

NINJA BOOK

Auditing & Attestation



Attestation Engagements

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Attestation Engagements

Overview of Attestation Standards

Attestation Engagements

1. **Attestation** An attest engagement is one in which a CPA in public practice (i.e., practitioner) is engaged to, or does, issue an examination, review, compilation or agreed-upon procedures report on subject matter, or an assertion about subject matter, that is the responsibility of another party (usually management). An attest engagement may be part of a larger engagement, for example, a feasibility study or business acquisition study that includes an examination of prospective financial information.
2. **Applicability** Attestation services include: agreed-upon procedures (excluding letters to underwriters and consulting services or any attest engagement concerning assertions about solvency); financial forecasts and projections; pro forma financial statements; internal control over financial reporting; compliance reporting (regulatory or contractual); and Management's Discussion and Analysis. An attest engagement can be: an audit or other engagement under SAS; a review of financial statements under SSARS; an examination of prospective financial information under SSAE; or any engagement under PCAOB. It does not include any other SSAE engagement (such as a review or agreed-upon procedure), nor does it include compilations under SSARS.
3. **Degrees of Responsibility** AT 20, *Defining Professional Requirements in Statements on Standards for Attestation Engagements*, defines two kinds of requirements that describe the practitioner's degrees of responsibility.
 - a. **Unconditional Requirements** The practitioner is required to comply with an unconditional requirement in all cases in which the requirement applies. The words *must* or *is required* indicate an unconditional requirement.
 - b. **Presumptively Mandatory Requirements** The practitioner is also required to comply with a presumptively mandatory requirement in all cases in which the requirement applies. However, in rare circumstances, the practitioner may depart from such a requirement provided the practitioner documents the justification in the workpapers and the alternative procedures performed to achieve the objectives of that requirement. The word *should* indicate a presumptively mandatory requirement.
4. **Subsequent Events** Attest standards define subsequent events in essentially the manner as for audits performed in accordance with GAAS. While the practitioner has no responsibility to detect subsequent events, the practitioner should inquire of the responsible party (and the client, if different) as to whether they are aware of any subsequent events through the report date. The representation letter ordinarily contains a representation about subsequent events.
5. **Subject Matter** The subject matter of an attest engagement may take many forms, including:
 - a. Historical or prospective performance or condition, for example, historical or prospective financial information, performance measurements, and backlog data
 - b. Physical characteristics, for example, narrative descriptions, square footage of facilities
 - c. Historical events, for example, the price of a market basket of goods on a certain date
 - d. Analyses, for example, break-even analyses
 - e. Systems and processes, for example, internal control
 - f. Behavior, for example, corporate governance, compliance with laws and regulations, human resource practices
6. **Written Assertion** An assertion is any declaration(s) about whether subject matter is based on, or in conformity with, selected criteria. A CPA may attest to a written assertion or directly on the subject matter.

In either situation, the CPA typically obtains a written assertion in an examination or a review engagement. A written assertion may be presented to the CPA in several ways, including: a narrative description, a schedule, or as part of a representation letter which clearly identifies what is being presented and the point in time or period of time covered. Without a written assertion, the CPA still may report on the subject matter; however, the CPA needs to exercise caution and ensure that interested parties clearly understand the subject matter in question, including restricting use of the report, when appropriate.

7. **Trust Services** Trust Services are a set of professional assurance services based on a framework comprised of a core set of principles and criteria. The framework addresses risk and opportunities associated with information technology. SysTrust and WebTrust are two specific services jointly developed by the AICPA and the Canadian Institute of Chartered Accountants. Engagements use the following five principles and criteria: security; availability; processing integrity; online privacy; and confidentiality.
 - a. **WebTrust** Practitioners who obtain a WebTrust business license from can provide assurance services to evaluate and test whether a particular eCommerce service meets the selected principles and criteria. The WebTrust seal of assurance is placed on the organization's website following the engagement and signifies the practitioner's unqualified opinion.
 - b. **SysTrust** A SysTrust engagement allows practitioners to provide assurance on the reliability of a system.

Attestation Standards

The AICPA Code of Professional Conduct requires an AICPA member who performs an attestation engagement to comply with Statements on Standards for Attestation Engagements (SSAE). SSAE are codified within the framework of the 11 attestation standards. Attestation interpretations are recommendations on the application of SSAE in specific circumstances. The practitioner should be aware of and consider attestation interpretations applicable to the attestation engagement. If the practitioner does not apply the attestation guidance included in an applicable attestation interpretation, the practitioner should be prepared to explain how he or she complied with SSAE provisions addressed by such attestation guidance.

1. **Applicability** SSAE do not apply to: audits; reviews and compilations of financial statements of nonissuers under SSARS; tax return preparation; advocating, consulting, or advisory services; or operational audits.
2. **General Standards**
 - a. **Training and Proficiency** The practitioner must have adequate technical training and proficiency to perform the attestation engagement.
 - b. **Adequate Knowledge of the Subject Matter** The practitioner must have adequate knowledge in the subject matter.
 - c. **Suitability and Availability of Criteria** The practitioner must have reason to believe that the subject matter is capable of evaluation against criteria that are suitable and available to users.
 - d. **Independence** The practitioner must maintain independence in mental attitude in all matters relating to the engagement.
 - e. **Due Professional Care** The practitioner must exercise due professional care in the planning and performance of the engagement and the preparation of the report.

Exercise 14.1 - Attestation Standards

The general standard regarding the suitability and availability of criteria for an attest engagement performed in accordance with the AICPA's Statements on Standards for Attestation Engagements (SSAE) requires that suitable criteria have all of the following attributes **except**

- a. Objectivity
- b. Measurability
- c. Relevance
- d. Acceptance

Answer d. is not one of the required attributes for suitable criteria for an attest engagement. There are four; the one missing from above is *completeness*. See the descriptions of each attribute in the supplemental material at the end of this chapter.

3. Fieldwork Standards

- a. **Planning and Supervision** The practitioner must adequately plan the work and must properly supervise any assistants.
- b. **Obtaining Sufficient Evidence** The practitioner must obtain appropriate sufficient evidence to provide a reasonable basis for the conclusion that is expressed in the report.

4. Reporting Standards

- a. **Identification of Subject Matter or Assertion** The practitioner must identify the subject matter or the assertion being reported on and state the character of the engagement in the report.
- b. **Conclusion** The practitioner must state the practitioner's conclusion about the subject matter or the assertion in relation to the criteria against which the subject matter was evaluated in the report.
- c. **Disclosure of Reservations** The practitioner must state all of the practitioner's significant reservations about the engagement, the subject matter, and, if applicable, the assertion related thereto in the report.
- d. **Restrictions** The practitioner must state in the report that the report is intended solely for the information and use of the specified parties under the following circumstances:
 - (1) When the criteria used to evaluate the subject matter are determined by the practitioner to be appropriate only for a limited number of parties who either participated in their establishment or can be presumed to have an adequate understanding of the criteria
 - (2) When the criteria used to evaluate the subject matter are available only to specified parties
 - (3) When reporting on subject matter and a written assertion has not been provided by the responsible party
 - (4) When the report is on an attestation engagement to apply agreed-upon procedures to the subject matter

Report Components

Standard reports for examinations and reviews share some elements:

- 1. **Title** The title includes the word *independent*, a signature, and a date.
- 2. **Responsible Party's Responsibility** A statement that the subject matter [or, assertion] is the responsible party's responsibility.
- 3. **Identification** An identification of the subject matter [or, assertion] and the responsible party. If the assertion doesn't accompany the practitioner's report, the first paragraph of the report also contains a statement of the assertion.

4. Restriction A statement restricting the report use to specified parties

Conclusions

Three types of conclusions can be issued by the accountant:

1. Examination Examinations represent the highest level of assurance. They usually include: search; verification; inquiry; and analysis procedures.

Examinations Engagements are of two types:

a. Assertion-Based Examination Engagements

(1) Report When CPAs are engaged to express an opinion as the result of an attestation engagement, they should state clearly whether: (1) management's assertion is presented (or fairly stated), in all material respects, based on (or in conformity with) the established/stated criteria, or (2) the subject matter of the assertion is based on (or in conformity with) the established or stated criteria in all material respects.

(2) Modifications Reports expressing a positive opinion on the reliability of an assertion may be qualified or modified for an aspect of the subject matter, assertion, or the engagement. In addition, examination reports may emphasize certain matters relating to the attest engagement, subject matter, or assertion. Remember, if deviations from the criteria or material misstatements exist, the practitioner should modify the report, directly expressing an opinion on the subject matter, rather than the assertion.

b. Direct Examination Engagements

SSAE 21 allows entities that do not provide an assertion about whether the underlying subject matter is in accordance with the criteria, to undergo an examination engagement, thus providing the public with confidence in information about the underlying subject matter. These engagements are called direct examination engagement.

Exhibit 14.1 - Examination Report on a Subject Matter

Independent Accountant's Report

[Appropriate Addressee]

We have examined the *[identify the subject matter—for example, the accompanying schedule of investment returns of XYZ Company for the year ended December 31, 20XX]*. XYZ Company's management is responsible for the schedule of investment returns. Our responsibility is to express an opinion based on our examination.

Our examination was conducted in accordance with attestation standards established by the AICPA. Those standards require that we plan and perform the examination to obtain reasonable assurance about whether *[identify the subject matter, for example, the schedule of investment returns]* is in accordance with (or based on) the criteria, in all material respects. An examination involves performing procedures to obtain evidence about *[identify the subject matter, for example, the schedule of investment returns]*. The nature, timing, and extent of the procedures selected depend on our judgment, including an assessment of the risks of material misstatement of *[identify the subject matter, for example, the schedule of investment returns]*, whether due to fraud or error. We believe that the evidence we obtained is sufficient and appropriate to provide a reasonable basis for our opinion.

We are required to be independent and to meet our other ethical responsibilities in accordance with relevant ethical requirements relating to the engagement.

[Include a description of significant inherent limitations, if any, associated with the measurement or evaluation of the subject matter against the criteria.] [Additional paragraphs may be added to emphasize certain matters relating to the attestation engagement or the subject matter.] In our opinion, *[identify the subject matter, for example, the schedule of investment returns of XYZ Company for the year ended December 31, 20XX, or the schedule of investment returns referred to above]*, is presented in accordance with (or based on) *[identify the criteria, for example, the ABC criteria set forth in Note 1]*, in all material respects. [Practitioner's signature]
[Practitioner's city and state] [Date of practitioner's report]

[Include a description of significant inherent limitations, if any, associated with the measurement or evaluation of the subject matter against the criteria.] [Additional paragraphs may be added to emphasize certain matters relating to the attestation engagement or the subject matter.] In our opinion, *[identify the subject matter, for example, the schedule of investment returns of XYZ Company for the year ended December 31, 20XX, or the schedule of investment returns referred to above]*, is presented in accordance with (or based on) *[identify the criteria, for example, the ABC criteria set forth in Note 1]*, in all material respects.

[Practitioner's signature]

[Practitioner's city and state]

[Date of practitioner's report]

2. **Review** A review report provides limited assurance. They usually include: inquiry and analysis procedures. The CPA's report states whether any information came to the CPA's attention on the basis of the work performed that indicates that the subject matter is materially misstated or divergent from criteria; or that assertions are not presented in all material respects in conformity with criteria. The report: (a) indicates that the work performed was less in scope than an examination, (b) disclaims a positive opinion on the assertions, and (c) contains a statement of limitations on the use of the report when it has been prepared in conformity with specified criteria that have been agreed upon by the specified parties because it is intended solely for specified parties.

Exhibit 14.2 - Review Report on an Assertion About a Subject Matter (Restricted)

Independent Accountant's Report

[Appropriate Addressee]

We have reviewed [identify the subject matter, for example, the accompanying schedule of investment returns of XYZ Company for the year ended December 31, 20XX]. XYZ Company's management is responsible for [identify the subject matter, for example, presenting the schedule of investment returns] in accordance with (or based on) [identify the criteria, for example, the ABC criteria set forth in Note 1]. Our responsibility is to express a conclusion on [identify the subject matter, for example, the schedule of investment returns] based on our review.

Our review was conducted in accordance with attestation standards established by the AICPA. Those standards require that we plan and perform the review to obtain limited assurance about whether any material modifications should be made to [identify the subject matter, for example, the schedule of investment returns] in order for it to be in accordance with (or based on) the criteria. The procedures performed in a review vary in nature and timing from and are substantially less in extent than, an examination, the objective of which is to obtain reasonable assurance about whether [identify the subject matter, for example, the schedule of investment returns] is in accordance with (or based on) the criteria, in all material respects, in order to express an opinion. Accordingly, we do not express such an opinion. Because of the limited nature of the engagement, the level of assurance obtained in a review is substantially lower than the assurance that would have been obtained had an examination been performed. We believe that the review evidence obtained is sufficient and appropriate to provide a reasonable basis for our conclusion.

We are required to be independent and to meet our other ethical responsibilities in accordance with relevant ethical requirements related to the engagement.

[Include a description of the work performed as a basis for the practitioner's conclusion.]

[Include a description of significant inherent limitations, if any, associated with the measurement or evaluation of the subject matter against the criteria.]

[Additional paragraphs may be added to emphasize certain matters relating to the attestation engagement or the subject matter.]

Based on our review, we are not aware of any material modifications that should be made to [identify the subject matter, for example, the accompanying schedule of investment returns of XYZ Company for the year ended December 31, 20XX], in order for it be in accordance with (or based on) [identify the criteria, for example, the ABC criteria set forth in Note 1].

[Practitioner's signature]

[Practitioner's city and state]

[Date of practitioner's report]

Editor's Note: Although suitable criteria exist for the subject matter, the report in exhibit 14.2 is restricted as to use because the criteria are available only to specified parties; otherwise, the paragraph restricting the use of the report would be omitted.

3. **Agreed-upon Procedures** No assurance is provided, but procedures and findings are listed. See next section for more detailed information.

Agreed-Upon Procedures

Definition

An agreed-upon procedures engagement is one in which a practitioner is engaged to issue a report of findings based on specific procedures performed on subject matter; a written assertion is not required. The nature, extent, and timing of procedures may vary widely. The specified parties assume responsibility for the sufficiency of the procedures since they best understand their own needs.

Required Conditions

To satisfy the agreement and responsibility requirements listed here, the practitioner ordinarily communicates directly with, and obtains affirming acknowledgments from, each specified party.

1. **Independence** The practitioner must be independent
2. **Responsibility** The client takes responsibility for the sufficiency of the agreed-upon procedures for their purpose, or a third party assumes responsibility for the subject matter
3. **Procedures and Criteria** The specified parties and the practitioner agree upon procedures to be performed by the practitioner, the criteria to be used in the determination of findings, and any materiality limits
4. **Measurement** The specific subject matter is subject to reasonably consistent measurement. The procedures are expected to result in reasonably consistent findings using the criteria. Evidential matter related to the specific subject matter is expected to exist to provide a reasonable basis for expressing findings in the practitioner's report
5. **Restricted Report** Use of the report is restricted to the specified parties
6. **Disclosure** For engagements involving prospective financial information, the prospective financial statements must include a summary of significant assumptions
7. **Specialist** The specified parties and the practitioner must agree explicitly on the involvement of a specialist.
8. **Internal Auditors and Other Personnel** The agreed-upon procedures are to be performed entirely by the practitioner and any assisting specialists; however, internal auditors or other client personnel may prepare schedules or provide other information for the practitioner's use in performing the procedures.

Exercise 14.2 - Agreed-Upon Procedures Engagement

When performing an agreed-upon procedures engagement, the practitioner

- a. And the specified parties should explicitly agree to the involvement of the specialist
- b. Is not required to be independent
- c. May issue a general-use report
- d. Makes the determination regarding materiality limits for reporting purposes

Answer a. is correct. The practitioner is required to be independent. Use of the report is required to be restricted to specified parties. Where applicable, the practitioner and the specified parties agree on any materiality limits for reporting purposes.

Report Components

The practitioner reports all findings from applying the agreed-upon procedures. The concept of materiality is inapplicable unless the specified parties and the practitioner have established a definition of materiality. The practitioner should **not** provide negative assurance about whether the subject matter or the assertion is fairly stated based on the criteria. For example, the practitioner should **not** include a statement in the report that “nothing came to my attention that caused me to believe that the [*identify subject matter*] is not presented based on [or the assertion is not fairly stated based on] [*identify criteria*].” The practitioner’s report should contain the following elements:

1. A title that includes the word independent to clearly indicate that it is the report of an independent accountant.
2. An appropriate addressee as required by the circumstances of the engagement.
3. Identification of the engaging party.
4. Identification of the subject matter to which the procedures have been applied.
5. Identification of the responsible party, including a statement that the responsible party is responsible for the subject matter. When the engaging party is not the responsible party and identification of the responsible party and its responsibility for the subject matter is based solely on representations received from the engaging party, the practitioner’s agreed-upon procedures report should include a statement to that effect.
6. A statement that the engaging party acknowledged that the procedures performed are appropriate to meet the intended purpose of the engagement.
7. An identification of the intended purpose of the engagement in sufficient detail to enable the user to understand the nature of the work performed.
8. A statement that the practitioner’s report may not be suitable for any other purpose
9. A statement that the procedures performed may not address all the items of interest to a user of the report and may not meet the needs of all users of the report and, as such, users are responsible for determining whether the procedures performed are appropriate for their purposes.
10. A statement that an agreed-upon procedures engagement involves the practitioner performing specific procedures that the engaging party has agreed to and acknowledged to be appropriate for the intended purpose of the engagement and reporting on findings based on the procedures performed.
11. A description of the procedures performed detailing the nature and extent, and if applicable, the timing, of each procedure.
12. A description of the findings from each procedure performed, including sufficient details on exceptions found.
13. If applicable, a description of any specified threshold established by the engaging party for reporting exceptions.
14. A statement that the agreed-upon procedures engagement was conducted in accordance with attestation standards established by the AICPA.
15. A statement that the practitioner was not engaged to and did not conduct an examination or review, the objective of which would be the expression of an opinion or conclusion, respectively, on the subject matter.
16. A statement that the practitioner does not express such an opinion or conclusion.
17. A statement that had the practitioner performed additional procedures; other matters might have come to the practitioner’s attention that would have been reported.
18. A statement that the practitioner is required to be independent of the responsible party and to meet the practitioner’s other ethical responsibilities, in accordance with the relevant ethical requirements relating to the agreed-upon procedures engagement.
19. If applicable, a description of the nature of the assistance provided by a practitioner’s external specialist, as discussed in paragraphs
20. When applicable, reservations or restrictions concerning procedures or findings.
21. The manual or printed signature of the practitioner’s firm.
22. The city and state where the practitioner’s report is issued.
23. The date of the report. The practitioner’s report should be dated no earlier than the date on which the practitioner completed the procedures and determined the findings

Report on Agreed-Up Procedures

Independent Accountant's Report on Applying Agreed-Up Procedures

[Appropriate Addressee]

We have performed the procedures enumerated below on [identify the subject matter, for example, the accompanying Statement of Investment Performance Statistics of XYZ Fund for the year ended December 31, 20X1]. [The responsible party, for example, XYZ Fund] is responsible for [the subject matter].

[The engaging party, for example, XYZ Fund] has agreed to and acknowledged that the procedures performed are appropriate to meet the intended purpose of [identify the intended purpose of the engagement, for example, assisting users in understanding the Statement of Investment Performance Statistics of XYZ Fund for the year ended December 31, 20X1]. This report may not be suitable for any other purpose. The procedures performed may not address all the items of interest to a user of this report and may not meet the needs of all users of this report and, as such, users are responsible for determining whether the procedures performed are appropriate for their purposes.

The procedures and the associated findings are as follows:

[Include paragraphs to describe the procedures performed detailing the nature and extent, and if applicable, the timing, of each procedure and to describe the findings from each procedure performed, including sufficient details on exceptions found.]

We were engaged by [the engaging party, for example, XYZ Fund] to perform this agreed-upon procedures engagement and conducted our engagement in accordance with attestation standards established by the AICPA. We were not engaged to and did not conduct an examination or review engagement, the objective of which would be the expression of an opinion or conclusion, respectively, on [identify the subject matter, for example, the accompanying Statement of Investment Performance Statistics of XYZ Fund for the year ended December 31, 20X1]. Accordingly, we do not express such an opinion or conclusion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

We are required to be independent of XYZ Fund and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements related to our agreed-upon procedures engagement.

[Additional paragraphs may be added to describe other matters.]

[Signature of the practitioner's firm]

[City and state where the practitioner's report is issued]

[Date of the practitioner's report]

Other Requirements

- 1. Explanatory Language** The practitioner may include explanations about issues such as the following: (a) disclosures of stipulated facts, assumptions, or interpretations used in applying procedures; (b) condition of records, controls, or data; (c) a statement that the practitioner has no responsibility to update the report.
- 2. Scope Limitations** When the situation imposes restrictions on the performance of procedures, the practitioner should obtain agreement from the specified parties to modify the agreed-upon procedures, describe any restrictions in the report, or withdraw from the engagement.
- 3. Outside Knowledge** The practitioner need not perform additional procedures, but if a matter comes to the practitioner's attention that significantly contradicts the subject matter, the practitioner should include this matter in the report.

- 4. Request to Change Engagement Type** If the practitioner concludes, based on professional judgment, that there is reasonable justification to change the engagement, and provided the practitioner complies with the standards applicable to that engagement, the practitioner issues the report appropriate to the new engagement type. This report should not include reference to either the original engagement or performance limitations that resulted in a different engagement.

Financial Forecasts and Projections

Guidance

AT 301, *Financial Forecasts and Projections*, establishes guidance concerning performance and reporting for engagements to examine, compile, or apply agreed-upon procedures to prospective financial statements (PFS). Pro Forma financial statements show what past financial results would have been if something had been different; they are not considered to be PFS.

Definitions

- 1. Financial Forecast** PFS that present, to the best of the responsible party's knowledge and belief, an entity's expected financial position, results of operations, and cash flows. A financial forecast may be expressed in specific monetary amounts as a single-point estimate of forecasted results or as a range.
- 2. Financial Projection** PFS that present, to the best of the responsible party's knowledge and belief, given one or more hypothetical assumptions, an entity's expected financial position, results of operations, and cash flows. A financial projection sometimes is prepared to present one or more hypothetical courses of action for evaluation. It answers the question, "What would happen if...?" It may also contain a range.

Restrictions

- 1. General Use** Refers to the use of PFS by persons with whom the responsible party is not negotiating directly. Since users are unable to ask questions of the responsible party, the presentation most useful to them is one that portrays, to the best of the responsible party's knowledge and belief, the expected results. *Only a financial forecast is appropriate for general use.*
- 2. Limited Use** Refers to the use of PFS by the responsible party alone or by the responsible party and third parties with whom the responsible party is negotiating directly. Third-party recipients of PFS intended for limited use can ask questions of the responsible party and directly negotiate terms with it. Any type of PFS that would be useful in the circumstances normally is appropriate for limited use. The presentation may be a financial forecast or a financial projection.

Report Components

1. **Formats** The practitioner may perform a compilation report, an examination (usually to be used by a third party), or an agreed-upon procedures report. A review of PFS is not permitted.
2. **Common Elements** Standard reports for the three engagements share some elements:
 - a. A caveat that the prospective results might not be achieved
 - b. A statement that the CPA assumes no responsibility to update the report for events and circumstances occurring after the date of the report
 - c. The practitioner's signature
 - d. The date of the completion of the CPA's procedures
3. **Compilation of PFS** Independence is **not** necessary for a compilation engagement.
 - a. A compilation of PFS involves:
 - (1) Assembling the PFS based on the responsible party's assumptions
 - (2) Performing the required compilation procedures, including reading the statements and considering whether they are appropriate and are presented in conformity with AICPA presentation guidelines
 - (3) Issuing a compilation report.
 - b. **Limited Procedures** A compilation is not intended to provide assurance on the PFS or the assumptions underlying such statements. Because of the limited nature of the CPA's procedures, a compilation does not provide assurance that the CPA will become aware of significant matters that might be disclosed by more extensive procedures.
 - c. **Assumptions** Since this summary is essential to the reader's understanding of PFS, the CPA should **not** compile PFS that exclude disclosure of the summary of significant assumptions. Also, the CPA should **not** compile a financial projection that omits:
 - (1) An identification of the hypothetical assumptions
or
 - (2) A description of the limitations on the usefulness of the presentation.
 - d. **Obviously Inappropriate** The practitioner should consider when representations or other information appear to be obviously inappropriate, incomplete, etc., and if so, should attempt to clarify the matter. If the matter is not clarified, the practitioner ordinarily withdraws from the engagement.
4. **Compilation Reports**
 - a. In addition to the previously discussed elements, the standard compilation report includes:
 - (1) Identification of the PFS presented by the responsible party
 - (2) A statement that the CPA has compiled the PFS in accordance with attestation standards established by the AICPA
 - (3) A statement that a compilation is limited in scope and does not enable the CPA to express an opinion or any other form of assurance on the PFS or the assumptions

Exhibit 14.4 - Compilation Report on a Forecast / Projection

We have compiled the accompanying forecasted [projected] balance sheet, statements of income, retained earnings, and cash flows of XYZ Company as of December 31, 20X1, and for the year then ending, in accordance with attestation standards established by the American Institute of Certified Public Accountants. [If for a projection add: The accompanying projection was prepared for (state special purpose, for example, "the purpose of negotiating a loan to expand XYZ Company's plant").]

A compilation is limited to presenting in the form of a forecast [projection] information that is the representation of management and does not include evaluation of the support for the assumptions underlying the projection. We have not examined the forecast [projection] and, accordingly, do not express an opinion or any other form of assurance on the accompanying statements or assumptions. Furthermore, [If for a projection, add: even if (describe hypothetical assumption, for example, "the loan is granted and the plant is expanded,")] there will usually be differences between the forecasted [projected] and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

<Additional paragraph for a projection>

The accompanying projection and this report are intended solely for the information and use of [identify specified parties, for example, "XYZ Company and DEF National Bank"] and is not intended to be and should not be used by anyone other than these specified parties.

[Signature]

[Date]

- b. **Projection Presentation** The practitioner's report should include a separate paragraph that describes the limitations on the usefulness of the presentation.
 - c. **Range** When the PFS contain a range, the practitioner's report also should include a separate paragraph that states that the responsible party has elected to portray the expected results of one or more assumptions as a range.
 - d. **Emphasis** In some circumstances, a CPA may wish to expand the report to emphasize a matter regarding the PFSs. Such information may be presented in a separate paragraph of the CPA's report. However, the CPA should exercise care that emphasizing such a matter does not give the impression that the CPA is expressing assurance or expanding the degree of responsibility the CPA is taking regarding such information.
 - e. **Historical Financial Information** PFS may be included in a document that also includes historical financial statements (HFS) with a related practitioner's report. Additionally, HFS may be summarized and presented with PFS for comparative purposes.
 - f. **Independence Not Required** A CPA may compile PFS for an entity with respect to which a CPA is not independent. When the CPA is not independent, the CPA should include the following as a separate paragraph in the report, "We are not independent with respect to XYZ Company." The CPA is permitted, but not required, to disclose (in the same paragraph) the reason(s) for the independence impairment. If the CPA elects to do this, *all* the reasons should be included.
5. **Examination of PFS** An examination of PFS is substantially more in scope and responsibility than a compilation or an agreed-upon procedures engagement. The practitioner must be independent, and follow the general, fieldwork, and reporting standards outlined in AT 101 as applicable to examination engagements.
- a. **Examination Reports** As a result of the examination, the CPA has a basis for reporting on whether, in the CPA's opinion:
 - (1) The assumptions provide a reasonable basis for the responsible party's forecast or projection, given the hypothetical assumptions
 - (2) Whether the PFS are presented in accordance with AICPA guidelines.

- b. **Standard Report** In addition to the previously listed elements, the CPA's standard report on an examination of PFS includes the following:
- (1) A title which includes independent; a signature, and a date
 - (2) Identification of the PFS presented
 - (3) Identification of the responsible parties and a statement that the PFS are the responsibility of said parties
 - (4) A statement that the practitioner's responsibility is to express an opinion on the PFS based on an examination
 - (5) A brief description of the nature of an examination of PFS
 - (6) The CPA's opinion that the PFS are presented in accordance with AICPA presentation guidelines and that the underlying assumptions provide a reasonable basis for the forecast (or projection, given the hypothetical assumptions).
- c. **Projection** The CPA should express an opinion on whether the assumptions provide a reasonable basis for the projection given the hypothetical assumptions. A reference should be included to the hypothetical assumption(s), and the report should include a separate paragraph that limits the use to specified parties.
- d. **Emphasis** The practitioner may wish to emphasize a matter regarding the PFS, but issue an unmodified opinion. The practitioner may present other information and comments, such as explanatory comments or other informative material, in a separate paragraph of the report.
- e. **Evaluation Based in Part on Report of Another Accountant** When the principal practitioner decides to refer to the report of another CPA as a basis, in part, for the principal's own opinion, the principal practitioner should disclose that fact in stating the scope of the examination and refer to the report of the other CPA in expressing the opinion. Such a reference indicates the division of responsibility for the performance of the examination.
- f. **Part of Larger Engagement** When the practitioner's examination of PFS is part of a larger engagement, for example, a financial feasibility study or business acquisition study, it is appropriate to expand the report on the examination of the PFS to describe the entire engagement.

Exhibit 14.5 - Standard Report on an Examination of Forecast / Projection

Independent Accountant's Report

We have examined the accompanying forecasted [projected] balance sheet, statements of income, retained earnings, and cash flows of XYZ Company as of December 31, 20X1, and for the year then ending. XYZ Company is responsible for the forecast [*projection*]. Our responsibility is to express an opinion on the forecast [*projection*] based on our examination.

Our examination was made in accordance with attestation standards established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as we considered necessary to evaluate both the assumptions used by management and the preparation and presentation of the forecast [*projection*]. We believe our examination provides a reasonable basis for our opinion.

<Opinion paragraph for a forecast>

In our opinion, the accompanying forecast is presented in conformity with guidelines for presentation of a forecast established by the American Institute of Certified Public Accountants, and the underlying assumptions provide a reasonable basis for management's forecast. However, there will usually be differences between the forecasted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

<Opinion paragraph for a projection>

In our opinion, the accompanying projection is presented in conformity with guidelines for presentation of a projection established by the American Institute of Certified Public Accountants, and the underlying assumptions provide a reasonable basis for management's projection [*describe the hypothetical assumption, for example, "assuming the granting of the requested loan to expand XYZ Company's plant as described in the summary of significant assumptions."*]. However, even if [*describe hypothetical assumption, for example, "the loan is granted and the plant is expanded,"*] there will usually be differences between the projected and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

<Additional paragraph for a projection report>

The accompanying projection and this report were prepared for [*identify specified parties, for example, "XYZ Company and DEF National Bank"*] and are not intended to be and should not be used by anyone other than these specified parties.

[Signature]

[Date]

- g. Qualified Opinion** In a qualified report, the CPA states, in a separate paragraph, all the substantive reasons for modifying the opinion, and describes the departure from AICPA presentation guidelines. The opinion includes the words *except* or *exception* as the qualifying language and refers to the separate explanatory paragraph.
- h. Adverse Opinion** In an adverse opinion, the CPA states, in a separate paragraph, all the substantive reasons for the adverse opinion. The opinion should state that the presentation is not in conformity with presentation guidelines and should refer to the explanatory paragraph. When applicable, the opinion paragraph also should state that, in the accountant's opinion, the assumptions do not provide a reasonable basis for the prospective financial statements.
 - (1)** If the presentation, including the summary of significant assumptions, fails to disclose assumptions that, at the time, appear to be significant, the CPA should describe the assumptions in the report and issue an adverse opinion.

- (2) The CPA should not examine a presentation that omits all disclosures of assumptions. Also, the CPA should not examine a financial projection that omits:
- (a) An identification of the hypothetical assumptions
 - or
 - (b) A description of the limitations on the usefulness of the presentation.
- i. **Disclaimer of Opinion** The CPA's report should indicate, in a separate paragraph, the respects in which the examination did not comply with standards for an examination. The CPA should state that the scope of the examination was not sufficient to enable an opinion to be expressed concerning the presentation or the underlying assumptions, and the CPA's disclaimer of opinion should include a direct reference to the explanatory paragraph. When there is a scope limitation and the CPA also believes that there are material departures from the presentation guidelines, those departures should be described in the CPA's report.

6. Agreed-Upon Procedures

- a. **Standards** The guidance in AT 101 (including general, fieldwork, and reporting standards) and AT 201 applies to engagements to apply agreed-upon procedures to PFS. This includes the extent of procedures and agreement among the parties regarding the procedures.
- b. **Conditions** A practitioner may accept an engagement to apply agreed-upon procedures to PFS provided that:
- (1) The practitioner is independent
 - (2) The practitioner and the specified users agree upon the procedures and criteria
 - (3) The specified users take responsibility for the sufficiency of the agreed-upon procedures for their purposes
 - (4) The PFS include a summary of significant assumptions
 - (5) The PFS are subject to reasonably consistent evaluation against criteria that are suitable and available to the specified parties
 - (6) The procedures are expected to result in reasonably consistent findings using the criteria
 - (7) Evidential matter related to the PFS is expected to exist to provide a reasonable basis for expressing the findings in the practitioner's report
 - (8) Where applicable, the practitioner and the specified user agree on any materiality limits for reporting purposes
 - (9) Use of the report is restricted to the specified parties.
- c. **Reports on Results** When the CPA reports on the results of applying agreed-upon procedures, the CPA should not express any form of negative assurance on the PFS. In addition to the previously discussed elements, the practitioner's report must include:
- A title that includes the word independent
 - Identification of the specified parties
 - Reference to the PFS and the character of the engagement
 - A statement that the procedures performed were those agreed to by the specified parties identified in the report
 - Identification of the responsible party and a statement that the PFS are the responsible party's responsibility

- A statement that the engagement was conducted in accordance with attestation standards established by the AICPA
- A statement that the sufficiency of the procedures is solely the responsibility of the specified parties and a disclaimer of responsibility for the sufficiency of those procedures
- A list of (or reference to) procedures performed and related findings
- Where applicable, a description of any agreed-upon materiality limits
- A statement that the practitioner was not engaged to and did not conduct an examination of PFS
- A disclaimer of opinion on whether the presentation of the PFS is in conformity with AICPA presentation guidelines and on whether the underlying assumptions provide a reasonable basis for the forecast or a reasonable basis for the projection given the hypothetical assumptions
- A statement that if the practitioner had performed additional procedures, other matters might have come to his or her attention that would have been reported
- A restriction on the use of the report, because it is intended to be used solely by the specified parties, and should not be used by others
- Where applicable, reservations or restrictions concerning procedures or findings
- Where applicable, a description of assistance provided by a specialist

Pro Forma Financial Information

Purpose

Pro forma financial information is used to show what the significant effects on historical financial information might have been if a consummated or proposed transaction or event had occurred at an earlier date. Pro forma financial information generally is used to show the effects of transactions such as a business combination, a change in capitalization, the disposition of a significant portion of a business, a change in the form of business organization, or the proposed sale of securities and the application of proceeds.

1. **Examination Objective** Examination procedures applied to pro forma financial information are to provide reasonable assurance as to whether the following exists:
 - a. Management's assumptions provide a reasonable basis for presenting the significant effects directly attributable to the underlying transaction or event
 - b. The related pro forma adjustments give appropriate effect to those assumptions
 - c. The pro forma column reflects the proper application of those adjustments to the historical financial statements
2. **Review Objective** Review procedures are to provide negative assurance as to whether any information came to the CPA's attention to cause a belief that: (a) management's assumptions do not provide a reasonable basis for presenting the significant effects directly attributable to the transaction or event; (b) the related pro forma adjustments do not give appropriate effect to those assumptions; and (c) the related pro forma column does not reflect the proper application of those adjustments to the historical financial statements.

Guidance

Engagements to report on an examination or review of pro forma financial information are covered by AT 101 and AT 401, *Reporting on Pro Forma Financial Information*.

Requirements

A CPA may agree to report on an examination or a review of pro forma financial information under certain conditions. The presentation should indicate that the pro forma information should be read in conjunction with the historical data, make reference to the financial statements from which the historical data is derived, and state

whether those statements were audited or reviewed. The presentation also should state that the pro forma financial information does not necessarily indicate the results that would have been attained had the transaction actually taken place earlier.

1. **Procedures** The procedures the CPA applies to the assumptions and pro forma adjustments for either an examination or a review engagement, other than those applied to the historical financial statements, include:
 - a. Obtain an understanding of the underlying transaction or event; obtain a level of knowledge of each significant constituent part of the combined entity in a business combination; and discuss with management its assumptions regarding the effects of the transaction or event.
 - b. Evaluate whether pro forma adjustments are included for all significant effects directly attributable to the transaction or event.
 - c. Obtain sufficient evidence in support of adjustments. The evidence required to support the level of assurance given is a matter of professional judgment.
 - d. Evaluate whether management's assumptions that underlie the pro forma adjustments are presented in a sufficiently clear and comprehensive manner.
 - e. Determine that computations of pro forma adjustments are mathematically correct.
 - f. Obtain written representations from management acknowledging responsibility for the assumptions used in determining the pro forma adjustments.
2. **Report** The report on pro forma financial information may be added to the CPA's report on historical financial information, or it may appear separately.
 - a. **Contents** In addition to the previously listed items, a report on pro forma financial information includes the following: a separate paragraph explaining the objective of pro forma financial information and its limitations; and reference to the financial statements from which the historical financial information is derived and any modification in the practitioner's report on the historical financial information.
 - b. **Date** The practitioner's report on pro forma financial information should be dated as of the completion of the appropriate procedures. If the reports are combined and the date of completion of the procedures for the examination or review of the pro forma financial information is after the date of completion of the fieldwork for the audit or review of the historical financial information, the combined report should be dual-dated.
 - c. **Modifications** Restrictions on the scope of the engagement, significant uncertainties about the assumptions that could affect the transaction or event materially, reservations about the propriety of the assumptions and the conformity of the presentation with those assumptions (including inadequate disclosure of significant matters), or other reservations may require the CPA to qualify the opinion, render an adverse opinion, disclaim an opinion, or withdraw from the engagement. The CPA should disclose all substantive reasons for any report modifications. Uncertainty as to whether the transaction or event will be consummated ordinarily would not require a report modification.
 - d. **Examination** In addition to the previously listed elements, an examination report also includes the following:
 - (1) **Reference** A statement that the historical financial statements were audited.
 - (2) **Responsibility** A statement that the practitioner's responsibility is to express an opinion on the pro forma financial information based on his or her examination.
 - (3) **Standards** A statement that the examination was made in accordance with attestation standards established by the AICPA, and accordingly, included such procedures as the practitioner considered necessary in the circumstances.

(4) **Basis** A statement that the practitioner believes the examination provides a reasonable basis for his or her opinion.

(5) **Opinion** The practitioner's opinion as to whether management's assumptions provide a reasonable basis for presenting the significant effects directly attributable to the transaction or event, whether the related pro forma adjustments give appropriate effect to those assumptions, and whether the pro forma column reflects the proper application of those adjustments to the historical financial statements.

e. **Review** In addition to the previously listed elements, a review report also includes the following:

(1) **Reference** A statement as to whether the historical financial statements were audited or reviewed.

(2) **Disclaimer** A statement that a review is substantially less in scope than an examination, the objective of which is the expression of an opinion on the pro forma financial information, and accordingly, the practitioner does not express such an opinion.

3. **Conclusion** The practitioner's conclusion as to whether any information came to the CPA's attention to cause a belief that management's assumptions do not provide a reasonable basis for presenting the significant effects directly attributable to the transaction or event, or that the related pro forma adjustments do not give appropriate effect to those assumptions, or that the pro forma column does not reflect the proper application of those adjustments to the historical financial statements.

Exhibit 14.6 - Report on an Examination of Pro Forma Financial Information

Independent Accountant's Report

We have examined the pro forma adjustments reflecting the transaction [*or event*] described in Note 1 and the application of those adjustments to the historical amounts in [*the assembly of*] the accompanying pro forma condensed balance sheet of X Company as of December 31, 20X1, and the pro forma condensed statement of income for the year then ended. The historical condensed financial statements are derived from the historical financial statements of X Company, which were audited by us, and of Y Company, which were audited by other accountants, appearing elsewhere herein [*or incorporated by reference*]. Such pro forma adjustments are based upon management's assumptions described in Note 2. X Company's management is responsible for the pro forma financial statements. Our responsibility is to express an opinion on the pro forma financial information based on our examination.

Our examination was made in accordance with attestation standards established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as we considered necessary under the circumstances. We believe our examination provides a reasonable basis for our opinion.

The objective of this pro forma financial information is to show what the significant effects on the historical financial information might have been had the transaction [*or event*] occurred at an earlier date. However, the pro forma condensed financial statements are not necessarily indicative of the results of operations or related effects on financial position that would have been attained had the above-mentioned transaction [*or event*] occurred earlier.

[*Additional paragraph(s) may be added to emphasize certain matters relating to the engagement.*]

In our opinion, management's assumptions provide a reasonable basis for presenting the significant efforts directly attributable to the above-mentioned transaction [*or event*] described in Note 1, the related pro forma adjustments give appropriate effect to those assumptions, and the pro forma column reflects the proper application of those adjustments to the historical financial statement amounts in the pro forma condensed balance sheet as of December 31, 20X1, and the pro forma condensed statement of income for the year then ended.

[*Signature*]

[*Date*]

Exhibit 14.7 - Report on a Review of Pro Forma Financial Information

Independent Accountant's Report

We have reviewed the pro forma adjustments reflecting the transaction [*or event*] described in Note 1 and the application of those adjustments to the historical amounts in [*the assembly of*] the accompanying pro forma condensed balance sheet of X Company as of March 31, 20X2, and the pro forma condensed statement of income for the three months then ended. These historical condensed financial statements are derived from the historical unaudited financial statements of X Company, which were reviewed by us, and of Y Company, which were reviewed by other accountants, appearing elsewhere herein [*or incorporated by reference*]. Such pro forma adjustments are based on management's assumptions as described in Note 2. X Company's management is responsible for the pro forma financial statements.

Our review was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. A review is substantially less in scope than an examination, the objective of which is the expression of an opinion on management's assumptions, the pro forma adjustments, and the application of those adjustments to historical financial information. Accordingly, we do not express such an opinion.

<Same third paragraph as in an examination report.>

[Additional paragraph(s) may be added to emphasize certain matters relating to the engagement.]

Based on our review, nothing came to our attention that caused us to believe that management's assumptions do not provide a reasonable basis for presenting the significant effects directly attributable to the above-mentioned transaction [*or event*] described in Note 1, that the related pro forma adjustments do not give appropriate effect to those assumptions, or that the pro forma column does not reflect the proper application of those adjustments to the historical financial statement amounts in the pro forma condensed balance sheet as of March 31, 20X2, and the pro forma condensed statement of income for the three months then ended.

[Signature]

[Date]

Examination of Internal Control Over Financial Reporting

AT 501, An Examination of an Entity's Internal Control Over Financial Reporting That Is Integrated with an Audit of Its Financial Statements, establishes requirements and provides guidance for the performance of an examination of a nonissuer's internal control over financial reporting (internal control) that is integrated with an audit of financial statements. (An auditor should **not** accept an engagement to review an entity's internal control or a written assertion thereon.) It aligns the definitions and related guidance for evaluating deficiencies in internal control with PCAOB AS 5, An Audit of Internal Control Over Financial Reporting That is Integrated with an Audit of Financial Statements (see chapter 11).

Overview

1. **Applicability** AT 501 does not provide guidance for the following engagements:
 - a. As covered under AT 101, *Attest Engagements*:
 - b. Performance of agreed-upon procedures on controls covered under AT 201, *Agreed-Upon Procedures Engagements*
 - c. Examining controls over compliance with laws and regulations covered under AT 601, *Compliance Attestation*
 - d. Reporting on controls at a service organization covered under AT 801, *Reporting on Controls at a Service Organization*

See the supplemental material at the end of this chapter for the definitions of relevant terms for this topic.

Examination Requirements

Management must: (1) accept responsibility for the effectiveness of the entity's internal control; (2) evaluate the effectiveness of the entity's internal control using suitable and available criteria; (3) support its assertion about the effectiveness of the entity's internal control with sufficient appropriate evidence, including documentation of the controls and their objectives and evidence of monitoring activities; and (4) provide its assertion about the effectiveness of the entity's internal control in a report that accompanies the audit report.

Material Weaknesses

If one or more material weaknesses exist, an entity's internal control cannot be considered effective, thus the auditor must obtain sufficient appropriate evidence to obtain reasonable assurance about whether material weaknesses exist as of the date specified in management's assertion. There may be a material weakness in internal control even when financial statements are not materially misstated. An auditor is not required to search for deficiencies that are less severe than a material weakness.

Integrating the Examination with the Financial Statement Audit

1. **Significant Accounts and Disclosures and Their Relevant Assertions** The significant accounts and disclosures and their relevant assertions and the risk factors used to identify them are the same in the examination of internal control (examination) as in an audit of financial statements (audit).
2. **Tests of Controls** The tests of controls should be designed to achieve the objectives of both engagements simultaneously, i.e., to obtain sufficient appropriate evidence to support the auditor's opinion on internal control as well as the auditor's risk assessment for purposes of the audit. As previously mentioned, for the purposes of the audit, the auditor is not required to test the controls of all relevant assertions as is required in the examination. Consideration of the results of the additional tests of controls performed for the purposes of the examination may affect the auditor's decisions about the nature, timing and extent of substantive procedures and further tests of controls for the purposes of the audit. Obviously, this would be particularly true if deficiencies were identified in the examination.
3. **Substantive Procedures** Likewise, the results of substantive procedures performed for purposes of the audit should be evaluated to determine their effect on the auditor's risk assessments regarding the testing

necessary to form a conclusion about the effectiveness of a control in the examination. Results of substantive tests of particular interest include those related to fraud, illegal acts, related-party transactions, and those that detect misstatements or indicate management bias in making accounting estimates or selecting accounting principles.

4. **Period End Reporting Process** As part of the examination, the auditor should evaluate the procedures that make up the period end reporting process because of its importance to financial reporting and the integrated approach.
5. **Risk Assessment and Materiality** The same materiality should be used for planning and performing both engagements and the same risk assessment process supports both.
6. **Fraud Risk Assessment** The results of the fraud risk assessment for the purposes the audit should be incorporated into the examination. The auditor should consider whether the identified risks due to fraud and inappropriate management override of other controls are sufficiently addressed by the internal control system.
7. **As of Date or Period Covered** The date specified in management's assertion (the as of date of the examination) should correspond to the balance sheet date of the period covered by the financial statements. If management chooses an as of date for the examination that is different than the end of the entity's fiscal year, the examination and the audit should still be integrated. If the auditor is engaged to examine the effectiveness of internal control for a period of time (rather than an as of date), the examination should be integrated with an audit that covers the same period.
8. **Audit Report Date** Because the examination is integrated with the audit, the dates of the reports should be the same.

Communications

Significant deficiencies and material weaknesses should be communicated, in writing by the audit report release date, to the entity's management and those charged with governance, including those previously communicated, but not remediated. In the case where the nature of some matters directs their early communication, even if such significant deficiencies or material weaknesses are remediated during the audit, they should still be included in this formal written communication.

Adverse Opinion

If there a material weakness, the auditor should express an adverse opinion. Under these circumstances, the auditor is prohibited from expressing an opinion on management's assertion and should report directly on the effectiveness of internal control. The auditor should determine the effect of an adverse opinion on the auditor's opinion on the financial statements and disclose whether the auditor's opinion on the financial statements was affected by the material weakness. The adverse report should include:

1. A definition of material weakness
2. A statement that one or more material weaknesses have been identified and an identification of the material weaknesses described in management's report; the audit report does not need to include a description of the material weaknesses as long as each material weakness is included and fairly presented in all material respects in management's report
3. If management's report does not include a fair presentation of all material weaknesses, the audit report should include a statement that one or more material weaknesses have been identified and not included in management's report, along with a description of all such material weaknesses which contains specific information about the nature of each, and its actual and potential effect on the presentation of the entity's financial statements.

Disclaimer of Opinion or Withdrawal

1. If there are restrictions on the scope of an engagement, for example, if management refuses to provide written representations, the auditor should either withdraw from the engagement or disclaim an opinion.

The auditor may issue the disclaimer of opinion as soon as the auditor concludes that the scope limitation will prevent the auditor from obtaining the reasonable assurance necessary to express an opinion. No additional work is required.

2. The auditor should disclaim an opinion when the auditor discovers a material weakness subsequent to the as of date of the examination, but before the date of the audit report that existed as of the date in management's assertion and whose effect on internal control cannot be determined. (If its effect can be determined, the auditor should issue an adverse opinion.)
3. A disclaimer of opinion should include: a statement that the auditor does not express an opinion on the effectiveness of internal control; an explanation in a separate paragraph that includes the substantive reasons for the disclaimer. The auditor should not identify the procedures that were performed nor include the statements describing the characteristics of an examination.

Compliance Attestation

AT 601, *Compliance Attestation*, provides guidance for engagements related to an entity's compliance with requirements of specified laws, regulations, rules, contracts, or grants, as well as the effectiveness of an entity's internal control (IC) over compliance with specified requirements. An attest engagement must comply with the general, fieldwork, and reporting standards delineated in AT 101 as well as specific standards established in AT 601.

Applicability

CPAs may be engaged to perform agreed-upon procedures to assist users in evaluating compliance with specified requirements (or related assertions) and/or the effectiveness of an entity's IC over compliance. These engagements also are subject to the requirements of AT 201. CPAs also may be engaged to examine, but not review, an entity's compliance with specified requirements, or related written assertions. CPAs may provide nonattest services connected with compliance; however, these services adhere to professional consulting standards, rather than SSAE.

1. **Agreed-Upon Procedures** The objective is to present specific findings to assist users in evaluating an entity's assertion about compliance with specified requirements or about the effectiveness of an entity's IC over compliance based on procedures agreed-upon by the report users. The CPA's procedures generally may be as limited or as extensive as the specified parties desire as long as the specified users participate in establishing the procedures to be performed, and take responsibility for the adequacy of such procedures for their purposes. Prior to performing procedures, the practitioner should obtain an understanding of the specified compliance requirements.
2. **Examination** The objective is to express an opinion on an entity's compliance with specified requirements (or related assertion) based on specified criteria. To express such an opinion, the practitioner accumulates sufficient evidence regarding the entity's compliance with specified requirements, thereby limiting attestation risk to an appropriately low level. Among other procedures, the practitioner considers subsequent events. The practitioner considers issues that parallel those in a financial statement audit, but the perspective may be different. Some of these issues are risk, materiality, planning, professional skepticism, relevant internal controls and internal audit functions, use of specialists, and obtaining sufficient evidence.
3. **Conditions for Engagement** For both types of engagements, the responsible party must accept responsibility for the entity's compliance with specified requirements and the effectiveness of IC over compliance, and provide a written assertion about compliance with specified requirements or IC over compliance in either: (a) a separate report to accompany the practitioner's report; or (b) a representation letter to the practitioner.
 - a. **Agreed-Upon Procedures** The responsible party evaluates compliance with specified requirements or the effectiveness of the entity's IC over compliance.
 - b. **Examinations** The responsible party evaluates compliance with specified requirements, and sufficient evidential matter exists, or could be developed, to support that evaluation.

Report Components

The practitioner modifies the report if: (1) material noncompliance with specified requirements exists; (2) a restriction on the engagement scope exists; or (3) the practitioner refers to another practitioner's report as the basis, in part, for the report.

1. When a situation imposes restrictions on the engagement scope, the practitioner attempts to obtain agreement to modify the procedures. If such agreement is not obtained, the practitioner should describe the restrictions in the report or withdraw from the engagement.
2. The practitioner has no obligation to perform beyond the agreed-upon procedures and no responsibility to perform procedures to detect noncompliance in the subsequent period, beyond obtaining the responsible party's representation about noncompliance in the subsequent period.
3. The practitioner's report should not provide negative assurance about whether management's assertion is fairly stated.

Management's Discussion & Analysis

Management is responsible for the preparation of management's discussion & analysis (MD&A). AT 701, *Management's Discussion and Analysis*, provides specific guidance to CPAs related to the performance of an attest engagement with respect to MD&A prepared pursuant to Securities and Exchange Commission (SEC) regulations. This guidance does not change an auditor's responsibility in a financial statement audit, or apply to situations where CPAs provide recommendations rather than assurance. (SSAE require an auditor to read the MD&A and consider whether it is materially inconsistent with information appearing in the financial statements.) A practitioner engaged to examine or review MD&A complies with AT 101 plus the specific standards in AT 701. A practitioner engaged to perform agreed-upon procedures on MD&A follows the guidance in AT 201.

Objectives

The objective is to report on MD&A taken as a whole. An examination of MD&A provides users with an independent opinion regarding whether: (a) the presentation meets SEC criteria; (b) the historical financial information is derived accurately from the financial statements; and (c) the underlying information and assumptions provide a reasonable basis for the disclosures contained therein. A review of MD&A provides users and preparers with negative assurance concerning such matters.

Engagement Acceptance

A CPA may perform an examination or review of MD&A for an annual period, an interim period, or a combined annual and interim period. A base knowledge of the entity gained through a financial statement audit is necessary to provide the CPA with sufficient knowledge to evaluate the results of procedures. For nonpublic entities, the CPA also must receive a written assertion from management that MD&A was prepared using SEC criteria.

1. **Annual Period** A CPA may accept an engagement to examine or review MD&A of an entity for an annual period, provided the practitioner audits the financial statements for at least the latest period to which MD&A relates and the financial statements for the other periods covered by MD&A have been audited.
2. **Review of Interim Period** A CPA may accept an engagement to review MD&A for an interim period provided that MD&A for the most recent fiscal year has been (or will be) examined or reviewed (by either the CPA or a predecessor) and the CPA performs either an audit of the interim financial statements or a review.
3. **Predecessor** If a predecessor audited prior period financial statements, the successor must acquire sufficient knowledge of the entity and apply appropriate procedures relating to prior years included in the MD&A presentation.

Scope

The practitioner considers the following as well as historical financial information:

1. **Pro Forma Information** The guidance in AT 401 when performing procedures with respect to any pro forma information, even if MD&A indicates that certain information is derived from unaudited financial statements
2. **External Information** For example, debt ratings of a rating agency
3. **Forward-Looking Information** Tested only for the purpose of expressing an opinion or providing limited assurance on MD&A taken as a whole; the CPA considers whether cautionary language concerning achievability is included
4. **Voluntary Information** When the entity includes other information in MD&A required by other SEC regulations, the CPA also considers those other SEC criteria in subjecting such information to procedures

Engagement Procedures

The CPA obtains an understanding of the SEC criteria for MD&A and management's MD&A preparation method; plans the engagement; considers materiality; considers relevant portions of the entity's internal control; considers subsequent events; and obtains appropriate written representations from management. The misstatement of an individual assertion is material if the magnitude of the misstatement (individually or aggregated) is such that a reasonable person would be influenced by its correction. A practitioner also considers whether management (and any assistants) has appropriate knowledge of rules and regulations of the SEC to prepare MD&A. Because the objective of an audit of financial statements is different from that of an examination of MD&A, additional procedures typically are performed in an examination of MD&A.

1. **Examination** The CPA obtains sufficient evidence, including testing completeness, and forms an opinion consistent with examination objectives. The CPA considers the results of financial statement audits for the periods covered by MD&A, including the possible impact on the examination engagement scope of a modified audit report.
2. **Review** Procedures generally are limited to inquiries and analytics concerning factors that have a material effect on financial condition, results of operations, and cash flows. The CPA also forms a conclusion consistent with review objectives.

Control Risk

After obtaining an understanding of the entity's internal controls over preparation of the MD&A section, the CPA assesses control risk for the content in the MD&A. Control risk may be assessed at the maximum level (the greatest probability that a material misstatement could occur in an assertion and will not be prevented or detected in a timely manner) if the CPA believes controls are ineffective.

Review Performance

The CPA develops an overall strategy for analytics and inquiries. The CPA considers factors such as matters affecting the entity's industry; matters relating to the entity's business; the types of relevant information that management reports to external analysts; the extent of management's knowledge of, and experience with, SEC criteria for MD&A; if the entity is a nonpublic entity, the intended use of MD&A; matters identified during other engagements; and, the nature of complex or subjective matters that may require special skill or knowledge.

Reports

A report on an examination or review of MD&A includes the date of the completion of the CPA's procedures, which should not precede the date of the audit (or review) report on the latest historical financial statements covered by the MD&A. An entity should not name the practitioner in a client-prepared document as having examined or reviewed MD&A unless the MD&A presentation and related practitioner's report and the related financial statements and auditor's (or accountant's review) report are included in the document (or, in the case of a public entity, incorporated by reference to such information filed with a regulatory agency). The practitioner's report on an examination or review of MD&A should include the following:

1. **Both:** a title that includes the word independent
2. **Both (introductory paragraph):** an identification of the MD&A presentation, including the period covered
3. **Responsibility (introductory paragraph contd.)**
 - a. **Both:** a statement that management is responsible for the preparation of the MD&A pursuant to the rules and regulations adopted by the SEC
 - b. **Examination only:** and a statement that the practitioner's responsibility is to express an opinion on the presentation based on his or her examination
4. **Both (introductory paragraph concluded):** a reference to the audit report on the related financial statements, and, if the report was other than a "standard" report, the substantive reasons
5. **Both (scope paragraph):** a statement that the examination or review was conducted in accordance with attestation standards established by the AICPA
6. **Scope (scope paragraph contd.)**
 - a. **Examination only:** a description of the scope of an examination of MD&A
 - b. **Review only:** a description of the procedures for a review of MD&A
7. **Nature of engagement (scope paragraph concluded)**
 - a. **Examination only:** a statement that the practitioner believes the examination provides a reasonable basis for his or her opinion
 - b. **Review only:** a statement that a review of MD&A is substantially less in scope than an examination, the objective of which is an expression of opinion regarding the MD&A presentation, and accordingly, no such opinion is expressed
8. **Both: Explanation of MD&A (explanatory paragraph)**
 - a. The preparation of MD&A requires management to interpret the criteria, make determinations as to the relevancy of information to be included, and make estimates and assumptions that affect reported information
 - b. Actual results in the future may differ materially from management's present assessment of information regarding the estimated future impact of transactions and events that have occurred or are expected to occur, expected sources of liquidity and capital resources, operating trends, commitments, and uncertainties
 - c. If the entity is a nonpublic entity, a statement that although the entity is not subject to the rules and regulations of the SEC, the MD&A presentation is intended to be a presentation in accordance with the rules and regulations adopted by the SEC
9. **Examination only (opinion paragraph):** the practitioner's opinion on whether:
 - a. The presentation includes, in all material respects, the required elements of the rules and regulations adopted by the SEC

- b. The historical financial amounts have been accurately derived, in all material respects, from the entity's financial statements
 - c. The underlying information, determinations, estimates, and assumptions of the entity provide a reasonable basis for the disclosures contained therein
- 10. Review only (concluding—negative assurance—paragraph):** a statement about whether any information came to the practitioner's attention that caused him or her to believe that:
- a. The MD&A presentation does not include, in all material respects, the required elements of the rules and regulations adopted by the SEC
 - b. The historical financial amounts included therein have not been accurately derived, in all material respects, from the entity's financial statements
 - c. The underlying information, determinations, estimates, and assumptions of the entity do not provide a reasonable basis for the disclosures contained therein
- 11. Review only (restricted use paragraph):** if the entity is a public entity or a nonpublic entity that is making or has made an offering of securities and it appears that the securities may subsequently be registered or subject to a filing with the SEC or other regulatory agency, a statement of restrictions on the use of the report to specified parties, because it is not intended to be filed with the SEC as a report under the 1933 Act or the 1934 Act
- 12. Both:** the manual or printed signature of the practitioner's firm
- 13. Both:** the date of the report

Review Presentation

In order for a CPA to issue a report on a review of MD&A, the financial statements for the periods covered by MD&A and the related auditor's or practitioner's report(s) should accompany MD&A (or be incorporated by reference to information filed with a regulatory agency). There are additional requirements in the following circumstances:

- 1. Interim Periods** The comparative financial statements for the most recent annual period and the related MD&A should accompany the interim MD&A (or be incorporated by reference). Generally, this requirement is satisfied by a public entity that has filed its annual financial statements and MD&A in its annual Form 10-K.
- 2. Nonpublic Entity** The MD&A should include a statement that it was prepared using SEC criteria or a separate written assertion should accompany MD&A.

Reporting on Controls at a Service Organization

Guidance

Service Organization Controls (SOC) are a series of accounting standards that measure the control of financial information for a service organization. SOC 1 reports are examination engagements prepared in accordance with SSAE No. 16, and are undertaken by a service auditor to report on controls at an organization that provides services to user entities when those controls are likely to be relevant to user entities' internal control over financial reporting. For reports that are not specifically focused on internal controls over financial reporting, SOC 2 and SOC 3 reports should be used, which focus on controls at a service organization relevant to

1. **Security** The system is protected against unauthorized access
2. **Availability** The system is available for operation and use as committed and agreed
3. **Processing Integrity** The system processing is complete, accurate, timely, and authorized
4. **Confidentiality** Information classified as confidential is protected as committed or agreed
5. **Privacy** Personal information is collected, used, retained, disclosed, and destroyed in conformity with the commitments in the entity's privacy notice and with criteria set forth in the AICPA's generally accepted privacy principles

Objective

The objectives of the service auditor are to:

1. Obtain reasonable assurance about whether, in all material respects, based on suitable criteria
 - a. Management's description of the service organization's system fairly presents the system that was designed and implemented throughout the specified period (or in the case of a type 1 report, as of a specified date)
 - b. The controls related to the control objectives stated in management's description of the service organization's system were suitably designed throughout the specified period (or in the case of a type 1 report, as of a specified date)
 - c. When included in the scope of the engagement, the controls operated effectively to provide reasonable assurance that the control objectives stated in management's description of the service organization's system were achieved throughout the specified period
2. Report on the preceding matters in accordance with the service auditor's findings

Engagement Acceptance

1. **Auditor Responsibilities** The service auditor has the capabilities and competence to perform the engagement. The service auditor should obtain an understanding of the service organization's system, including controls that are included in the scope of the engagement. The service auditor's preliminary knowledge of the engagement circumstances indicates that the
 - a. Criteria to be used will be suitable and available to the intended user entities and their auditors
 - b. Service auditor will have access to sufficient appropriate evidence to the extent necessary
 - c. Scope of the engagement and management's description of the service organization's system will not be so limited that they are unlikely to be useful to user entities and their auditors.

2. **Management's Responsibilities** Management agrees to the terms of the engagement by acknowledging and accepting its responsibility in that they have used suitable criteria in:
 - a. Preparing its description of the service organization's system
 - b. Evaluating whether controls were suitably designed to achieve the control objectives stated in the description
 - c. Evaluating whether controls operated effectively throughout the specified period to achieve the control objectives stated in the description of the service organization's system
3. **Materiality** In an engagement to report on controls at a service organization, the concept of materiality relates to the information being reported on, not the financial statements of user entities.
4. **Internal Audit** If the work of the internal audit function has been used, the service auditor should not make reference to that work in the service auditor's *opinion*; however, in the case of a type 2 report, if the work of the internal audit function has been used in performing tests of controls, that part of the service auditor's report that describes the service auditor's tests of controls and results thereof should include a description of the internal auditor's work and of the service auditor's procedures with respect to that work.

Report Components

1. **Date** The service auditor should date the service auditor's report no earlier than the date on which the service auditor has obtained sufficient appropriate evidence to support the service auditor's opinion.
2. **Time Frame** A Type 1 Report is a report on management's description of a service organization's system and the suitability of the design of controls for a specific date. A Type 2 Report expands on the Type 1 Report and includes the operating effectiveness of controls as well as the suitability of their design for a period of time.
3. **Elements** A Type 1 Report will include:
 - a. A description of the service organization's system prepared by management
 - b. A written assertion by management about whether, in all material respects, and based on suitable criteria:
 - (1) The description of the service organization's system fairly presents the design and implementation of the system as of a specified period/date.
 - (2) The controls related to the control objectives stated in management's description were suitably designed to achieve those control objectives as of the specified period/date.
 - (3) For Type 2 Reports only, the controls that were tested were operating effectively to provide reasonable, but not absolute, assurance that the control objectives were achieved during the period specified.
 - c. A service auditor's opinion on management's assertions.

- 4. Modified Opinion** The service auditor's opinion should be modified and the service auditor's report should contain a clear description of all the reasons for the modification, if the service auditor concludes that:
- Management's description of the service organization's system is not fairly presented, in all material respects
 - The controls are not suitably designed to provide reasonable assurance that the control objectives stated in management's description of the service organization's system would be achieved if the controls operated as described
 - In the case of a type 2 report, the controls did not operate effectively throughout the specified period to achieve the related control objectives stated in management's description of the service organization's system
 - The service auditor is unable to obtain sufficient appropriate evidence
- 5. Disclaimer** If the service auditor plans to disclaim an opinion because of the inability to obtain sufficient appropriate evidence, and, based on the limited procedures performed, has concluded that:
- Certain aspects of management's description of the service organization's system are not fairly presented, in all material respects
 - Certain controls were not suitably designed to provide reasonable assurance that the control objectives stated in management's description of the service organization's system would be achieved if the controls operated as described
 - In the case of a type 2 report, certain controls did not operate effectively throughout the specified period to achieve the related control objectives stated in management's description of the service organization's system

The service auditor should not identify the procedures that were performed nor include statements describing the characteristics of a service auditor's engagement in the service auditor's report; to do so might overshadow the disclaimer.

Supplemental Material

Overview of Attestation Standards—Representation Letter from the Responsible Party

- (1) When the client is the responsible party, the following are examples of matters that might appear in a representation letter:
- A statement acknowledging responsibility for the subject matter and, when applicable, the assertion
 - A statement acknowledging responsibility for selecting the criteria, where applicable
 - A statement acknowledging responsibility for determining that such criteria are appropriate for its purposes, where the responsible party is the client
 - The assertion about the subject matter based on the criteria selected
 - A statement that all known matters contradicting the assertion and any communication from regulatory agencies affecting the subject matter or the assertion have been disclosed to the practitioner
 - Availability of all records relevant to the subject matter
 - A statement that any known events subsequent to the period (or point in time) of the subject matter being reported on that would have a material effect on the subject matter (or, if applicable, the assertion) have been disclosed to the practitioner
 - Other matters as the practitioner deems appropriate
- (2) When the client is **not** the responsible party, the following are examples of matters that might appear in a representation letter:

- A statement that any known events subsequent to the period (or point in time) of the subject matter being reported on that would have a material effect on the subject matter (or, if applicable, the assertion) have been disclosed to the practitioner
- A statement acknowledging the client's responsibility for selecting the criteria, where applicable
- A statement acknowledging the client's responsibility for determining that such criteria are appropriate for its purposes
- Other matters as the practitioner deems appropriate

General Attestation Standards—Adequate Knowledge of the Subject Matter

The CPA may use specialists, provided that the CPA has enough knowledge of the subject matter:

- (1) To communicate to the specialist the objectives of the work
- (2) To evaluate the specialist's work to determine if the objectives were achieved.

General Standards—Suitability and Availability of Criteria

- (1) Criteria are the standards or benchmarks used to measure and present the subject matter and against which the practitioner evaluates the subject matter. Suitable criteria must have each of the following attributes:
 - (a) Objectivity: Criteria should be free from bias.
 - (b) Measurability: Criteria should permit reasonably consistent measurements, qualitative or quantitative, of subject matter.
 - (c) Completeness: Criteria should be sufficiently complete so that those relevant factors that would alter a conclusion about subject matter are not omitted.
 - (d) Relevance: Criteria should be relevant to the subject matter.
- (2) The criteria should be available to users in one or more of the following ways:
 - Available publicly
 - Available to all users through inclusion in a clear manner in the presentation of the subject matter or in the assertion
 - Available to all users through inclusion in a clear manner in the practitioner's report
 - Well understood by most users, although not formally available (for example, "The distance between points A and B is twenty feet;" the criterion of distance measured in feet is considered to be well understood)
 - Available only to specified parties; for example, terms of a contract or criteria issued by an industry association that are available only to those in the industry

Fieldwork Standards—Planning and Supervision

Planning factors include:

- The criteria to be used
- Preliminary judgments about attestation risk and materiality for attest purposes
- The nature of the subject matter or the items within the assertion that are likely to require revision or adjustment
- Conditions that may require extension or modification of attest procedures
- The nature of the report expected to be issued

Fieldwork Standards—Obtaining Sufficient Evidence

Presumptions about evidence that are generally true:

Evidence obtained from independent sources outside an entity provides greater assurance about the subject matter or the assertion than evidence secured solely from within the entity.

- Information obtained from the independent attester's direct personal knowledge (such as through physical examination, observation, computation, operating tests, or inspection) is more persuasive than information obtained indirectly.
- The more effective the controls over the subject matter, the more assurance they provide about the subject matter or the assertion

Reporting Standards—Identification of Subject Matter or Assertion

If the attestation is on an assertion, the assertion must accompany, or be restated within, the CPA's report. The statement of the character of an attest engagement designed to result in a general-use report (i.e., an examination or a review) includes two elements:

- (1) A description of the nature and scope of the work performed
- (2) A reference to the professional (AICPA) standards governing the engagement.

Reporting Standards—Conclusion

- (1) **Misstatements:** If deviations from the criteria or material misstatements exist, the practitioner should modify the report, directly expressing an opinion on the subject matter, rather than the assertion.
- (2) **Materiality:** The CPA should consider the idea of materiality in applying this standard. Materiality is determined by the relative size of a misstated or omitted fact, rather than by its absolute amount. Materiality considerations include whether a reasonable person relying on the presentation of assertions would be influenced by the inclusion or correction of an individual assertion.

Reporting Standards—Disclosure of Reservations

- (1) **Unresolved Problem** Reservations about the engagement refers to any unresolved problem the CPA had in complying with the standards and guidance applicable to attestation services or procedures agreed to by the specified parties. An unqualified conclusion should not be expressed if the CPA has been unable to apply all the procedures considered necessary to comply with attestation standards.
- (2) **Scope Restrictions** Restrictions on the scope of the engagement, whether imposed by the client or by other circumstances, may require the CPA to qualify the report, to disclaim any assurance, or to withdraw from the engagement. When restrictions that significantly limit the scope of the engagement are imposed by the client, the CPA generally should either withdraw from the engagement or disclaim any assurance on the subject matter, assertions, or presentation. An incomplete review engagement requires the CPA to withdraw.

Reporting Standards—Restrictions

When a report is restricted as to use, it contains a separate final paragraph that includes the following types of statements:

- (1) Indicate the report is intended solely for the use of the specified parties
- (2) Identify the specified parties
- (3) Indicate the report is not intended to be, and should not be, used by anyone other than the specified parties.

Agreed-Upon Procedures—Agreement on and Sufficiency of Procedures

- (1) If the practitioner is not able to communicate directly with all of the specified parties, the practitioner may satisfy the requirements for agreement on and sufficiency of procedures by applying any one or more of the following or similar procedures:
 - Compare the procedures to be applied to written requirements of the specified parties.
 - Discuss the procedures to be applied with appropriate representatives of the specified parties involved.
 - Review relevant contracts with or correspondence from the specified parties.
- (2) The practitioner should not agree to perform procedures that are overly subjective and thus possibly open to varying interpretations.
 - (a) Examples of appropriate procedures:
 - Execution of a sampling application after agreeing on relevant parameters
 - Inspection of specified documents evidencing certain types of transactions or detailed attributes thereof
 - Confirmation of specific information with third parties
 - Comparison of documents, schedules, or analyses with certain specified attributes
 - Performance of specific procedures on work performed by others (including the work of internal auditors)
 - Performance of mathematical computations
 - (b) Examples of inappropriate procedures:
 - Mere reading of the work performed by others solely to describe their findings
 - Evaluating the competency or objectivity of another party
 - Obtaining an understanding about a particular subject
 - Interpreting documents outside the scope of the practitioner's professional expertise

Agreed-Upon Procedures—Involvement of a Specialist

It may be appropriate to involve a specialist to assist the practitioner in the performance of one or more procedures. The following are examples:

- An attorney might provide assistance concerning the interpretation of legal terminology involving laws, regulations, rules, contracts, or grants.
- A medical specialist might provide assistance in understanding the characteristics of diagnosis codes documented in patient medical records.
- An environmental engineer might provide assistance in interpreting environmental remedial action regulatory directives that may affect the agreed-upon procedures applied to an environmental liabilities account in a financial statement.
- A geologist might provide assistance in distinguishing between varying physical characteristics of a generic minerals group related to information to which the agreed-upon procedures are applied.

Agreed-Upon Procedures—Use of Internal Auditors and Other Personnel

- (1) A practitioner may agree to perform procedures on information documented in the working papers of internal auditors. For example, the practitioner may agree to:
 - Repeat all or some of the procedures.

- Determine whether the internal auditors' working papers contain documentation of procedures performed and whether the findings documented in the working papers are presented in a report by the internal auditors.

(2) However, it is **not** appropriate for the practitioner to:

- Agree to merely read the internal auditors' report solely to describe or repeat their findings.
- Take responsibility for all or a portion of any procedures performed by internal auditors by reporting those findings as the practitioner's own.
- Report in any manner that implies shared responsibility for the procedures with the internal auditors.

Examination of Internal Control Over Financial Reporting—Definitions

- (1) **Control Objective:** The aim or purpose of specified controls. Control objectives ordinarily address the risks that the controls are intended to mitigate. In the context of internal control, a control objective generally relates to a relevant assertion for a significant account or disclosure and addresses the risk that the controls in a specific area will not provide reasonable assurance that a misstatement or omission in that relevant assertion is prevented, or detected and corrected on a timely basis.
- (2) **Deficiency:** A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis.
 - (a) A deficiency in design exists when
 - A control necessary to meet the control objective is missing or
 - An existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met.
 - (b) A deficiency in operation exists when a properly designed control does not operate as designed, or when the person performing the control does not possess the necessary authority or competence to perform the control effectively.
- (3) **Detective Control:** A control that has the objective of detecting and correcting errors or fraud that have already occurred that could result in a misstatement of the financial statements.
- (4) **Financial Statements and Related Disclosures:** An entity's financial statements and notes to the financial statements as presented in accordance with the applicable financial reporting framework. References to financial statements and related disclosures do not extend to the preparation of other financial information presented outside an entity's basic financial statements and notes.
- (5) **Internal Control Over Financial Reporting:** A process effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance regarding the preparation of reliable financial statements for external purposes in accordance with the applicable financial reporting framework and includes those policies and procedures that
 - (a) Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of an entity
 - (b) Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with the applicable financial reporting framework, and that receipts and expenditures of an entity are being made only in accordance with authorizations of management and those charged with governance
 - (c) Provide reasonable assurance regarding prevention, or timely detection and correction of unauthorized acquisition, use, or disposition of an entity's assets that could have a material effect on the financial statements

- (d) Internal control has inherent limitations. Internal control is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control also can be circumvented by collusion or improper management override.
- (6) **Material Weakness:** A deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility (per the FASB's definition regarding accounting for contingencies) that a material misstatement of an entity's financial statements will not be prevented, or detected and corrected on a timely basis.
- (7) **Preventive Control:** A control that has the objective of preventing errors or fraud that could result in a misstatement of the financial statements.
- (8) **Relevant Assertion:** A financial statement assertion that has a reasonable possibility of containing a misstatement or misstatements that would cause the financial statements to be materially misstated. The determination of whether an assertion is a relevant assertion is made without regard to the effect of controls.
- (9) **Significant Account or Disclosure:** An account balance or disclosure that has a reasonable possibility that it could contain a misstatement that, individually or when aggregated with others, has a material effect on the financial statements, considering the risks of both overstatement and understatement. The determination of whether an account balance or disclosure is a significant account or disclosure is made without regard to the effect of controls.
- (10) **Significant Deficiency:** A deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.
- (11) **Engagement Objective:** The auditor's objective is to form an opinion on the effectiveness of an entity's internal control as of a point in time and taken as a whole. To express an opinion as of a point in time, the auditor should obtain evidence that internal control has operated effectively for a sufficient period of time which may be less than the period covered by the company's financial statements. To express an opinion on internal control taken as a whole, the auditor should obtain evidence about the effectiveness of selected controls over all relevant assertions. This involves testing the design and operating effectiveness of controls that in most cases would not be required if only expressing an opinion on the financial statements.

Exhibit 14.8 - Summary of Statements on Standards for Attestation Engagements (SSAE)

<p>Statements on Standards for Attestation Engagements (SSAE) (Covers Examination, Review or Compilation of anything other than Historical Financial Statements)</p>	<p>Examination</p> <p>Prospective Financial Statements (Forecast/Projection)</p> <p>Pro-Forma Financial Statements</p> <p>Compliance with specified laws, rules or regulations</p> <p>Management Discussion and Analysis</p> <p>Internal Controls at Service Organization</p>	Opinion is Expressed	Independence is required
	<p>Review</p> <p>Pro-Forma Financial Statements</p> <p>Management Discussion and Analysis</p>	Negative Assurance (Not aware of any material modifications)	Independence is required
	<p>Agreed-upon Procedures</p>	No Opinion is expressed	Independence is required

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