



## Agenda Item 1J

### **Analysis of Due Process Related Proposed Revised Attestation Standards (AT-C sections 105 and 205 revised; proposed new AT-C section 206)**

#### **Overview**

At its meeting, July 20-23, 2020, the Auditing Standards Board (ASB) will be asked to vote to issue a final Statement on Standards for Attestation Engagements (SSAE) that revises AT-C section 105, *Concepts Common to All Attestation Engagements* and AT-C section 205, *Examination Engagements* and will result in a new AT-C section 206, *Direct Examination Engagements*.

If the Board votes to issue the proposed SSAE as a final standard, a separate vote will be held on whether due process was followed with respect to the development and issuance of the standard including whether the standard should be re-exposed for public comment. Based on the revisions to the attestation standards documented in the agenda materials, the Task Force and the Audit & Attest Standards staff, including the Chief Auditor, believe that due process has been followed and that re-exposure of the SSAE is not warranted.

Should a motion be made by a member of the ASB to re-expose the proposed SSAE, the vote would be conducted in the same manner in which the ASB would vote to ballot for issuance of any exposure draft of a proposed SSAE (i.e., re-exposure is the same as exposure). As such, to require re-exposure of the proposed SSAE, two-thirds of the ASB members would need to vote in favor of re-exposure (assuming all ASB members vote, this would require 13 ASB members to vote for re-exposure).

An analysis follows with respect to the provisions of due process related to the development and issuance of a proposed SSAE as a final standard.

#### **What Does Due Process Require?**

The AICPA's Auditing, Attestation and Quality Control Standards Setting Activities Operating Policies document<sup>1</sup> states that the ASB is the senior committee of the AICPA designated by Council to issue auditing, attestation, and quality control standards and practice guidance for

<sup>1</sup> The Operating Policies document is available at <https://www.aicpa.org/content/dam/aicpa/research/standards/auditattest/asb/downloadabledocuments/asb-operating-policies.pdf>.

performing and reporting on audit and attestation engagements for nonissuers (that is, entities not included within the jurisdiction of the Public Company Accounting Oversight Board (PCAOB)). Council resolved that any committee or board authorized by the Council to issue enforceable standards under the “General Standards Rule” (AICPA, Professional Standards, ET sec. 1.300.001), and the “Compliance With Standards Rule” must observe an exposure process seeking comment from other affected committees and boards, as well as the general membership.

Drafts of the proposed revisions to the attestation standards were presented to the ASB at numerous meetings leading up to the ASB’s meeting in May 2018. At that meeting, the ASB voted to expose for public comment a proposed SSAE that would, among other things, supersede AT-C sections 105 and 205 with revised sections. The proposed standard also included proposed revisions to AT-C sections 210, *Review Engagements* and 215, *Agreed-Upon Procedures Engagements* – which are not contemplated in the proposed SSAE that the ASB is asked to vote to issue at its meeting in July 2020. Fifteen members voted to ballot the proposed SSAE for public exposure and five members dissented. The dissenting members were Jay Brodish, Dora Burzenski, Joe Cascio, Ilene Kassman, and Steve Morrison. Their reasons for dissenting were included in the exposure draft of the proposed standard (see pages 16-22 of the exposure draft).<sup>2</sup>

The proposed SSAE was exposed for public comment on July 11, 2018 with a comment period ending on October 11, 2018. As stated on page 4 of the exposure draft, if the proposed standard were issued as a final standard as written, the most significant revision to AT-C sections 105 and 205 would be that the practitioner would no longer be required to request a written assertion from the responsible party when the practitioner is reporting directly on the subject matter.

The Task Force considered whether substantial changes were made to the exposed document that would result in a failure to follow due process and would therefore require that the proposed standard be re-exposed for public comment. There will almost always be changes to proposed standards from the exposure draft to the final standard in order to be appropriately responsive to comments received on the exposure draft – and this is certainly true with respect to the proposed revised attestation standards.

### **The Objective of the Exposure Draft**

In April 2016, the ASB issued SSAE No. 18, *Attestation Standards: Clarification and Recodification*, which clarified the attestation standards. As stated on page 6 of the July 2018 exposure draft, in completing the clarity attestation project, the ASB acknowledged that its standards were not converged with the ISAEs, in particular, because ISAE 3000 (Revised) does not require the practitioner to request a written “assertion” from the responsible party. The clarified standards require the practitioner to request such an assertion in order to perform an examination or review engagement. Accordingly, the ASB determined that such matters should be the subject

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<sup>2</sup> The exposure draft is available at <https://www.aicpa.org/content/dam/aicpa/research/exposedrafts/accountingandauditing/downloadabledocuments/20180711/20180711a-ed-ssae-18-revisions.pdf>.

of a follow-on ASB project to further evaluate the requirement for the practitioner to request an assertion.

To more closely converge with ISAE 3000, the July 2018 exposure draft proposed to revise the standards for examination engagements to

- No longer require the practitioner to request a written assertion from the responsible party when the practitioner is reporting directly on the subject matter. In the proposed SSAE, a written assertion from the responsible party would be required only if the practitioner were reporting on the assertion. In engagements in which the practitioner reports directly on the subject matter, requesting a written assertion from the responsible party would no longer be required.
- Add a statement to the practitioner's report regarding independence.
- Add a requirement for the practitioner to request a written representation stating whether the subject matter has been measured or evaluated against the criteria. In all examination engagements, the proposed SSAE would require the practitioner to request a representation from the appropriate party (either the engaging party or, if different, the responsible party) about whether the subject matter has been measured or evaluated against the criteria and, if so, the results of that measurement or evaluation. Because the practitioner may perform some or all of the measurement or evaluation of the subject matter against the criteria, the appropriate party may or may not have performed any such measurement or evaluation, depending on the engagement circumstances. The proposed SSAE acknowledges that there may be situations in which the practitioner is required to report on the responsible party's assertion or to request an assertion, for example, to comply with the terms of an engagement; management's request that the practitioner report on the assertion; the requirements of a law, regulation, or contract; or the requirements of a particular AT-C section, such as extant AT-C section 320, *Reporting on an Examination of Controls at a Service Organization Relevant to User Entities' Internal Control Over Financial Reporting*.
- Require the practitioner to determine whether management has a reasonable basis for its assertion when management provides an assertion. In order to report on management's assertion, the proposed SSAE requires the practitioner to use professional judgment in determining whether the appropriate party has a reasonable basis for making its assertion.
- Acknowledge the practitioner's ability to add information to the practitioner's report that goes beyond the minimum report elements required by AT-C section 205.
- Eliminate the required report modification resulting from the practitioner's inability to obtain one or more requested written representations.

While the exposure draft proposed to facilitate the performance of an examination engagement in which the practitioner reports directly on the subject matter within a revised AT-C section 205, the

ASB subsequently determined to substantially retain extant AT-C section 205 and instead include differential performance and reporting requirements for a direct examination engagement in a separate AT-C section (AT-C section 206). This change is intended to result in attestation standards that are easier to use and to apply. The public exposure is intended to provide commenters the opportunity to provide input with respect to proposed revised requirements and application guidance. How such revisions are codified in Professional Standards is at the discretion of the ASB and AICPA staff.

### **How are Significant Changes Proposed in the Exposure Draft Addressed in the Proposed Final SSAE?**

The following sections discuss how the significant proposed changes are addressed in the proposed final SSAE:

*No longer require the practitioner to request a written assertion from the responsible party when the practitioner is reporting directly on the subject matter.*

The exposure draft proposed the following revision to AT-C section 205 (see page 46 of the document that maps the extant AT-C sections to the exposure draft<sup>3</sup>):

#### **~~Requesting a Written Assertion~~**

~~10. The practitioner should request from the responsible party a written assertion about the measurement or evaluation of the subject matter against the criteria. When the engaging party is the responsible party and refuses to provide a written assertion, paragraph .82 requires the practitioner to withdraw from the engagement when withdrawal is possible under applicable law or regulation. When the engaging party is not the responsible party, and the responsible party refuses to provide a written assertion, the practitioner need not withdraw from the engagement. In that case, paragraph .84 requires the practitioner to disclose that refusal in the practitioner's report and restrict the use of the report to the engaging party. (Ref: par. A5, A8 and A97)~~

The proposed final SSAE retains the requirement in paragraph .10 of AT-C section 205 for the practitioner to request from the responsible party a written assertion about the measurement or evaluation of the underlying subject matter against the criteria. Paragraph .05 of proposed AT-C section 206 states, in performing a direct examination engagement, the practitioner is not required to request a written assertion from the responsible party.

Therefore, the proposed final SSAE accomplishes the objective of permitting the practitioner to perform an examination engagement without a requirement to request a written assertion from the responsible party while retaining the practitioner's ability to perform an examination engagement when it is appropriate to request such a written assertion.

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<sup>3</sup> The document that maps the extant AT-C sections to the exposure draft is available at <https://www.aicpa.org/content/dam/aicpa/research/exposedrafts/accountingandauditing/downloadabledocuments/20180711/20180711a-ed-supp.pdf>

***Add a statement to the practitioner's report regarding independence.***

The exposure draft included a requirement that the practitioner's examination report include a statement that the practitioner is independent and has fulfilled the practitioner's other ethical responsibilities in accordance with relevant ethical requirements related to the examination engagement (see page 101 of the July 2018 exposure draft).

Both proposed revised AT-C section 205 and 206 include a requirement that the practitioner's examination report include a statement that the practitioner is required to be independent and to meet the practitioner's other ethical responsibilities in accordance with relevant ethical requirements related to the examination engagement.

While the language is substantially the same as that which was exposed for public comment, the ASB determined, in open meeting deliberation, that it is appropriate the language in the final SSAE be consistent with the corresponding language in the auditing standards.

***Add a requirement for the practitioner to request a written representation stating whether the subject matter has been measured or evaluated against the criteria.***

The July 2018 exposure draft included a requirement that practitioner request from the appropriate party written representations in the form of a letter addressed to the practitioner. The representations should include a statement whether a party other than the practitioner has measured or evaluated the subject matter against the criteria, and, if another party has measured or evaluated the subject matter, the results of that measurement or evaluation. (see pages 90-92 of the July 2018 exposure draft).

As the ASB determined that extant AT-C section 205 should be retained for examination engagements in which an assertion is requested, such a representation is not applicable because an assertion is required pursuant to AT-C section 205 and is considered the equivalent of such a representation. Paragraph .07 of proposed AT-C section 206 provides the following as part of acceptance/continuance in a direct examination engagement:

- .07** Before accepting or continuing a direct examination engagement, the practitioner should obtain an understanding of the following matters through inquiries of the appropriate party:
- a. The intended purpose of the engagement, how the practitioner's report will be used, and why the engaging party wishes to engage the practitioner to perform a direct examination engagement
  - b. If the responsible party has not measured or evaluated the underlying subject matter against the criteria, why the responsible party has not done so
  - c. If the responsible party has measured or evaluated the underlying subject matter against the criteria, why the responsible party has not provided an assertion

Further, paragraph .A11 of proposed AT-C section 206 provides that if the responsible party states that it has measured or evaluated the underlying subject matter against the criteria, the practitioner may request the results of that measurement or evaluation.

The intent of the proposed requirement in the exposure draft is met by the requirement in proposed AT-C section 206.

***Require the practitioner to determine whether management has a reasonable basis for its assertion when management provides an assertion.***

Paragraph .60 of the July 2018 exposure draft includes a requirement, before the practitioner reports on management's assertion, that the practitioner use professional judgment in determining whether management has a reasonable basis for making its assertion (see page 97 of the exposure draft). That requirement is retained in paragraph .67 of proposed revised AT-C section 205. The requirement is not applicable in a direct examination engagement and, as such, is appropriately not included in proposed AT-C section 206. Further, paragraph .A11 of AT-C section 205 indicates that an assertion based solely on the practitioner's procedures would not be considered a reasonable basis for the assertion.

***Acknowledge the practitioner's ability to add information to the practitioner's report that goes beyond the minimum report elements required by AT-C section 205.***

The exposure draft includes the following application paragraph (see page 96 of the July 2018 exposure draft):

**.A81** The practitioner may choose to issue a report that contains only the minimum reporting elements included in paragraphs .62– .63 of this section or may issue a report that expands on or supplements those elements. In addition to the basic elements, the report may include information or explanations that are not intended to affect the practitioner's opinion, for example, detail about the terms of the engagement, the applicable criteria being used, findings relating to particular aspects of the engagement, details of the qualifications and experience of the practitioner and others involved with the engagement, a description of the procedures the practitioner performed, and, in some cases, recommendations. The practitioner may find it helpful to consider the importance of providing such information to the information needs of the intended users. As required by paragraph .79, additional information is clearly separated from the practitioner's opinion and phrased in a manner that makes clear that it is not intended to detract from that opinion.

Such guidance is provided, with additional clarifying language, in paragraph .A82 of proposed revised AT-C section 205.

***Eliminate the required report modification resulting from the practitioner's inability to obtain one or more requested written representations.***

The exposure draft proposed to revise paragraph .A64 of extant AT-C section 205 as follows:

~~**.A68** A64 In the situation discussed in paragraph .55, the refusal to furnish such evidence in the form of written representations constitutes a limitation on the scope of an examination sufficient to preclude an unmodified opinion and may be sufficient to cause the practitioner to withdraw from the engagement.~~ ***The engaging party's refusal to furnish written representations constitutes a limitation on the scope of the examination. Such refusal is***

*often sufficient to preclude an unmodified opinion and, particularly with respect to the representations in paragraph .A67, may cause a practitioner to disclaim an opinion or withdraw from the engagement when withdrawal is possible under applicable law or regulation. However, based on the nature of the representations not obtained or the circumstances of the refusal, the practitioner may conclude that a qualified opinion is appropriate.*

The proposed revision is included in paragraph .A67 of proposed revised AT-C section 205.

### **Changes Included in the Proposed Final SSAE That Were Not Explicitly Included in the ED**

#### ***Clarification that an examination engagement may be assertion-based or a direct engagement***

To clarify that an examination engagement may be assertion-based (and therefore covered by AT-C section 205) or a direct engagement (and therefore covered by AT-C section 206), AT-C section 105 is revised to describe the differences between an assertion-based and a direct examination engagement as well as to clarify that such engagements are both reasonable assurance engagements. The revisions to AT-C section 105 are necessary and appropriate due to retaining extant AT-C section 205 with only minor revisions.

#### ***Subject matter information/Underlying Subject Matter vs. Subject Matter***

Paragraph .10 of extant AT-C section 105 defines *subject matter* as the phenomenon that is measured or evaluated by applying criteria. The proposed revised AT-C section 105 replaces that term with the following defined terms:

**Subject matter information.** The outcome of the measurement or evaluation of underlying subject matter against criteria. An assertion about whether the underlying subject matter is in accordance with the criteria is a form of subject matter information

**Underlying subject matter.** In an examination or review engagement, the phenomenon that is measured or evaluated by applying criteria. In an agreed-upon procedures engagement, the phenomenon upon which procedures are performed.

The revision results in further convergence with ISAE 3000 (Revised) and was initially considered by the ASB as a result of comment letters received on the exposure draft (see pages 5-8 of the highlights of the January 14-17, 2019 ASB meeting).<sup>4</sup> Further, to clarify the practitioner's independence requirements run to the underlying subject matter as opposed to the subject matter information, such defined terms are necessary.

<sup>4</sup> The highlights of the January 14-17, 2019 meeting are available at <https://www.aicpa.org/content/dam/aicpa/research/standards/auditattest/asb/documents/mtg/1901/2019-01-asb-highlights.pdf>.

Paragraph .01 of proposed AT-C section 105 clearly states that in all attestation engagements the underlying subject matter is the responsibility of a party other than the practitioner. The Audit & Attest Standards staff and the Task Force also discussed independence matters with the AICPA Ethics Division staff as well as representatives of the AICPA Professional Ethics Executive Committee and agreement was reached that as long as someone other than the practitioner takes responsibility for the underlying subject matter, the practitioner's independence would not be impaired.

### **Overall Conclusion**

The Task Force and the Audit & Attest Standards staff, including the Chief Auditor, believe that the revisions proposed in the July 2018 exposure draft have clarified the requirements for the proposed direct examination engagement while retaining the practitioner's ability to perform an assertion-based engagement in accordance with extant AT-C section 205. The revisions reflected in the proposed final SSAE have not resulted in a departure from the objective of the project nor have they resulted in the introduction of significant new concepts.

The public interest is not served by further delay of the proposed revised standards which will result in flexibility in the performance of examination engagements and closer convergence with ISAE 3000 (Revised). In addition, the Task Force does not believe that re-exposure of the proposed revised attestation standards will provide any new feedback that has not already been considered through the comment letters received or ASB deliberations conducted in open public meetings on the July 2018 exposure draft.

The Task Force recognizes that additional guidance will most likely be necessary to assist practitioners in implementing AT-C section 206. Such guidance should be developed post-issuance of the proposed standard.