contractual relationship exists between the subservice organization and the practitioner. (The inclusive method is based on the relationship that exists between the service organization and the subservice organization, to which the service auditor is not a party.) The counterargument is that the subservice organization should be entitled to a document that, among other things, contains the subservice organization's written assertion and description of the subservice organization's system; therefore, a practitioner may wish to consent to the designation of the subservice organization as an intended user of the report.

To address this issue, the task force added the following application paragraphs, which are linked to the requirement in new paragraphs 8.39*m* and 8.40*m* regarding the restricted-use paragraph.

8.A71. In engagements in which the inclusive method is used, the users of a subservice organization's system that are not users of the service organization's system are not user entities, as defined in paragraph 8.8s. (Ref: par. 8.30*m* and 8.40*m*)

8.A72. Management of the subservice organization may be identified as a specified party and, if so, would be included in the alert language described in paragraphs 8.39*m* and 8.40*m*. (Ref: par. 8.30*m* and 8.40*m*)

Deletion of Paragraph 8.A25

Paragraph 14 of extant AT 801 identifies the criteria to be used in determining whether management's description of the service organization's system is fairly presented. Paragraph 8.14a (iii) of extant AT 801 indicates that the description should include the following information about the system.

8.14 a (iii) The related accounting records, whether electronic or manual, and supporting information involved in initiating, authorizing, recording, processing, and reporting transactions. This includes the correction of incorrect information and how information is transferred to the reports and other information prepared for user entities.

Paragraph 8.14a (iii) has been redrafted in chapter 8 (par. 8.13a (iii) in the July draft) to be more generic with respect to the type of system being described and less financial-reporting oriented. (See below)

~~8.13a(iii)~~ 8.14a (iii). The information used in the performance of the procedures, including, if applicable, related accounting records, whether electronic or manual, and supporting information involved in initiating, authorizing, recording, processing, and reporting transactions. This includes the correction of incorrect information and how information is transferred to the reports and other information prepared for user entities.

This redrafting obviates the need for paragraph 8.A25 of the July draft which identifies examples of systems to which the criteria in paragraph 8.13a (iii) would not relate, for example, a system that relates to IT general controls over hosting of an IT application; a system that accumulates and reports data, for example, prices; or a system that generates and distributes statements for customers and user entities.

The following are the agenda materials for the ASB's discussion of chapter 8:

Item 2: Discussion Memo: Proposed Chapter 8, "Reporting on an Examination of Controls at a Service Organization Relevant to User Entities' Internal Control Over Financial Reporting" of the Proposed Clarified Attestation Standards (Clarified AT 801)

Item 2A: Draft of chapter 8 dated September 30, 2015 marked to show changes from the July 21, 2015 draft

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