

Agenda Item 3



Consideration of Potential Revisions to SSARs for Consistency With Proposed Revisions to AU-C sections 700 and 800

Discussion Memo

Objective of Agenda Item

To discuss significant proposed revisions to the auditor reporting model under consideration by the Auditing Standards Board (ASB) and whether similar revisions should be considered for reports issued in accordance with SSARs.

Background

On November 28, 2017 the Auditing Standards Board (ASB) issued an exposure draft addressing several different AU-C sections with respect to auditor reporting. That exposure draft is available at <https://www.aicpa.org/content/dam/aicpa/research/exposuredrafts/accountingandauditing/downloadabledocuments/20171128c-ed-auditor-reporting.pdf>.

Comments were due on the proposed revisions on May 15, 2018. The ASB met on July 23-26, 2018 and was provided preliminary feedback from the comment letters received and was requested to provide direction to the Task Force working on the proposed revisions.

The ASB undertook its project that resulted in the exposure draft of the proposed SAS in an effort to increase the informational value and relevance for users of the auditor's report. In addition, both the International Auditing and Assurance Standards Board (IAASB) and the Public Company Accounting Oversight Board (PCAOB) undertook separate auditor reporting projects. The ASB monitored those projects and formed a task force to consider the implications of those projects on auditor's reports for audits of nonissuers.

The exposure draft proposes significant changes to extant auditing standards if issued as final. The most obvious change is that the exposure draft proposes that the "Opinion" section be presented first in the auditor's report, followed by the "Basis for Opinion"

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section. This change is consistent with the changes to the auditor's report resulting from the IAASB's new and revised ISAs as well as the PCAOB auditor reporting model.

The ARSC has previously discussed whether it would be appropriate to position the accountant's review report model so that the "Accountant's Conclusion" was presented first. The ARSC noted that the reporting requirements in AR-C section 90 do not prescribe the ordering of the paragraphs so that if an accountant wanted to present the review report in a manner that resembled the auditor reporting model, he or she would not be precluded from doing so. Additionally, the illustrative review reports included in International Standard for Review Engagements (ISRE) 2400 (Revised), *Engagements to Review Historical Financial Statements* maintain the conclusion paragraph at the end of the report and the proposed revised AT-C section 210, *Review Engagements* (exposed for public comment as part of the proposed revised attestation standards) likewise includes illustrations with the conclusion paragraph at the end of the report. The ARSC had concluded that it would not require that the conclusion paragraph be presented first in an accountant's review report in accordance with AR-C section 90.

Additionally, the exposure draft proposes a requirement that the "Basis for Opinion" section of the auditor's report include an affirmative statement about the auditor's independence and fulfillment of the auditor's other ethical responsibilities in accordance with relevant ethical requirements related to the audit. Paragraph 72h of the proposed revised AR-C section 90 to be discussed at the ARSC meeting as part of Agenda item #1 includes a requirement that the accountant's review report include a statement that the accountant is independent and has fulfilled the accountant's other ethical responsibilities in accordance with relevant ethical requirements relating to the review engagement.

The exposure draft also includes requirements regarding communication of key audit matters (KAMs) when the terms of the audit engagement include reporting KAMs (note that communication of KAMs would not be required for audits of nonissuers). The concept of "key review matters" is not contemplated.

Issues for ARSC Consideration

Reporting When There is Substantial Doubt About the Entity's Ability to Continue as a Going Concern

The proposed amendments to AU-C section 570 modify the requirements relating to auditor reporting on going concern to be consistent with the corresponding requirements in ISA 570 (Revised). The underlying auditor performance requirements relating to going concern are not changing.

If, after considering identified conditions or events and management's plans, the auditor concludes that substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time remains, the auditor would include a separate section in the auditor's report under the heading "Substantial Doubt About the Entity's Ability to Continue as a Going Concern" instead of an emphasis-of-matter paragraph. The content of this separate section would be similar to that included in the emphasis-of-matter paragraph.

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The proposed revisions to the auditing standards are presented on pages 290-297 of the exposure draft.

The following represents the revisions that would be made to draft of the proposed revised AR-C section 90 (included as agenda item 1B) if the ARSC determines to revise the review reporting requirements to be consistent with the proposed revised auditor reporting requirements:

<p>Implications for the Accountant’s Review Report When Substantial Doubt Exists About the Entity’s Ability to Continue as a Going Concern</p>	<p>Implications for the Accountant’s Review Report When Substantial Doubt Exists About the Entity’s Ability to Continue as a Going Concern (Ref: par. 93)</p>	<p>Deleted: an emphasis-of-matter paragraph</p>
<p>.93 If, after considering conditions or events and management’s plans, the accountant concludes that substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time remains, the accountant should include <u>a separate section</u> in the accountant’s review report with the heading “Substantial Doubt About the Entity’s Ability to Continue as a Going Concern” that; (Ref: par. .A140–.A143)</p>	<p>.A140 The identification of substantial doubt is a matter that <u>important to users’ understanding of the financial statements. The use of a separate section with a heading that includes reference to the fact that substantial doubt exists about the entity’s ability to continue as a going concern alerts users to this circumstance.</u></p>	<p>Deleted: .</p>
<p>a. <u>Draws attention to the note in the financial statements that discloses</u></p> <p>i. <u>The conditions or events identified and management’s plans that deal with these conditions or events; and</u></p> <p>ii. <u>That these conditions or events indicate that substantial doubt exists about the entity’s ability to continue as a going concern for a reasonable period of time, and</u></p> <p>b. <u>States that the accountant’s conclusion is not modified with respect to the matter.</u></p>	<p>.A141 <u>The appendix to this section provides illustrations of the statements that are required to be included in the accountant’s review report on the financial statements. The illustrations provide examples in which FASB ASC is the applicable financial reporting framework. If an applicable financial reporting framework other than FASB ASC is used, the wording of the illustrative reports in the appendix to this section may need to be adapted to reflect the application of the applicable financial reporting framework in the circumstances.</u></p>	<p>Deleted: A140</p>
	<p>.A142 If conditions or events, considered in the aggregate, have been identified that raise substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time but, based on the review evidence obtained, the accountant concludes that substantial doubt has been alleviated by management’s plans <u>a adequate disclosure has been made in the financial statements,</u> the accountant may include an emphasis-of-matter paragraph making reference to management’s disclosures related to the conditions or events and management’s plans related to those conditions or events. <u>In this circumstance, the use of an emphasis-of-matter paragraph to draw users’ attention to the disclosures of conditions and events</u></p>	<p>Commented [MG1]: Note to ARSC – Illustrative reports will be prepared if the ARSC determines that the proposed revisions are appropriate.</p>
		<p>Deleted: The following is an illustration of a going concern emphasis-of-matter paragraph when (a) the accountant concludes that substantial doubt exists about the entity’s ability to continue as a going concern for a reasonable period of time, (b) management’s plans do not alleviate the substantial doubt, and (c) the entity is required under the applicable financial reporting framework to include a statement in the notes to the financial statements that substantial doubt exists: ¶ Emphasis of Matter Regarding Going Concern¶ The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note X to the financial statements, the Company has suffered recurring losses from operations, has a net capital deficiency, and has stated that substantial doubt exists about the Company’s ability to continue as a going concern. Management’s evaluation of the events and conditions and management’s plans regarding these matters are also described in Note X. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our conclusion is not modified with respect to this matter.¶ .A141 The following is an illustration of a going concern emphasis-of-matter paragraph when (a) the accountant concludes that substantial doubt exists about the entity’s ability to continue as a going concern for a reasonable period of time, (b) management’s plans do not alleviate the substantial doubt, and (c) the entity is not required under the applicable financial reporting framework to include a statement in the notes to the financial statements that substantial doubt exists.¶ ¶ Emphasis of Matter Regarding Going Concern¶ ¶ The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note X to the financial statements, the Company has suffered recurring losses from operations and has a net capital deficiency, which raises substantial doubt about its ability to continue as a going concern. Management’s evaluation of the events and conditions and management’s plans regarding these matters at ...</p>

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	<p><u>and management's plans. It is distinguished from the situation in which the accountant concludes, after considering identified conditions or events and management's plans, that substantial doubt about an entity's ability to continue as a going concern remains, in which case the accountant is required by paragraph .93 to include a separate "Going Concern" section in the accountant's review report.</u></p>
<p>.94 The <u>description in the going concern section</u> about the entity's ability to continue as a going concern for a reasonable period of time should use terms consistent with those included in the applicable financial reporting framework. The accountant should not use conditional language concerning the existence of substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time. (Ref: par. .A143)</p>	<p>.A143 Examples of conditional language <u>that are inappropriate to use in the "Going Concern" section</u> include the following:</p> <ul style="list-style-type: none"> • If the entity continues to experience recurring losses from operations and continues to have a net capital deficiency, there may be substantial doubt about ability to continue as a going concern. • The entity has been unable to renegotiate its expiring credit agreements. Unless the entity is able to obtain financial support, there is substantial doubt about ability to continue as a going concern.
<p>.95 If adequate disclosure about an entity's ability to continue as a going concern for a reasonable period of time is not made in the financial statements, the accountant should apply paragraphs .67—.70 regarding modified conclusion when the financial statements are materially misstated <u>and in the basis for conclusion paragraph state that</u></p> <p>a. <u>Substantial doubt exists about the entity's ability to continue as a going concern and that the financial statements do not adequately disclose this matter or</u></p>	

Deleted: The following is an illustration of an emphasis-of-matter paragraph when management has disclosed (a) conditions or events, considered in the aggregate, that raised substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time; (b) its evaluation of the significance of those conditions or events, considered in the aggregate, in relation to the entity's ability to meet its obligations; and (c) that the substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time has been alleviated by management's plans.

Deleted: Emphasis of Matter Regarding Going Concern¶ As discussed in Note X to the financial statements, the Company has suffered recurring losses from operations and has a net capital deficiency. Management's evaluation of the events and conditions and management's plans to mitigate these matters are also described in Note X. Our conclusion is not modified with respect to this matter.

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- b. [Substantial doubt about the entity's ability to continue as a going concern has been alleviated by management's plans but the financial statements do not adequately disclose this matter.](#)

Action Requested of ARSC

The ARSC is asked to consider AR-C section 90 should be revised as indicated so as to be consistent with the proposed revisions to the auditor reporting requirements. If so, the ARSC is asked whether the proposed revisions should be included in the draft revised AR-C section 90 that the ARSC is asked to consider voting to issue for public exposure (as part of Agenda item 1).

Responsibilities of Management for the Preparation and Fair Presentation of the Financial Statements

The proposed revised auditor reporting requirements expands the description of management for the preparation and fair presentation of the financial statements, and includes a requirement to identify those responsible for the oversight of the financial reporting process when those responsible for such oversight differ from those responsible for the preparation of the financial statements. See pages 45-47 of the exposure draft at <https://www.aicpa.org/content/dam/aicpa/research/exposedrafts/accountingandauditing/downloadabledocuments/20171128c-ed-auditor-reporting.pdf>.

If corresponding requirements were included in AR-C section 90, paragraph 72d of the draft proposed AR-C section 90 (Agenda item 1B) would be revised as follows:

d. A section with the heading “Responsibilities of Management for the Financial Statements” that describes management’s responsibility for the following:

i. The preparation and fair presentation of the financial statements in accordance with the applicable financial reporting framework; this responsibility 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 (Ref: par. .A106)

ii. Assessing the entity’s ability to continue as a going concern in accordance with the applicable financial reporting framework and determining whether the use of the going concern basis of accounting is appropriate.

Additionally, the following would be included as new paragraphs 73-74:

.73 The section of the accountant’s review report with the heading “Responsibilities of Management for the Financial Statements” as required by paragraph .72d should also identify those responsible for the oversight of the financial reporting process when those responsible for such oversight are different from those who fulfill the responsibilities described in paragraph .72d. In this case, the heading of this section should also refer to “Those Charged With Governance” or another appropriate term.

.74 The description of management’s responsibility for the financial statements in the auditor’s report should not reference a separate statement by management about

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[such responsibilities, even if such statement is included in a document containing the accountant's review report.](#)

Note that the proposed SAS is organized so that the reporting requirements are presented as individual paragraph numbers – whereas the reporting requirements in AR-C section 90 are presented in one paragraph number with subparagraphs presented as letters.

The proposed SAS also includes additional application guidance that the ARSC may consider for inclusion in any revision of AR-C section 90.

The proposed SAS also expands the description of the responsibilities of the auditor and key features of the audit (see pages 47-50 of the exposure draft at <https://www.aicpa.org/content/dam/aicpa/research/exposedrafts/accountingandauditing/downloadabledocuments/20171128c-ed-auditor-reporting.pdf>). The required description of the accountant's responsibilities in a review report are considered appropriate and no revisions are proposed.

Action Requested of ARSC

The ARSC is asked to consider whether AR-C section 90 should be revised as indicated so as to be consistent with the proposed revisions to the auditor reporting requirements. If so, the ARSC is asked whether the reporting requirements in AR-C section 90 should be rearranged so as to be consistent with the formatting in the proposed SAS, *Forming an Opinion and Reporting on Financial Statements* and whether the proposed revisions should be included in the draft revised AR-C section 90 that the ARSC is asked to consider voting to issue for public exposure (as part of Agenda item 1).

Financial Statements Prepared in Accordance With a Special Purpose Framework

In a project separate from the exposure draft, the ASB's Auditor Reporting Task Force has proposed revisions to AU-C section 800, *Special Considerations—Audits of Financial Statements Prepared in Accordance With Special Purpose Frameworks*, to (1) reflect changes to the auditor's report included in the November 2017 ASB exposure draft, and (2) introduce the concept of a compliance framework, which is included in ISA 800 (Revised) *Special Considerations—Audits of Financial Statements Prepared in Accordance With Special Purpose Frameworks*.

SSARS 24 added a definition for the term *fair presentation framework* and amended the definition of *financial reporting framework* included in paragraph .07 of AR-C section 60, as follows:

Financial reporting framework. A set of criteria used to determine measurement, recognition, presentation, and disclosure of all material items appearing in the financial statements (for example, accounting principles generally accepted in the United States of America [U.S. GAAP], International Financial Reporting Standards promulgated by the International Accounting Standards Board, or a special purpose framework).

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The term fair presentation framework refers to a financial reporting framework that requires compliance with the requirements of the framework and does one of the following:

- a. Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework.*
- b. Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in rare circumstances.*

A financial reporting framework that requires compliance with the requirements of the framework but does not contain the acknowledgment in (a) or (b) is not a fair presentation framework.

The preceding definition is consistent with the corresponding definitions in extant auditing standards. A “compliance framework” would be a framework as contemplated by the final paragraph in the preceding.

The ASB Auditing Reporting Task Force presented a proposed revised AU-C section 800 to the ASB at its meeting in July 2018. That proposed revised draft is available at <https://www.aicpa.org/content/dam/aicpa/research/standards/auditattest/asb/documents/mtg/1807/2018-07-asb-item6a.pdf>.

Action Requested of ARSC

Because there are far more reviews and compilations on financial statements prepared in accordance with special purpose frameworks than audits on such financial statements, the ARSC is asked to consider the revisions being considered by the ASB. The ARSC is further asked to consider whether any revisions should be proposed to SSARSs with respect to the revisions being considered by the ASB. If the ARSC determines that revisions need not be made, the Committee is asked to provide feedback to the ASB.

Agenda Items Presented:

No additional agenda material is presented.