

## Agenda Item 1



# Proposed Revisions to SSARSs – Materiality/Adverse Conclusions/Special Purpose Frameworks

## Discussion Memo

### Objective of Agenda Item

To consider proposed SSARS, *Materiality In a Review of Financial Statements; Adverse Conclusions; and Special Purpose Frameworks* and vote to ballot to expose the proposed SSARS for public comment.

### Background

At its meeting in August 2018, the ARSC voted to ballot to expose certain revisions to AR-C sections 60 and 90 for public exposure. The exposure draft proposed to more closely converge AR-C section 90 with ISRE 2400 (Revised), *Engagements to Review Historical Financial Statements*. Those most significant revisions were proposals to:

- Explicitly require the accountant to determine materiality for the financial statements as a whole, and apply this materiality in designing the procedures and in evaluating the results obtained from those procedures
- Permit the accountant to express an adverse conclusion when he or she determines, or otherwise becomes aware, that the financial statements are materially misstated and the effects of the matter(s) are both material and pervasive to the financial statements.

Subsequently, at the August 2018 meeting, the ARSC separately considered revisions that the ASB's Auditor Reporting Task Force had proposed to AU-C section 800, *Special Considerations—Audits of Financial Statements Prepared in Accordance With Special Purpose Frameworks*, to 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* and ISRE 2400 (Revised).

Proposed Revisions to SSARs  
Materiality/Adverse Conclusions/Special Purpose Frameworks  
Discussion Memorandum  
ARSC Meeting, May 7-8, 2019

The ARSC directed revisions be developed to SSARs that would be consistent with the proposed revisions to AU-C section 800 and, if determined to be appropriate by the ARSC, that such proposed revisions be included in the exposure draft of the proposed revisions to further converge the requirements for reviews performed in accordance with SSARs with ISRE 2400 (Revised).

The ASB's Auditor Reporting Task Force will be discussing a proposal to not make any revisions that would incorporate the concept of a compliance framework with the ASB at its meeting in May 2019. Therefore, the proposed revisions to SSARs have excluded any revisions to incorporate the concept of a compliance framework but does include certain other revisions for consistency with the proposed revisions to AU-C section 800 as well as Statement on Auditing Standards No. 134, *Auditor Reporting and Amendments, Including Amendments Addressing Disclosures in the Audit of Financial Statements* (issued April 2019).

The ASB expects to vote to ballot to expose the proposed revisions to AU-C section 800 at its meeting in July 2019. The ARSC had previously determined that it is appropriate to expose the proposed SSARS for public comment simultaneously with the ASB's exposure draft.

Additionally, the ASB's Materiality Definition Task Force was charged with developing amendments to the auditing and attestation standards to align the materiality concepts described in *Professional Standards* with the definition of materiality used by the United States judicial system, the auditing standards of the Public Company Accounting Oversight Board, the Financial Accounting Standards Board (FASB), the Government Accounting Standards Board, and the U.S. Securities and Exchange Commission (SEC). ARSC member Victoria Pitkin is a member of that Task Force. Revisions for consistency with the proposed revisions to the auditing standards are included in the proposed revised AR-C section 90. The ASB expects to vote to ballot to expose the proposed materiality definition revisions to the auditing and attestation standards at its meeting in May 2019.

### **Issues for ARSC Consideration**

#### **Issue #1 – Revision to AR-C section 70 when the accountant withdraws from a preparation engagement**

When the accountant is unable to include a statement on each page of the prepared financial statements that “no assurance is provided,” paragraph .14 of extant AR-C section 70 requires that the accountant:

- a. Issue a disclaimer that makes clear that no assurance is provided on the financial statements;
- b. Perform a compilation engagement in accordance with AR-C section 80; or

Proposed Revisions to SSARs  
Materiality/Adverse Conclusions/Special Purpose Frameworks  
Discussion Memorandum  
ARSC Meeting, May 7-8, 2019

- c. Withdraw from the engagement.

The withdrawal requirement in subparagraph c contrasts with similar withdrawal language in paragraph 16 of AR-C section 80 which states “The accountant should withdraw from the engagement ***and inform management of the reasons for withdrawing*** if...” (emphasis added). Paragraphs .A22-.A23 of AR-C section 80 state the following:

**.A22** In circumstances addressed by the requirements of this section in which withdrawal from the engagement is necessary, the responsibility to inform management of the reasons for withdrawing provides an opportunity to explain the accountant's ethical obligations.

**.A23** When making a determination about whether and how to withdraw from an engagement, the accountant may wish to consult with legal counsel.

It seems that the reasoning for informing management for the reasons for withdrawing from a compilation engagement would equally pertain to a preparation engagement. Therefore, it is proposed that paragraph .14 of AR-C section 70 be revised as follows:

**.14** The accountant should ensure that a statement is included on each page of the financial statements indicating, at a minimum, that "no assurance is provided" on the financial statements. If the accountant is unable to include a statement on each page of the financial statements, the accountant should (Ref:par..~~A13~~**A12**)

- a. issue ~~either~~ a disclaimer that makes clear that no assurance is provided on the financial statements; (Ref:par..~~A14~~**A13**)
- b. perform a compilation engagement in accordance with section 80, *Compilation Engagements*; or
- c. withdraw from the engagement ***and inform management of the reasons for withdrawing***. (Ref: par. **A14 - .A15**)

The proposed application guidance in paragraphs .A14-.A15 is consistent with paragraphs .A22-.A23 of AR-C section 80.

**Action Requested of ARSC**

The ARSC is asked to consider whether it agrees with the proposed revisions to AR-C section 70 when the accountant intends to withdraw from a preparation engagement.

*Issue #2 – Revision to AR-C section 70 regarding misleading financial statements*

Paragraph .21 of AR-C section 70 states that the accountant should not prepare financial statements that omit substantially all disclosures required by the financial reporting framework if the accountant becomes aware that the omission of substantially all

Proposed Revisions to SSARSs  
Materiality/Adverse Conclusions/Special Purpose Frameworks  
Discussion Memorandum  
ARSC Meeting, May 7-8, 2019

disclosures was undertaken with the intention of misleading users of such financial statements.

Paragraphs .A20-.A21 of AR-C section 80 provide the following guidance with respect to misleading financial statements:

.A20 Financial statements may be misleading, for example, if the applicable financial reporting framework includes the premise that the financial statements are prepared on the going concern basis, and undisclosed uncertainties exist regarding the entity's ability to continue as a going concern. If the accountant becomes aware that uncertainties exist regarding the entity's ability to continue as a going concern, the accountant may suggest additional disclosures concerning the entity's ability to continue as a going concern in order to avoid the financial statements being misleading.

.A21 Disclosure of items, such as an uncertainty, is not required in financial statements in which substantially all the disclosures required by the applicable financial reporting framework are omitted.

It is proposed that the application guidance from paragraphs .A20-.A21 of AR-C section 80 be repeated as paragraphs .A21-.A22 of AR-C section 70.

**Action Requested of ARSC**

The ARSC is asked to consider whether it agrees with the proposed additional application paragraphs to provide guidance regarding misleading financial statements in a preparation engagement.

*Issue #3 – Proposed amendments to AT-C section 210*

The Attestation Standards Task Force has been working with both the ARSC and the ASB on proposed revisions to the attestation standards. At its meeting in January 2019, the ASB was generally comfortable that if an adverse conclusion is permitted in a review of financial statements in accordance with AR-C section 90, that AT-C section 210 would also permit the expression of adverse conclusion in a review of other subject matter. Because the expression of an adverse conclusion in an attestation review was proposed in the exposure draft of the proposed revised attestation standards, there will be no re-expose of the specific proposal with respect to an attestation review. The ASB asked the Task Force to include a question about consistency between proposed revised AR-C section 90 and AT-C section 210 in this specific respect in the Explanatory Memorandum to the proposed SSARS ED.

A specific request for comment with respect to the consistency between proposed revisions to both AR-C section 90 and AT-C section 210 is included in the proposed wrap document (agenda item 1C).

Proposed Revisions to SSARSs  
Materiality/Adverse Conclusions/Special Purpose Frameworks  
Discussion Memorandum  
ARSC Meeting, May 7-8, 2019

**Action Requested of ARSC**

The ARSC is asked to consider whether it agrees with the specific request for comment included in the proposed wrap document.

*Issue #4 – Effective Date*

The proposed effective date for the revisions to AR-C sections 60, 70, 80, and 90 is for engagements performed in accordance with SSARSs for periods ending on or after July 15, 2021. This date is consistent with the proposed effective date for the attestation standards. While that date is subject to change pursuant to ARSC and ASB deliberations, it would make sense to have the two sets of standards have consistent effective dates. Nevertheless, while the proposed attestation standards preclude early implementation, it is proposed that the SSARSs ED allow for early implementation. The effect would be that a practitioner could issue an adverse conclusion on a review performed in accordance with AT-C section 210 upon issuance of the proposed SSARS.

**Action Requested of ARSC**

The ARSC is asked to consider whether it agrees with the proposed effective date.

**Overall Action Requested of ARSC**

The ARSC is asked to vote to ballot the proposed SSARS for public comment.

**Agenda Items Presented:**

- |                |   |
|----------------|---|
| Agenda item 1A | Proposed SSARS, <i>Materiality In a Review of Financial Statements; Adverse Conclusions; and Special Purpose Frameworks</i> – redline to show changes from the January 2019 draft |
| Agenda item 1B | Proposed SSARS, <i>Materiality In a Review of Financial Statements; Adverse Conclusions; and Special Purpose Frameworks</i> – clean   |
| Agenda item 1C | Proposed wrap document  |
| Agenda item 1D | Mapping document comparing ISRE 2400 (Revised) and extant AR-C sections 60 and 90 to proposed revisions to AR-C sections 60 and 90  |

Mr. Glynn will use Agenda item 1A in leading the discussion of the proposed SSARS.